Trust and Control in Sino-German Business Co-Operation

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ABSTRACT

Trust and control have been recognized to be decisive factors for successful cross-border business partnerships. However, there is a lack of studies that explore the concepts’ embeddedness in different socio-cultural backgrounds. This paper seeks to fill this paucity by linking trust, control, and economic performance to the two socio-cultural contexts that are involved in Sino-German business co-operation. The overall results of our comparative study suggest that the socio-cultural background needs to be taken into consideration when examining the relationships; Western theories may not apply worldwide.

Keywords: trust, control, international business co-operation

INTRODUCTION

The need as well as the opportunity for businesses to compete in multiple markets around the world has led to a spread of inter-organizational collaboration across national borders. The significance of managing international business co-operation is reflected in the extensive literature on this topic (for a review see Child & Faulkner, 1998; Doz & Hamel, 1998). It is argued that trust among the business partners is of paramount importance for the co-operation’s success. As a consequence, numerous empirical studies have examined the process of mutual trust in international business co-operation (Aulakh, Kotabe & Sahay, 1996; Child & Möllering, 2003; Huff & Kelley, 2003; Inkpen & Currall, 1997; Sako & Helper, 1998). Another success element is claimed to be the use of control mechanisms (Kumar & Khanna, 2000; Newburry & Zeira, 1999; Wang, Wee & Koh, 1998). Yet, even though both trust and control are central explanatory factors for collaboration success, the relationship between the two concepts is far from clear (Das & Teng, 1998).

Furthermore, cross-border partnerships usually involve different cultures. However, despite a magnitude of studies that have explored phenomena like trust and control in business partnerships, relatively few scholars have directly addressed the different national cultures and their link to the formation of trust as well as to the application of control mechanisms in cooperative relationships (Huff & Kelley, 2003). This paper seeks to overcome the outlined deficiencies by addressing the impact of national cultures on trust and control, the relationship between trust and control, and the contribution of trust and control to the business success in the context of Sino-German business co-operation. The focus on Sino-German
business co-operation was chosen because the two countries’ contrasting values and norms promise new and context-sensitive insights. Compared to Germany, the Chinese business environment is known for its weak institutional support and guarantees. Therefore, business transactions in China are strongly dependent on trustful relations between business partners. On the other hand, it is difficult for foreigners to build up trust because Chinese do not easily extend trust outside their kinship and community based social networks (Child & Möllering, 2003). Ultimately, analysing trust and control in Sino-German business co-operation is also of practical relevance since Germany has become China’s most important European trade partner and German foreign direct investments into China have accelerated in recent years (Deutsche Bank Research, 2004; Eurostat, 2004).

THEORY AND HYPOTHESES

Definitions of Terms

The literature on trust reveals various conceptualizations and so far, there have been only very few attempts to integrate the different perspectives (McKnight & Chervany, 2001; Rousseau, Sitkin, Burt & Camerer, 1998). However, our review of the multidisciplinary literature on trust shows that most of the previous definitions have three assumptions in common: (1) Risk is a prerequisite for trust to arise. Risk is defined as the potential of negative outcomes for the trustor if the trustee does not prove trustworthy (Lewis & Weigert, 1985; Rousseau et al., 1998). (2) Trust is based on a set of beliefs and expectations the trustor holds about the trustee’s competence, benevolence, and behaviours (McKnight & Chervany, 2001). (3) Beliefs and expectations of the other party’s trustworthiness stimulate the trustor’s willingness to put its fate in the hand of the trustee and to take actions which make him vulnerable to the trustee (Mayer, Davis & Schoorman, 1995). Thus, incorporating these assumptions, we define trust as a willingness to rely on another party under a condition of risk based on positive evaluations of the intention, competence and behaviour of the trustee (for similar definitions see Mayer et al., 1995; Rousseau et al., 1998).

Traditionally, control has been a core concept for the analysis of processes within and between organizations. Its definition varies across scholars and disciplines (Das & Teng, 1998). In the context of business co-operation the concept of control refers to the actions one partner develops in order to
influence the other partner’s behaviours in a way that helps to attain the partnership’s goals (Inkpen & Currall, 1997). Control actions include a range of formal and informal (social) governance mechanisms. Formal controls are codified in rules and procedures. They involve regular and explicit information transfer. Informal controls utilize values and norms to foster a partner’s desirable behaviour. The latter are more uncertain and embedded in the social relations between the partners (Das & Teng, 1998).

The dichotomy individualism vs. collectivism represents a basic value dimension which Hofstede (1980) proposed for analysing variations among cultures. Individualism characterizes societies in which people look after themselves and their immediate family but neglect the interests of other groups or the society as a whole. In individualist countries (such as Germany) values and actions like initiative, autonomy, assertiveness, and self respect are highly valued. In collectivist societies, on the other hand, people prefer to act as members of a group rather than individuals. Extended and tight social networks exert control over their members through social pressure as well as through emotional dependence. People from collectivist societies (such as China) make a sharp distinction between the members of their own social networks (‘in-group’) and members from other groups (‘out-group’). Within the boundaries of the in-group they emphasize cooperation, harmony and ‘saving face’. However, it is argued that beyond the boundaries of the in-group, collectivists compete with and exploit people more extensively than individualists (Watkins & Liu, 1996).

**Trust and Control in Individualist and Collectivist Cultures**

So far, only very few scholars have linked trust in cross-borders business relationships directly to the prevalent societal cultures in general or the cultural dimension ‘individualism vs. collectivism’ in particular. The popular view holds that trust between business partners is high in collectivist societies and low in individualist societies (Dyer & Singh, 1998; Doney, Cannon & Mullen, 1998). However, some authors have challenged this reasoning. For example, Fukuyama (1995) identified both collectivist and individualist societies that generally show a low level of trust (e.g. China, Korea, France) respectively a high level of trust (e.g. Germany, Japan, United States) in other people. In the case of China, several authors have confirmed the low level of trust prevalent in Chinese society (Child & Möllering, 2003; Kiong & Kee, 1998, Wang & Yamagishi, 1999). The tendency to distrust members of
the out-groups might be increased by the weak institutional safeguards China has developed regarding business partners’ capriciousness and opportunism. As the neo-institutionalist view of trust (e.g. Lane & Bachmann, 1996) emphasizes, trusting relationships are promoted by effective and comprehensive rules and norms which deter from and sanction misbehaviour. Despite significant advances in the legal provisions, China has made little progress to put into effect the institutional bases for trust between (economic) actors, both Chinese and foreign. Thus, our first hypothesis is as follows:

_Hypothesis 1. In Sino-German business co-operation Chinese managers show less trust in their foreign business partners than German managers in their Chinese partners._

A co-operation might also be successful if effective control mechanisms are put in place (Geringer & Hebert, 1989; Newbury & Zeira, 1999). Due to the lack of a system of trustworthy institutions and legal protection outside the circles of family or guanxi networks, Chinese business partners have to resort to additional approaches to exercise control over the foreign partner. We therefore propose:

_Hypotheses 2. In Sino-German business co-operation Chinese managers employ more control mechanisms than German managers._

Traditionally, the two concepts of trust and control have been conceptualised as opposing alternatives (Aulakh et al., 1996; Inkpen & Currall, 1997; Parkhe, 1993; Ring & Van de Ven, 1994). But some researchers claim that control mechanisms support the generation of mutual trust (e.g. Sitkin, 1995). Their argument is that exerting control enables to document and to evaluate trustful behaviours which consequently provides a basis for generating trust between the business partners. In a review of the literature Das & Teng (1998) suggest that trust and control can exist simultaneously, that is, they operate independently from each other and contribute jointly to the co-operation’s success. However, since the few studies that empirically analysed the relationship between trust and control concluded that the deployment of controls leads to a decline of trust in the partner (Mohr, 2003) we propose an inverse relationship between the level of trust and control in cross-cultural business co-operation.

_Hypothesis 3. The less control mechanisms are applied the more trust a business partner has in the foreign business partner._
**Trust, Control and Business Performance**

Despite the increasing recognition of the role that trust plays for the success of cross-border business partnerships, very little empirical research has attempted to document the relationship between trust and performance. In accordance with a study by Child and Möllering (2003) who were able to confirm a positive relationship between trust and business success in the context of joint ventures and other forms of co-operation between Hong Kong based companies and partner firms in Mainland China, we propose:

*Hypothesis 4. The more trust one partner in a Sino-German business co-operation has in his counterpart the better its economic performance.*

A positive relationship between control and business success is particularly supported by agency theory and transaction cost theory (Dyer, 1997, Ramanathan, Seth & Thomas, 1997). Yet, empirical research has produced mixed results (Child & Faulkner, 1998; Geringer & Hebert, 1989). As the discrepant findings can be attributed to the lack of consistency across different investigations we propose:

*Hypothesis 5. The more control mechanisms one partner deploys in a Sino-German business co-operation the better its economic performance.*

**METHODOLOGY**

**Sample**

The data used to test the above hypotheses were collected during 2002 in Germany and China. To define the sample we used two approaches. First, we contacted the Delegation of German Industry & Commerce in China and asked for their support in identifying German small and medium-sized enterprises (SMEs) which collaborated with Chinese partners. Second, we visited several international trade fairs in Germany in order to contact German and Chinese companies. These two approaches resulted in the identification of 81 German and 152 Chinese companies. A questionnaire was mailed to the key-informant of each company who had a primary responsibility for managing the day-to-day relationship with the partner. The response rate for the German sample was 63% and 26% for the Chinese sample. Useable questionnaires were obtained from 51 German respondents and 40 Chinese respondents. The main industries covered by the sample are engineering (24%), automobile (19%), and
A majority of the companies has less than 250 employees. The most frequent forms of collaboration are the equity joint venture (58%), followed by distribution partnerships and contract production (each about 20%).

Measures

The questionnaire included a broad range of items concerning trust and control in Sino-German business relationships. It was fully structured and the responses had to be given on a 5-point Likert-type scale ranging from (1) ‘strongly disagree’ to (5) ‘strongly agree’. Based on the back-translation strategy we constructed a German and a Chinese version of the questionnaire. Items that measured the concept of trust were addressing the five components integrity, openness, competence, reliability, and loyalty. These components of trust were selected by surveying the literature (Butler, 1991; Schindler & Thomas, 1993; Cummings & Bromiley, 1996) and by analysing the answers of German and Chinese MBA-students given in an exploratory study concerning the meanings of trust/distrust which was conducted at our department. Overall, ten items were designed to measure organization-oriented trust. The trust scale is one-dimensional with a Cronbach’s alpha coefficients of .89 in the German sample and .81 in the Chinese sample, indicating high reliability.

Control was measured by using seven statements about the use of specific formal as well as informal control mechanisms. The selection of control mechanisms was guided by the existing literature on control in business co-operation (Child & Faulkner, 1998; Geringer & Hebert, 1989). The items were combined into one scale that reflects the extent of controls one business partner deploys in the relationship (Cronbach’s alpha is .84 in the German and .80 in the Chinese sample).

As the participating companies were not willing to provide ‘hard’ data about the cooperation’s success, its performance was measured by a success rating. The respondents were asked to assess the cooperation’s return on sales compared to the return on sales in their domestic business activities.

RESULTS

Table 1 reports the means, standard deviations and correlations of trust, control and business success both for the German and the Chinese sample.
TABLE 1
Means, Standard Deviations, and Pearson Correlations by Samples\textsuperscript{a,b}

<table>
<thead>
<tr>
<th></th>
<th>Chinese sample</th>
<th>German sample</th>
</tr>
</thead>
<tbody>
<tr>
<td>Items</td>
<td>Mean</td>
<td>s.d.</td>
</tr>
<tr>
<td>1. Trust scale</td>
<td>3.63</td>
<td>.47</td>
</tr>
<tr>
<td>2. Control scale</td>
<td>3.18</td>
<td>.66</td>
</tr>
<tr>
<td>3. Return on sales</td>
<td>2.53</td>
<td>.62</td>
</tr>
</tbody>
</table>

\textsuperscript{a} Chinese sample N = 40
\textsuperscript{b} German sample N = 51

\textit{Trust, Control and Cross-Cultural Differences}

Hypothesis 1 predicts that German managers exhibit a higher level of trust in their Chinese partners than vice versa. Yet, as can be seen in Table 1, Chinese business partners report more trust in their German partners than German partners in their Chinese partners. The difference in the level of trust is statistically significant ($t = -3.68, p < .01$). Hypothesis 1 is therefore not corroborated. Hypothesis 2 proposes a higher extent of controls for the Chinese sample than for the German sample. But the average level of controls is about the same in both samples ($t = .05, \text{n.s.}$). Therefore, Hypothesis 2 is not supported. Hypothesis 3 predicts an inverse relationship among trust and control. The correlations of both measures reported in Table 1 indicate a negative and statistically significant relationship between trust and control only for the German sample ($r = -.35, p < .05$). The Chinese sample reveals a positive correlation coefficient ($r = .34, p < .05$), suggesting that control fosters rather than impedes trust and vice versa.

\textit{Trust, Control, and Business Performance}

The calculation of a linear regression analysis with trust and control as predictors of the co-operation’s success shows that both predictors significantly contribute to the economic success of the partnership from a German point of view (see Table 2). However, the results concerning the Chinese sample do not
corroborate the theoretical predictions. From a Chinese perspective, trust and control do not appear as significant predictors for the partnership’s economic success in Germany.

**TABLE 2**

Results of Regression Analysis of Trust and Control on the Co-Operation’s Return on Sales *(by Samples)*

<table>
<thead>
<tr>
<th>Independent variables</th>
<th>Chinese sample</th>
<th>German sample</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust scale</td>
<td>-.15</td>
<td>.35*</td>
</tr>
<tr>
<td>Control scale</td>
<td>.06</td>
<td>.36*</td>
</tr>
<tr>
<td>R</td>
<td>.15</td>
<td>.45</td>
</tr>
<tr>
<td>R²</td>
<td>.02</td>
<td>.20</td>
</tr>
<tr>
<td>Adjusted R²</td>
<td>-.05</td>
<td>.16</td>
</tr>
<tr>
<td>F</td>
<td>.33</td>
<td>4.80*</td>
</tr>
</tbody>
</table>

*standardized regression coefficients are reported*

* p< .05 (two-tailed)

**DISCUSSION**

The primary purpose of our study has been to empirically test whether the embeddedness of trustors and trustees in different socio-cultural contexts promote a specific pattern of trust and control in cross-border business co-operation. We were particularly interested in finding out whether managers from individualist cultures trust and control their foreign business partners more or less than managers from collectivist cultures. Contrary to Hypothesis 1 we found that business partners from the collectivist Chinese society show a higher propensity to trust foreign business partners than individuals from the individualist German society. A possible explanation might be that the Chinese respondents took into account the reliable and impartial functioning of the German legal and economic institutions when assessing their level of trust in their German partners. On the other hand, German partners seem to recognize the weak institutional foundations in the Chinese business environment and do not take the protection of these institutions in the commercial disputes for granted. Therefore, the risks involved in collaboration with Chinese companies prohibit ‘too much’ trusting. Thus, our results challenge the taken for granted assumption that Chinese business practices emphasize the traditional sources of trust embedded in strong social relations and neglect the importance of societal institutions as safeguards.
against opportunistic behaviours (Child & Möllering, 2003). Furthermore, it seems inadequate to infer from a nation’s alleged societal trust (Fukuyama, 1995) the degree of displayed trust toward a foreign business partner. The concept of high-trust and low-trust countries is therefore only appropriate when it refers to characterizing the relationships within a society. Yet, when it concerns relationships with people from other societies the distinction is not very helpful. Another interpretation of the unexpected higher level of Chinese managers’ trust holds that Chinese businessmen do not start a business co-operation until they have developed a strong trusting relationship with the potential partners. To overcome the handicap of distrusting external partners, Chinese managers may have expanded the scope of their in-groups to include foreign partners. We suggest that future studies should examine whether collectivist business partners invest more time and effort to develop trusting relationships with outsiders before cross-border business transactions start than business partners from individualist societies.

Moreover, our prediction that the Chinese partners are applying more control mechanisms than German partners (Hypothesis 2) was not corroborated. The results suggest that the control activities of German business partners compensate for their low trust level in the Chinese partners. At the same time, Chinese partners who trust their opposite seem to pursue control activities at the same time. These post hoc interpretations imply different relationships between trust and control in the two cultures under study. Indeed, the sample-specific correlations indicate that trust and control are associated in the predicted way of mutual exclusiveness only in the German sample, thus confirming Hypothesis 3. However, in the Chinese sample we found a positive correlation, indicating that trust and control supplement each other. It might be argued that for Chinese managers, control guarantees trust whereas for German managers, control impedes trust.

Finally, concerning the success of cross-cultural co-operation, the linear regressions of the variables ‘trust’ and ‘control’ on the measure ‘return on sales’ indicate that both predictors have a significant effect in the German sample but not in the Chinese sample. This might reflect the different economic contexts in which the partnerships are embedded. From the perspective of German business partners, trust and control play an important role for the economic performance in a highly dynamic and unreliable business environment like the Chinese. On the other hand, the Chinese business partners’ experience shows that
trust and control do not constitute significant factors for business success in the highly regulated and stable German business system.

In sum, our research results suggest that in order to understand the role of trust and control in cross-border business relationships it is not enough to study the relationship per se but rather seems necessary to also look at the socio-cultural contexts from which the partnering companies and individuals originate. Therefore, future research is encouraged to examine the interdependencies of trust, control and performance in cross-border business partnerships by incorporating socio-cultural differences that exist across countries.

**Limitations and Implications for Future Research**

Due to limited resources and the small size of the participating companies, we interviewed only one key person from each company. Therefore the subjectivity of the answers could not be controlled for. Moreover, collecting data from just one person implies that the respondent has to provide information on both the independent as well as the dependent variables which might result in a common-method bias (e.g. Avolino, Yammarino, & Bass, 1991).

Although we can, based on the answers of our German respondents, agree with the argument that trust is a prerequisite for business success our study lacks ‘hard’ data about the economic success. Therefore, further research is needed to explore the influence of trust and control on economic performance of cross-border-business partnerships.

Finally, we would like to comment self-critically on the research method we applied. The questionnaire approach might have reproduced a specific understanding of trust and control which corresponds with popular theorizing but not necessarily with the respondents’ point of view. Our approach is particularly questionable if the respondents live and work in socio-cultural contexts that are different from the researchers’. We therefore call for more qualitative, in-depth approaches which take these considerations into account.
REFERENCES


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1 The full questionnaire is available upon request from the first author.