



## ***Guanxi* Dynamics and Entrepreneurial Firm Creation and Development in China**

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**ABSTRACT** *Guanxi* networks are critical for achieving entrepreneurial success in China. Informed by the literatures on network-based entrepreneurship and *guanxi*, this study used a multiple-case method to examine the development of Chinese entrepreneurs' *guanxi* networks in the entrepreneurial process. Data induction based on within- and cross-case analyses of six entrepreneurial firms revealed three major findings. First, *guanxi* network dynamics in terms of network structure, governance mechanisms, and network content change systematically across the stages of the entrepreneurship process. Second, the usefulness of *guanxi* ties (such as family, business associates, or government officials) is contingent on the stage of the entrepreneurial process as well as on industrial-level factors. Third, in knowledge-intensive industries, cultivating and maintaining *guanxi* can be achieved through knowledge and information exchange rather than traditional gift-giving or favours. The overall conclusion is that *guanxi* is still of paramount importance for Chinese entrepreneurs in the midst of China's transformation from a centrally planned to a socialist market economy. We propose a stage model of *guanxi* network development in the entrepreneurial process and discuss implications for future research.

**KEYWORDS** China, entrepreneurial processes, firm creation, firm development, *guanxi*

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### **INTRODUCTION**

In the transition from a centrally planned to a socialist market economy, China has experienced the emergence and prosperity of entrepreneurial activities in the last two decades (Zapalska & Edwards, 2001). The private sector is now playing an important role in driving China's economic growth (Pistrui, Huang, Oksoy, Zhao, & Welsch, 2001; Tsui, Bian, & Cheng, 2006). Despite the Chinese government's focus on expanding the private sector, researchers (e.g., Peng, 2000; Xin & Pearce, 1996) have observed that entrepreneurs still face considerable barriers, such as a volatile institutional environment, limited access to critical resources, and lack of governmental support. Hence, it is important to understand how Chinese

entrepreneurs overcome environmental barriers and resource deficiency in the venture creation and development process.

Previous research (e.g., Guthrie, 1998; Xin & Pearce, 1996) has shown that one of the most important ways Chinese entrepreneurs overcome obstacles to venture formulation is through *guanxi*, or personal connections. In addition, researchers have examined the influence of *guanxi* on entrepreneurs' growth intentions (Lau & Busenitz, 2001), strategic development in response to the institutional environment (Ahlstrom & Bruton, 2002), venture capitalists' investment decisions (Batjargal & Liu, 2004), and entrepreneurial firm performance (Batjargal, 2007).

Although these studies suggest that *guanxi* nurtures China's entrepreneurial economy, the reliance on cross-sectional data prevents the development of a dynamic understanding of both *guanxi* and entrepreneurship. In fact, neither *guanxi* (Yang, 2002), nor entrepreneurship (Baron, 2006) are static, unchanging entities. In a recent study conducted in a Chinese context, Fu, Tsui, and Dess (2006) speculated that the usefulness of *guanxi* in knowledge management would vary at different developmental stages of high-tech entrepreneurial firms.

The paucity of research on *guanxi* dynamics and the entrepreneurial process in China leads to two general questions that guide the present investigation. First, how do entrepreneurs develop and use *guanxi* in order to support entrepreneurial firm creation and development in China? Second, do entrepreneurs' *guanxi* networks differ systematically across stages of the entrepreneurial process? To address these questions, this exploratory study uses a qualitative, multiple-case study method. We assess empirical data on the components of *guanxi* networks relative to the network-based entrepreneurship and *guanxi* literatures, leading to an initial understanding of *guanxi* network dynamics in the entrepreneurial process in China.

The current research contributes to the literature on *guanxi* and Chinese entrepreneurship by: (i) providing empirical insights into characteristics of *guanxi* networks at different stages of the entrepreneurial process; (ii) uncovering contingency factors that may lead to variations in the usefulness of *guanxi* ties and in ways of initiating and maintaining *guanxi* in an entrepreneurial context; and (iii) explaining why *guanxi* remains important in the midst of China's economic reform and construction of a legal infrastructure.

The present study represents what Whetten (2009: 30) calls 'the cross-context approach to fostering context sensitive theorizing'. By contextualizing existing concepts and theories in explaining unique features of *guanxi* in the entrepreneurial process in China, we 'make the novel appear familiar' to scholars who are not familiar with Chinese culture and management practices (Whetten, 2009: 47). Also, by theorizing the findings from the case analyses, we are able to develop new insights into the familiar topics such as network-based entrepreneurship and social networks, hence making contributions to general theory development (Whetten, 2009).

The paper begins with an introduction to network-based entrepreneurship and the literature on *guanxi*. We then explain the research design and case study method. The remainder of the paper reports the key findings of the case analysis and offers our proposed stage model of *guanxi* network development in the entrepreneurial process. Finally, we provide discussions and implications for future research at the end.

## THEORETICAL BACKGROUND

### Network Approach to Entrepreneurship

Based on Stevenson, Roberts, and Grousbeck's (1989) work, Stevenson and Jarillo (1990: 23) define entrepreneurship as 'a process by which individuals – either on their own or inside organizations – pursue opportunities without regard to the resources they currently control'. The process perspective of entrepreneurship focuses on studying entrepreneurial behaviours (Stevenson & Jarillo, 1990), and according to Gartner (1985: 699–700), there are six common behaviours in the entrepreneurial process, such as 'locates a business opportunity', 'accumulates resources', 'markets products and services', 'produces the product', 'builds an organization', and 'responds to government and society'. From a process perspective, 'entrepreneurship should be viewed as a continuous, evolving process rather than a single event or a series of unrelated events' (Baron, 2006: 19).

Aldrich and Zimmer (1986) were among the first who proposed the network approach to entrepreneurship. Drawing on previous studies of networks and entrepreneurship, Larson and Starr (1993) developed a network model that theorizes how entrepreneurs' network ties are developed in the organization formation process. They argue that the network approach provides better explanations of venture creation phenomena by simultaneously capturing the unfolding entrepreneurial process and the evolving social relationships between entrepreneurs and their associated others (Larson & Starr, 1993).

Based on a review of primarily Western network-based entrepreneurship research, Hoang and Antoncic (2003) identified content, governance mechanisms, and social structure as three major components of entrepreneurial networks. The first component, content, refers to resources that are delivered by entrepreneurs' interpersonal relationships (Hoang & Antoncic, 2003). The second component, governance mechanisms, refers to mechanisms that support network exchanges (Hoang & Antoncic, 2003). The third component, social structure, is defined as 'the pattern of direct and indirect ties between actors' (Hoang & Antoncic, 2003: 170) and can be measured by variables such as network size, the strength of ties, and network configurations. Specifically, network size is indicated by the degree to which an entrepreneurial network can be enlarged overtime (Greve & Salaff, 2003). The strength of a social tie, according to Granovetter (1973: 1361), 'is a

(probably linear) combination of the amount of time, the emotional intensity, the intimacy (mutual confiding), and the reciprocal services'. In terms of network configurations, a closure structure refers to the condition under which actors are well-connected to each other (Coleman, 1988), and a sparse network is characterized by structural holes or the lack of connection between actors in a social network (Burt, 1992).

### ***Guanxi* and Its Cultural Roots in Confucian Social Theory**

Based on the definition of *guanxi* in previous research (Chen & Chen, 2004; Jacobs, 1979; Tsui & Farh, 1997; Yang, 1994) and the concept of 'group identification' in Yeung and Tung's (1996: 61) work, we broadly define *guanxi* as a dyadic interpersonal relationship ascribed to or achieved by an individual. Following this conceptualization, a *guanxi* web (*wang*) refers to an aggregation of *guanxi* ties possessed by an individual. We agree with Tsui and Farh (1997) and other scholars (Jacobs, 1979; Yang, 1994) that *guanxi*, in essence, is a particularistic personal relationship between two individuals. Hence, it is the concept of *guanxi* webs, not *guanxi*, that is comparable with the Western social network construct.

*Guanxi* is a natural manifestation of Confucianism, the underlying philosophy that is the fabric of Chinese society. Confucian social theory suggests that family is the basic social unit and kinship is the most important social relation to an individual (Fei, 1947/1992; King, 1991; Tsui & Farh, 1997). Family ties are characterized by unconditional loyalty and involve social obligations that are not based on reciprocity (Tsui & Farh, 1997). However, people cannot solely rely on family in dealing with everyday life, and therefore, *guanxi* serves as a mechanism by which 'quasifamilial' relations can be created to cultivate trust among non-kin (Bell, 2004: 180). Researchers (e.g., Fei, 1947/1992; King, 1991; Yang, 1994) observe that family is an elastic concept in Chinese culture and can refer to any people one wants to include. Hence, *guanxi* ties with non-kin can be viewed as an extension of *guanxi* ties inherent in family members (Bell, 2004); and one may expect that *guanxi* webs, like 'ripples . . . spreading out from the center', can expand infinitely (Fei, 1947/1992: 65).

### ***Guanxi* and Entrepreneurship in China**

In the case of Chinese entrepreneurship, Chu (1996) argues that the network approach is particularly appropriate due to the relational nature of the Chinese culture. Indeed, researchers (e.g., Luo, 2000; Tsui & Farh, 1997; Yang, 1994) have observed the pervasiveness and significance of *guanxi* in doing business in China. Previous studies (e.g., Batjargal, 2007; Batjargal & Liu, 2004; Carlisle & Flynn, 2005; Wu & Leung, 2005) have shown that there is a significant association between entrepreneurs' *guanxi* ties and entrepreneurial outcomes in China.

These prior studies have enriched our understanding of network-based entrepreneurship in China. However, most have conceptualized entrepreneurship and *guanxi* networks as static entities. The dynamic nature of *guanxi* and entrepreneurship highlights the importance of process-oriented research on *guanxi* network development in the venture creation and development processes. Although not specifically focusing on the entrepreneurial context, Chen and Chen (2004) propose a process model in which the development of a dyadic *guanxi* tie goes through three major steps – initiating, building, and using *guanxi*. Informed by the literature on *guanxi*, social network, and network-based entrepreneurship, we conducted an exploratory, multiple-case study to deepen our understanding of *guanxi* dynamics in the entrepreneurial process in China.

## METHOD

### Research Design

In the present study, we use a qualitative and inductive multiple-case study approach to our inquiry. Researchers (e.g., Elsbach & Kramer, 2003; Lee, 1999) suggest that qualitative research designs are more appropriate for studying evolutionary phenomena. The sampling strategy follows Yin's (1984) suggestion that case selection should generate predictions of both similar and contrary results. The preponderance of previous Chinese entrepreneurship research was conducted on high-tech firms. However, many Chinese entrepreneurial firms are in low-tech, less knowledge-intensive industrial sectors, such as manufacturing (Gao, Cheng, Li, & Jiang, 2008). Therefore, it is theoretically important to examine entrepreneurial firms from both knowledge-intensive and less knowledge-intensive industrial sectors.

Consistent with Eisenhardt's (1989) recommendation of four to ten cases for inductive research, six exemplar entrepreneurial firms were selected. Four of them were from less knowledge-intensive sectors (automation equipment manufacturing, plastic product manufacturing, entertainment, and energy) and the other two were from knowledge-intensive sectors (internet and consulting). Using this sampling strategy, we could examine: (i) whether similar patterns would emerge from case studies of firms in the less knowledge-intensive sectors; and (ii) if so, whether these patterns are similar to or different from those of firms in knowledge-intensive sectors.

In order to ensure a more valid comparison, all participating entrepreneurial firms had gone through three entrepreneurial stages based on Kazanjian's (1988) stage model of entrepreneurship: firm creation, early firm growth, and later firm growth. The firm creation stage involves pre-launch idea generation, opportunity identification, resource acquisition, and actual launch of a new venture. The early growth stage is marked by the initial market acceptance of the product or

service introduced by the entrepreneurial venture; and the later growth stage features steady growth of the emerging firm's sales/market share. In accordance with previous exploratory, inductive research (e.g., Graebner & Eisenhardt, 2004; Siu & Bao, 2008), the participant entrepreneurial firms were selected for their geographic diversity and their location in active entrepreneurial areas in China (Gao et al., 2008; Zhang & Yang, 2006). Among the six participating firms, two are located in Beijing, one in Shanghai, one in Hangzhou, Zhejiang Province, and two in Chongqing. Although these entrepreneurial firms are of varying sizes (ranging from seven to 1,100 employees), it is not uncommon to study diverse firms in a study of this kind (e.g., Fu et al., 2006; Gilbert, 2005; Graebner & Eisenhardt, 2004). The cases were selected in an exploratory effort to gain an initial understanding of the evolution of entrepreneurs' *guanxi* networks and to propose a theoretical model that could capture this dynamic process.

### Data Collection

The primary data source of the present study was in-depth personal interviews with entrepreneurs and their co-founders, following up with emails and phone calls if clarification was needed. These informants are considered appropriate because of their direct involvement in the venturing process and their intimate knowledge of their *guanxi* networks. In addition, we examined secondary data, including company websites and brochures, in order to gain an understanding of the company's history, scope of businesses, and areas of specialization.

The Chinese author of this study conducted eleven in-depth, semistructured interviews with the entrepreneurs and, in five cases, their co-founders between Fall 2007 and Spring 2009. The interviews were about 90–120 minutes in length and were conducted in Mandarin Chinese because researchers (Siu & Bao, 2008) suggest that the use of the native language could allow participants to express ideas freely and accurately. After the assurance of confidentiality, the entrepreneurs were initially asked to provide demographic and company information. Based on the categorization of entrepreneurial stages we provided, entrepreneurs were also asked to indicate the current stage of their entrepreneurial firms and: (i) to indicate whether *guanxi* ties were established at different stages of the entrepreneurial process; and (ii) if so, to specify dominant *guanxi* ties and major *guanxi* associates at each stage. As all of the entrepreneurs indicated the existence of *guanxi* ties in the entrepreneurial process, we then asked them to further elaborate on (iii) the specific network benefits generated by dominant *guanxi* ties at each entrepreneurial stage; (iv) the specific methods used in cultivating and maintaining *guanxi* ties; and (v) the overall importance of *guanxi* for firm creation and development in China. Data collection proceeded until we reached 'theoretical saturation' or incremental learning from the data was minimal (Eisenhardt, 1989: 545).

## Data Analysis

Because identifying specific Chinese words or phrases describing *guanxi* mechanisms and dynamics requires proficiency in the Chinese language and an indigenous understanding of the Chinese culture, the Chinese author of the present study analysed and coded the qualitative data based on the Chinese transcripts for each individual case. Using a single analyst in the case study method is not uncommon. Previous examples can be found in high-quality inductive studies, such as Gilbert (2005) and Graebner (2004).

Data analysis in this study closely followed two major steps typical in inductive multi-case research (e.g., Graebner, 2004; Graebner & Eisenhardt, 2004; Mauer & Ebers, 2006): building individual cases and then comparing across cases to construct a conceptual framework. The Chinese author built individual case studies by synthesizing the qualitative data from different sources for all six entrepreneurial firms (Eisenhardt, 1989). The Chinese author then used these case histories for within- and cross-case analyses.

The within-case analysis focused on applying existing theories and concepts in describing the features of *guanxi* dynamics. For each individual case, the Chinese author content-analysed the qualitative data along three important dimensions of network dynamics as suggested by Hoang and Antoncic (2003): social structure, content, and governance mechanisms. The coding process was guided by the existing literature on *guanxi* and social networks.

First, the Chinese author coded qualitative data involving ‘the major *guanxi* associates and the types of *guanxi* ties established in the entrepreneurial process’ according to characteristics of structural variables (network size, the nature and strength of ties, and network configurations) of *guanxi* networks in each entrepreneurial stage. Specifically, she coded: (i) the size of a certain *guanxi* network in each stage as small, large, or medium; (ii) the nature of compositional ties of a *guanxi* network as mainly composed either of kin or non-kin members and as ‘expressive’ (affection-based), ‘instrumental’ (economically driven), or ‘mixed’ (both expressive and instrumental) (Hwang, 1987: 949–953); (iii) the strength of compositional *guanxi* ties as either ‘strong’ or ‘weak’ (Granovetter, 1973); and (iv) the configuration of a certain *guanxi* network as possessing either a closure (Coleman, 1988) or a sparse structure (Burt, 1992).

Second, for content, the Chinese author coded the qualitative data regarding ‘the usefulness of, and major benefits generated by, *guanxi* ties in each entrepreneurial stage’ as either delivering financial capital or intangible resources or both. Third, she examined the qualitative data regarding ‘the specific methods used in cultivating and maintaining *guanxi* ties’ to identify specific Chinese words or phrases that described governance mechanisms. Finally, she compared interview excerpts that address the ‘overall importance of *guanxi* for firm creation and development’ in China (across cases) to search for similarities and differences.

The Chinese author conducted cross-case analysis after within-cases analyses were completed. Specifically, she first investigated whether similar or different themes and patterns emerged in multiple cases, and then she took into consideration differences in patterns in refining and modifying the stage model of *guanxi* network development. After the cross-case analyses were done, the Chinese author re-examined the original interviews to ensure that the conceptual model is consistent with the data.

## RESULTS

Through within- and cross-case analyses, we were able to provide some preliminary answers to the two research questions raised at the beginning of the paper. With regard to the first question, we found that as entrepreneurial processes unfolded, Chinese entrepreneurs intentionally expanded their *guanxi* webs and developed multiple layers of *guanxi* circles composed of different *guanxi* ties with different social associates. An entrepreneurial *guanxi* network started with a small, core circle of *ganqing* (affection)-based *guanxi* ties with the entrepreneurs' family members and close friends. As the entrepreneurial firm grew, this initial *guanxi* network was enlarged and included an intermediary and then a periphery circle composed, respectively, of *renqing* (reciprocity)- and *jiaoqing* (acquaintance)-based *guanxi* ties with other non-kin members to support the expanding needs and growth momentum of the new venture. With regard to the second question, we found that these *guanxi* networks differed systematically in terms of social structure, content, and governance mechanisms across stages of the entrepreneurial process. These network dynamics generated benefits that facilitate the entrepreneurial process. Table 1 summarizes the key findings of these *guanxi* dynamics in the entrepreneurial process. Detailed descriptions can be found below.

### Network Dynamics in the Entrepreneurial Process

An overall finding of the analysis is that the phrase *guanxi quan* (circle) was frequently used by all Chinese entrepreneurs to describe layers of their *guanxi* webs. Throughout the entrepreneurial process, we found that entrepreneurs intentionally expanded their *guanxi* webs and developed different *guanxi* circles in order to meet unique challenges at different developmental stages. In theorizing the development of the *guanxi* webs, we use 'core', 'intermediary', and 'periphery' to differentiate *guanxi* circles. This typology is consistent with the concentric feature of Chinese social structure described by Fei (1947/1992).

*Core guanxi circle.* During the firm creation stage, the Chinese entrepreneurs mentioned that a small, core *guanxi* circle was formed and consisted of *guanxi* ties with family members and close friends. From the structural perspective, the core

Table 1. *Guanxi* network evolution in the entrepreneurial process

	Stage 1 <i>Firm creation</i>	Stage 2 <i>Early firm growth</i>	Stage 3 <i>Later firm growth</i>
Network structural characteristics	Core circle	Intermediary circle	Periphery circle
Size	Small	Medium	Large and indefinitely expanding
Configuration	Closure structure	Sparse structure	Sparse structure
Major <i>guanxi</i> associates	Family members, relatives, close friends	Governmental officials, bank investors, key clients, business associates	Random, previously unknown individuals from diverse backgrounds
Nature/strength of ties	Expressive, affection-based, strong ties	Mixed (both instrumental and affection-based), strong ties	Instrumental, opportunistic, weak ties
Network mechanisms	<i>Ganqing</i> Acquiring resources without being overly burdened by payback obligations	<i>Renqing</i> Creating social obligations, exchanging gifts and favours, giving banquets, and sharing knowledge and information	<i>Jiaqing</i> Building acquaintance for future business cooperation
Network content	Initial start-up financial capital, advice, critical feedback for firm creation	Additional resources for firm growth, updated knowledge/information of business partners' needs, business routines, and practices	Fast, diverse information, potential business opportunities for keeping growth momentum

*guanxi* circle embodies a closure structure because family members and close friends are well-connected and known to each other. These *guanxi* ties are strong ties that are not economically driven, but rather are ‘expressive ties’ (Hwang, 1987: 949), which are based on ‘relatively permanent and stable social relationship[s]’ that ‘render an individual’s feeling of affection, warmth, safety, and attachment’.

The closure structure coupled with strong *guanxi* ties squarely addresses the major challenges entrepreneurs face during the firm creation stage – evaluating opportunities, assessing the availability of resources, and making the decision to start a business. In terms of network content of the core circle, strong norms generated by a closure structure (Coleman, 1988) and strong affection-based *guanxi* ties provide entrepreneurs with insights into and critical feedback on entrepreneurial ideas. Also, these structural characteristics ensure that all the information and advice entrepreneurs receive are sincere. Within this core circle, entrepreneurs conducted open, in-depth discussions with their family members and friends about the decision to start a business. As the entrepreneurs explained,

In this initial stage, you may have several business ideas in mind, but you are not sure which one or ones you can pursue. Your close friends or family members are the ones you can trust and communicate with. But communication with close friends or family members does not always guarantee that you will get support from them. For example, when I told my best friend that I wanted to start a business in the energy industry, he was the first one voting against the idea, even though now he is one of my business partners. So the purpose of communicating with your close *guanxi* ties is to make sure that you see both sides of a coin and to help you decide whether or not to start a business. (Case 02, Interview 01 – designations used to anonymously identify cases and interviews; all quotations are translated from Chinese)

Another challenge facing entrepreneurs at this stage is how to acquire initial resources. We observe that *guanxi* relationships at this stage are governed by the *ganqing* mechanism, through which acquiring resources from family members and close friends could be realized. *Ganqing* refers to the emotional feelings and affection of human beings, which can be created and accumulated through long-term social relations, such as those between parents and children, between husband and wife, or between close friends (King, 1991; Yang, 1994). Entrepreneurs mentioned that few bank investors or venture capitalists in China were willing to invest in an entrepreneurial opportunity due to the perceived low credibility of individual entrepreneurs. Hence, entrepreneurs had to draw on their personal savings and on the financial resources of their family members and/or close friends. As one entrepreneur mentioned,

When I had an idea to start my own business in plastic product manufacturing, I had to ask my relatives if they could provide me with financial support because the local bank refused to loan money to me. I had two family members who, with no hesitation, generously offered me the help so I could build up the plant, purchase equipment, and hire employees to pursue the opportunity. They did not even ask me to sign a letter to acknowledge the debt or give me a payback deadline, because we are *qinren* (family members) and these documents are completely unnecessary when we have such a strong *ganqing jichu* (base). If it was not for their support, I would not have been able to start the business at all. (Case 06, Interview 02)

Indeed, *ganqing* implies sacrificing, giving, or unconditional loyalty and obligations to relational associates with little or no expectation of repayment or material compensation (Tsui & Farh, 1997; Yang, 1994). Informed by these findings, we agree with Bell (2004) that *guanxi* ties among kinship members should not be viewed as exchange-based relations, but rather asymmetrical and non-reciprocal ones that require sharing of good fortune or resources with family members when they suffer from financial difficulties. As such, *ganqing* serves as a mechanism that allows entrepreneurs to acquire resources (both tangible and intangible) from various sources without being overly burdened by the payback obligations, hence increasing the possibility of actually creating new ventures.

*Intermediary guanxi circle.* During the early firm growth stage, we observe that Chinese entrepreneurs intentionally expanded their *guanxi* webs beyond the core circle because they could not count on their family members or close friends for all needed resources. Thus, Chinese entrepreneurs constructed intermediary *guanxi* circles to acquire additional resources. To achieve this goal, cultivating *guanxi* ties with non-kin members, especially key business associates such as business partners, investment banks, major clients, or governmental officials, became the entrepreneurs' dominant networking activities at this stage. For example, an entrepreneur who operates an internet business explains that,

Generally, using *geren* (personal) *guanxi* with close friends or family members is far from enough to grow an internet business. Since our business is mainly B2B, what matters most at this stage is the *yewu* (business) *guanxi* with major clients and business partners. Besides, unlike other businesses, *guanxi* with mass media, such as newspaper or TV channels, is of paramount importance for growing an online business. (Case 03, Interview 01)

From a network structure perspective, the intermediary circle is a sparse structure in that the business associates in this circle are unlikely to be as densely connected to each other as family members in the core circle; therefore, structural

holes exist between some *guanxi* parties. Sparse networks allow actors to have non-redundant contacts that can offer additive rather than overlapping information or resources (Burt, 1992). Through these *guanxi* ties, entrepreneurs could access additional resources that are unavailable in the core circle. Moreover, these *guanxi* associates usually have their own unique *guanxi* webs, so they serve as intermediaries or brokers. When problems cannot be solved by entrepreneurs' direct *guanxi* ties, members in the intermediary circle can refer to their own *guanxi* associates for consultation and assistance. As one entrepreneur notes, the most important function of his *guanxi* web at this stage is providing references and problem-solving:

. . . by the time I launched my business, I had to expand my initial *guanxi* circle to include more new contacts. At that time, although I had a passion for my business, I did not have all required human and financial resources to grow the firm. So I spent time searching for potential business partners who might contribute a portion of the needed resources. Also I recruited several staff members to support the daily operation of the firm . . . My firm now has achieved some initial growth . . . I further expanded my *guanxi* web to include key contacts in business associations and professional groups. If I had problems that my direct *guanxi* ties could not solve, they always referred me to their own *guanxi* ties for help. (Case 01, Interview 01)

At this stage, we observe that Chinese entrepreneurs intentionally developed *renqing* as a mechanism to channel the network activities. According to Hwang (1987), *renqing* involves less affection than *ganqing* and refers to a social debt that must be repaid in the future; it also defines social norms that guide individual behaviour in Chinese society. Consistent with this notion, in our case studies, entrepreneurs mention that *renqing* provides important criteria and modes of proper conduct when interacting with their *guanxi* associates. They cultivate and maintain *renqing*-based *guanxi* ties by constantly creating social obligations that need to be fulfilled by their *guanxi* associates in the future. As an entrepreneur explained,

In the stage of growth, it is of paramount importance to have *renqing*-based *guanxi*, especially with governmental officials in business-related bureaus . . . Even though you have done everything in a legal way in China, if you do not cultivate *renqing* with governmental officials in these bureaus, they will think you don't know *renqing shigu* (social etiquette), and they may not trust you when you need their help for certain things. Nowadays, offering *hongbao* (red envelopes with money enclosed) to governmental officials is definitely illegal, and no one would accept it. But *renqing* could be cultivated through, for example, inviting them out for banquets, offering gifts on special occasions, such as national holidays, and sending constant greetings. These social activities,

although they may look trivial, are essential for building long-lasting harmonious relationships. Through these ongoing social interactions, the governmental officials will know you and your business better, and more importantly, they know they are well respected. Over time, a certain degree of trust and affection will be cultivated . . . I know if I need their assistance and advice some day in the future, they will help me without question. (Case 04, Interview 02)

Unlike *ganqing*-based *guanxi* ties, *renqing*-based *guanxi* ties, in essence, have an instrumental component. Although they are built as long-lasting exchange relationships and based on mutual trust and commitment, these affective components serve the ultimate goal of supporting firm growth. Hence, *renqing*-based *guanxi* relationships are 'mixed ties' (Hwang, 1987: 952–953), which not only involve affection, but also economic instrumentality. Nevertheless, the long-term orientation, ongoing social exchanges, frequent communications, and mutual commitment and obligations ensure that these mixed ties are also strong ties. From a structural perspective, although a sparse network configuration provides entrepreneurs with access to additional resources critical for supporting firm growth, it is the strong norms, mutual trust, and interdependence generated by *renqing* that provide a control mechanism for prohibiting opportunistic behaviour of the intermediaries or brokers, thereby reducing risks and maximizing network benefits generated by this *guanxi* circle in the early growth stage.

*Periphery guanxi circle.* During the later firm growth stage, the case studies show that entrepreneurs were actively seeking new business opportunities in order to maintain growth momentum, a unique challenge in later stages of the entrepreneurial process (Kazanjian, 1988). To meet this challenge, entrepreneurs further enlarged their *guanxi* webs by randomly establishing *guanxi* ties with people previously unknown and from diverse backgrounds. Together, these ties serve as the information pool that could keep entrepreneurs alert to changes in the institutional environment and new market information. Because entrepreneurs do not count on such *guanxi* ties for daily business operations, these ties are remote from the centre and, hence, constitute a periphery circle in one's *guanxi* web. Entrepreneurs described their periphery *guanxi* ties as follows:

Overall, I think the ability to build *guanxi* with people from diverse backgrounds is very important in the growth stage. Although now I have stable *guanxi* circles composed of different business connections, I also keep in touch with people, for example, from the college alumni association and from the North American Chinese Student Association and attend academic conferences in my area every year in the U.S. and Europe. I keep relationships with universities in Shanghai, and I am very active in participating in university workshops or giving presentations to college students. Through these activities, I can increase my

company's reputation and also get informed about the development of the market. (Case 05, Interview 01)

Through *yiban* (mere acquaintance) *guanxi* ties, you may get lots of information and resources. I think one of my strengths is that I like to make friends with people from diverse backgrounds. Even though we may have very different backgrounds, I always treat them with sincerity. My point is that we may not have the opportunity to cooperate now, but who knows the future? Extensive and diverse *guanxi* ties are of great importance for any entrepreneur. (Case 01, Interview 01)

The *guanxi* associates in the periphery circle are strangers to each other. Consistent with Chen and Chen's (2004) theoretical proposition, we found that *guanxi* ties with strangers were initiated by revealing personal information, the process referred to by the entrepreneurs as *jianli* (establishing) *jiaoqing* (acquaintance) to explore possibilities of future interactions. Although *jiaoqing* may involve various degrees of affection in social relationships in Chinese society, it is enacted by Chinese entrepreneurs in the present study as building acquaintance for the purpose of future business cooperation. We found that *jiaoqing*-based *guanxi* ties provided the mechanism for cultivating and maintaining relationships with previously unknown individuals. For example, one entrepreneur explains,

I got to know one of my business associates because we were on a business trip, same flight, and we sat next to each other. At a certain point, we started talking. We talked about our hometowns and the kind of business we were engaged in. Although I did not disclose too much detailed information about my business because I didn't even know this person, we did exchange business cards before we got off the plane and promised we would contact each other in the future if an opportunity arises to do business together. Two months later, I received a phone call from this person asking me if I would be interested in establishing a joint-venture with his company. If I didn't *jianli* (establish) some *jiaoqing* (acquaintance) with him beforehand, I wouldn't have this business opportunity at all. (Case 02, Interview 02)

From a network structure perspective, the periphery circle is a sparse network abundant in structural holes. As Burt (1997: 342) notes, 'networks rich in structural holes present opportunities for entrepreneurial behavior'. Although these *jiaoqing*-based *guanxi* relations are instrumental, weak ties as they are economically driven, built on mere acquaintance and require low degrees of maintenance and reciprocal obligations, they are also 'opportunistic ties' (Larson & Starr, 1993: 6), which may offer valuable opportunities that enable the entrepreneurial firm to grow beyond short-term survival and achieve long-term success.

A peripheral location in the *guanxi* web does not mean it is insignificant. Rather, the sparse structure coupled with weak ties offers unique network benefits. Although providing channels to non-redundant resources has long been recognized as the strength of weak ties, the benefit of timeliness is not well-studied. In other words, the sparse structure of the intermediary circle can provide entrepreneurs with additive resources but possibly not in a timely manner as it is costly and takes time to cultivate and develop *renqing* and strong relations. Changes in government policies, investment environment, technology, and the market can all be sources of business opportunities. Hence, both the timeliness and the scope of information are important in seeking new business opportunities. The interview data revealed that diverse *jiaoping*-based *guanxi* ties provided entrepreneurs with fast and low-cost access to diverse, novel information and, more importantly, to opportunity ties with which they can maintain growth momentum. As one entrepreneur describes such opportunity ties,

... business opportunity is embedded in one's *guanxi* web. In the consulting industry where the industry structure is quite stable, diverse *guanxi* ties will allow us to know different services provided by other consulting firms and to seek the business opportunity of establishing a strategic alliance that may increase the competitiveness of individual, privately-owned consulting firms. (Case 05, Interview 01)

Finally, we observe that in the later growth stage, entrepreneurs also spent time managing different *guanxi* circles. Although the composition of the core circle remains highly stable over the entrepreneurial process, entrepreneurs intentionally drew members from the periphery to the intermediary circles and/or intentionally distanced or dropped members from the intermediary circles when they were not active or became irrelevant. An entrepreneur accounted for changes in *guanxi* ties as follows:

Sometimes I form new *guanxi* ties because new tasks and new organizational needs require new interpersonal relations. I also intentionally distance or drop bad or inactive *guanxi* ties from my existing *guanxi* webs. People may change their jobs or retire. Thus, it is not wise to spend time and energy on keeping all these *guanxi* ties. (Case 02, Interview 01)

### Major Differences between Two Industry Sectors

In addition to the above common themes about *guanxi* dynamics in the entrepreneurial process, the cross-case analysis shows two major differences between entrepreneurial firms in knowledge-intensive and less knowledge-intensive industry sectors: (i) ways of conducting and maintaining *renqing*-based *guanxi* ties;

and (ii) perceived usefulness and importance of *guanxi* ties with governmental officials.

First, a clear distinction was found in the ways entrepreneurs cultivated and maintained *renqing*-based *guanxi*. Entrepreneurs from less knowledge-intensive sectors practiced the traditional ‘art of doing *guanxi*’ (Yang, 1994: 6), which involves ‘the exchange of gifts, favors, and banquets’ and ‘the manufacturing of obligation and indebtedness’. However, in knowledge-intensive sectors, we found that although the ultimate goal is still to cultivate trust and affection in relationships with key business associates, the currency being exchanged in this *guanxi*-building process was very different. In knowledge-intensive businesses, *guanxi* ties can be cultivated through knowledge and information sharing. As the entrepreneurs from the knowledge-intensive sectors explained,

The way of cultivating and maintaining *guanxi* is different from ten years ago. In the past, *guanxi* cultivation and maintenance mainly depended on gift-giving or banquets. But now I can establish new *guanxi* ties and maintain *guanxi* relations not by *chichi hehe* (eating and drinking), but rather by information and knowledge sharing. For example, in the past several years, I held a seminar every two months on consulting topics of interest to our clients. Initially, the seminars were not well attended, but after 25 seminars, I now have 5–6 guest speakers and 40–50 attendees at each seminar. These seminars provide our company and our clients with very good opportunities to create new contacts, maintain existing ones through face-to-face interactions, and to be informed about the market. (Case 05, Interview 01)

I established the call center system to maintain a good relationship with existing clients and reach potential customers. I will call our existing clients regularly to inform them about the new services provided by our company. When talking with clients, I also learn about their new needs as well as other possible services I may offer to improve the quality of our service. Through such interaction, the *guanxi* with clients has been significantly strengthened. (Case 03, Interview 01)

The above interview excerpts show that *renqing*-based *guanxi* ties can be initiated and maintained through frequent information exchanges with business associates. By doing so, Chinese entrepreneurs remain informed about their key business associates’ needs and, hence, better adapt to their business routines and practices. Moreover, the commitment to learn and adapt through sharing knowledge and information with business partners is a way of cultivating mutual trust and commitment that is critical to maintaining long-term, *renqing*-imbued *guanxi* ties.

Second, the cross-case analysis also revealed sharply contrasting opinions towards the relative usefulness and importance of *guanxi* ties with governmental officials. We found that only in less knowledge-intensive industries such as energy,

entertainment, and manufacturing, in which government controlled and distributed critical inputs and resources (e.g., land, power) for firm creation and growth, did entrepreneurs report a heavy reliance on *guanxi* with governmental officials in business-related bureaus to obtain accurate information and acquire needed scarce resources. As the entrepreneurs in the energy industry told us,

It is very important to establish good *guanxi* ties with governmental officials in industry-related bureaus because these governmental officials have authorities over resource allocation. . . . In the energy industry where government owns critical resources (e.g., natural gas) and controls the resource distribution process, governmental officials have the final say on who can do the business and who cannot. For example, if firms with similar backgrounds compete for the same business project, the firm with good *guanxi* with bureau officials will have the priority to get the project because good *guanxi* simply means that the government trusts you have the ability to accomplish the task. (Case 02, Interview 01)

. . . It is very important to have *rongchia* (harmonious) *guanxi* with local Chinese governmental officials or officials in related industrial bureaus. The most critical resource for us to start a plastic manufacturing plant is land. Now the Chinese government has a very strict policy on not selling *nongbaodi* (guaranteed land for agriculture), and hence, the land available for industrial uses is very limited. . . . We tried various ways to establish contact and spent a long time on developing good *guanxi* with officials in order to get land. (Case 06, Interview 01)

However, if the critical inputs or resources for creating and operating an entrepreneurial firm were not controlled and allocated by the government, entrepreneurs considered *guanxi* with governmental officials to be relatively unimportant. For example, an entrepreneur who runs an internet business said,

Relationships with governmental officials are not important for our company because the resources needed to sustain and grow an online business are not controlled by the government. . . . However, other businesses, for example businesses in the real estate industry, may need to rely heavily on *guanxi* with governmental officials for the needed resources. Although the Chinese government has now shifted its focus to servicing the society, individual officials still have decision power and authority in distributing scarce resources, such as land. (Case 03, Interview 01)

### **Overall Importance of *Guanxi* for Chinese Entrepreneurship**

Despite the above differences, all entrepreneurs in our study agreed that, overall, *guanxi* is still very important in the midst of China's economic reform and the

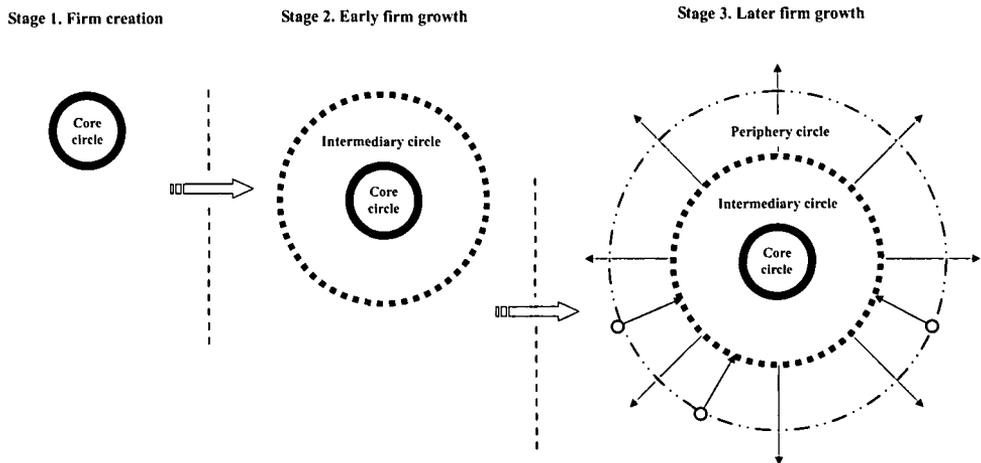
development of a legal infrastructure. The entrepreneurs mentioned that the importance of *guanxi* not only lies in its instrumental usefulness of making resources accessible, but also is deeply ingrained in the Chinese culture. As the entrepreneurs mentioned,

*Guanxi* is of great importance for entrepreneurs because . . . *guanxi* is part of Chinese culture. Western societies give priority to laws and regulations. The order of principles governing personal conduct is *fa, li, qing* (law, reason, and affection). However, in Chinese culture, the order is completely reversed, that is *qing, li, fa*. From this perspective, even though Chinese people now recognize the importance of the law, people still like to rely on *guanxi* in dealing with daily life because culture is difficult to change and *guanxi* is the operationalization of the *qing, li, fa* principle. (Case 05, Interview 01)

*Guanxi* is a unique feature of China. For thousands of years, Chinese people relied on *guanxi* and *qingqing* (affection inherent in family members) in dealing with their lives. Even though we might eventually have a mature legalistic system, using legal means such as filing lawsuits to solve problems is not a typical Chinese way of doing things, and people will call you *mei renqingwei* (lacking human affection) and *lengxue* (cold-blooded). For example, if I have an economic dispute with my clients, the first thing I will do is to contact that person and discuss the situation openly with him or her and figure out ways to solve it. If the attempt fails, I will find common friends, normally ones high in social status such as local governmental officials, to mediate the dispute. Filing a lawsuit will be my last resort. (Case 06, Interview 01)

### **The Emerging Model of *Guanxi* Network Development in the Entrepreneurial Process**

Based on Chen and Chen's (2004) framework and the findings of the present study, we developed a stage model of *guanxi* network development in the entrepreneurial process. Unlike Chen and Chen's (2004) framework, which focuses on the quality of *guanxi* ties and the process through which *guanxi* ties are created and employed, our model is at the aggregate network level and illustrates how an entrepreneur's *guanxi* network evolves over the stages of the entrepreneurial process. According to the nature of compositional ties and the characteristics of network structures, we used different types of lines to indicate the permeability of different *guanxi* circles (core = solid line/not permeable; intermediate = dotted line/moderately permeable; periphery = dashed lines/highly permeable). As the entrepreneurs suggest, the *guanxi* ties in the core circle remain highly stable over the venturing process, and it is the periphery circle that experiences constant change and continuous expansion. Moreover, although the intermediary circle is not as permeable as the

Figure 1. A stage model of *guanxi* network development in the entrepreneurial process

periphery circle, entrepreneurs could still add, distance, or delete members when needed. Therefore, arrows are in both directions between the periphery and the intermediary circle (Fig. 1).

## DISCUSSION

### New Insights into the Network-based Entrepreneurship Literature

In the present study, we employed a multiple-case study method that approached *guanxi* and Chinese entrepreneurship by 'tak[ing] the context seriously' (Tsui, 2009: 7). By contextualizing established social network and entrepreneurship theories and concepts in explicating the features of Chinese entrepreneurs' *guanxi* webs in the firm creation and development process, we are able to develop new insights into the mainstream (largely Western) network-based entrepreneurship literature.

First, we construct a stage model of *guanxi* network development that is shaped by the qualitative data induced from the field study and informed by both Western and Chinese theoretical perspectives. This conceptual model visualizes what Hite and Hesterly (2001) call the phenomenon of the co-evolution of entrepreneurs' social networks and entrepreneurial processes in the Chinese context. Our findings extend this theoretical proposition by adding that the entrepreneurial process is not a linear progression but probably a circular one, wherein business opportunities obtained from the periphery circle could stimulate a new round of the entrepreneurial process, hence maintaining the growth momentum of entrepreneurial firms. Indeed, researchers recently have raised concerns about the dark side of entrepreneurial networks, such as network rigidity (Mort & Weerawardena, 2006) and over-embeddedness (Hite, 2005), which are typical in later stages of the

entrepreneurial process and could largely limit entrepreneurs' ability to identify new business opportunities. Our study suggests that developing a periphery circle with *jiaoqing*-based, weak ties in one's social network, one that continuously expands and contracts, is Chinese entrepreneurs' means for addressing these issues.

Second, the findings of the present study highlight the importance of what Hoang and Antoncic (2003) refer to as the contingency approach to the benefits of different network ties and structures in the entrepreneurial process. Our study provides empirical evidence and supports the previous Western research (Bhave, 1994; Greve & Salaff, 2003; Hite & Hesterly, 2001; Rowley, Behrens & Krackhardt, 2000) that strong ties with family members and close friends are more useful in starting business ventures, whereas weak ties are more valuable for entrepreneurial firms in the growth stage. Moreover, our theorizing of the *guanxi* network development extends this previous understanding by providing a comprehensive examination of characteristics of all major components of network dynamics in the entrepreneurial process.

Indeed, although researchers have extensively studied the benefits and the evolution of network ties (e.g., Hite, 2005; Larson & Starr, 1993) in an entrepreneurial context, we know little about how network structures coupled with network ties may hamper or facilitate firm creation and development. Our findings suggest that in the firm creation stage, the combination of affection-based strong ties and a closure network provides entrepreneurs with access to start-up resources without payback obligations. As the firm reaches the early growth stage, the additional layer of a sparse network enables entrepreneurs to acquire other resources from the non-kin business associates or through brokers and intermediaries. Also, the strong ties with these key business associates provide a control mechanism that reduces the likelihood of opportunistic behaviour highly possible in a sparse network. Finally, in the later growth stage, a third layer of a network rich in structural holes and composed of instrumental weak ties allows entrepreneurs to fully take advantage of the network benefits: fast, diverse market information and a cost-efficient way of identifying new business opportunities. Hence, different combinations of network configurations and network ties fuel the entrepreneurial activities and help emerging ventures overcome initial resource deficiency, grow beyond short-term survival, and achieve long-term success. We believe these findings are probably not unique to China and, hence, contribute to a holistic view of network dynamics in the entrepreneurial process.

### **New Insights into the *Guanxi* Literature**

Our study also developed new insights into the *guanxi* literature. First, we speculate that the identified new ways of cultivating and maintaining *guanxi* are due to the adaptable nature of *guanxi* practice. In theory, *guanxi* practice is embedded in people's social activities and, hence, should be continuously influenced by and

reflect changes in the institutional environment and society at large (Yang, 2002). Although reciprocal exchange is still a major *guanxi* mechanism in the entrepreneurial process, our findings suggest that what comprises the exchange may be adaptable. Although traditional practices (gift or favour exchanges) still exist in the Chinese business environment, there is an emerging new form of *guanxi* conduct that involves knowledge and information exchange. However, given the research design, we cannot draw conclusions regarding how prevalent this new conduct is in China.

Moreover, because this new mode of conducting *guanxi* was observed in knowledge-intensive entrepreneurial firms in both Beijing and Shanghai, we speculate that this may not be a localized phenomenon, and industrial-level factors, such as the degree of reliance on knowledge and information for firm survival and success, may contribute to the emergence of this phenomenon. Future quantitative studies with large, geographically and industrially diverse samples are needed in order to assess the prevalence of these new practices. In addition, given the adaptable nature of *guanxi* practice, qualitative research is critical for identifying whether other new modes of *guanxi* exist in the business context that did not emerge in the current study.

Second, we found that strong *guanxi* ties with governmental officials are not necessary for all entrepreneurial firms. This finding challenges the conclusion in previous studies (e.g., Park & Luo, 2001; Tjosvold, Peng, Chen, & Su, 2008; Xin & Pearce, 1996) that establishing strong *guanxi* ties with government officials is of pivotal importance for private firms in China. In our study, we found this to be true only in less knowledge-intensive industries. We speculate that the usefulness of *guanxi* with governmental officials is contingent on an industry's regulatory strictness or the extent to which the critical resources or inputs for firm creation and growth are controlled and closely regulated by the government. As such, in knowledge-intensive sectors where critical inputs (e.g., entrepreneurs' knowledge and skills) are not under the control of the government, there is less need and motive for Chinese entrepreneurs to invest time and effort in developing a strong relationship with government officials. Although entrepreneurs from knowledge-intensive sectors consider keeping an arm's-length relationship with the government desirable, for them establishing *guanxi* relationships with scholars at research institutes, universities, or executives in other business-related organizations is of greater importance. To confirm this finding, future quantitative research is needed to examine the relationship between the regulatory strictness of the industry and entrepreneurs' tendency to establish *guanxi* ties with governmental officials.

Third, this study has also enlightened the conversation among scholars (e.g., Guthrie, 1998; Yang, 1994; 2002) about the fate of *guanxi* in China's transition. The findings have shown why, in general, *guanxi* is still of great importance in the midst of China's economic reform and the construction of a legal infrastructure. Our findings suggest that, in addition to the instrumental values provided by one's

*guanxi* networks, *guanxi* is part of the traditional Chinese culture that emphasizes human affection. We found that Chinese entrepreneurs gave the ability to exhibit human affection top priority and considered people who merely rely on legal procedures to be socially incompetent. Following this rationale, even though mature legal systems will be established in China eventually, we speculate that it is unlikely that Chinese people would choose the rational legal procedures as the first response in a conflict situation. We argue that this has less to do with the so-called backwardness associated with personalism in pre-modernization societies, but rather is about a fundamental difference between Confucian affection-oriented ethics and what Yang (2002: 472) calls the 'market coldness' of the Western mindset of human relations.

### Limitations and Future Research Implications

The current research has at least two limitations. First, this study focused solely on the entrepreneurs' *guanxi* network dynamics. From our multiple-case study, we also observed that, although network development was resource-dependent, entrepreneurs' proactive network activities have the potential to strongly influence the transitions between the stages of the entrepreneurial process. Accordingly, it is possible that there are human factors that influence network efficacy. Future research could examine the human agency in this process by giving special attention to variations in entrepreneurs' *guanxi* skills and network capabilities.

Second, in the present study, we did not examine potential entrepreneurs who were unable to acquire needed start-up resources for firm creation or who failed shortly after the launch of the firm, phenomena that are well documented in the entrepreneurship literature. It would be interesting for researchers to examine whether deficiencies in entrepreneurs' networking capabilities prevent them from pursuing valuable business opportunities.

### CONCLUSION

The contemporary Chinese context is characterized by a crossvergence of traditional collectivist cultural values and individualist, capitalist ones (Ralston, 2008; Ralston, Pounder, Lo, Wong, Egri, & Stauffer, 2006). This crossvergence highlights a great need for more context-sensitive research, which could capture these changes while developing novel theories that also inform the Western literature. This is a challenge facing all scholars interested in doing management research in China. We believe the current investigation suggests new directions for future empirical examination of *guanxi* networks and entrepreneurship in China and could potentially inform theoretical developments of a possible general theory of network-based entrepreneurship across different cultural contexts.

## NOTES

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