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**Social Capital and China's Private Enterprise Start-ups:
An Examination with Special Reference to the IT Sector**

Qihai Huang

A thesis submitted to the University of Bristol in accordance with the requirements of the degree of PhD in the Management Research Centre, the Faculty of Social Sciences

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Abstract

This thesis examines what kinds of *guanxi* are resorted to and how *guanxi* networks are mobilized by Chinese private entrepreneurs for their business start-ups. It does so with special reference to the private IT sector.

Guanxi are personal relations that can be resorted to for certain ends based on the norm of reciprocity. It is argued that *guanxi* is a similar concept to social capital in the West. Like social capital, *guanxi* has an instrumental function, and is used for personal ends. *Guanxi* overlaps with the three main streams of social capital theory. They have common ingredients. Nevertheless, there are some differences between the two terms. It is further argued that research on *guanxi* can contribute to social capital theory in terms of how social capital is brought into being.

Much has been made of the advantages of those who have been cadres in entering the private sector in post-communist societies. It is argued that a well-defined cadre concept is the precondition to do further analysis of whether being a cadre or having close cadre connections confers advantage in private business operations, as it has several meanings in different contexts in China. The thesis utilizes both quantitative and qualitative methodologies and uses several different research sources. These include the unpublished 1995 national survey data set on private enterprises in China and an original analysis of thirty private IT companies situated at Beijing Zhongguancun Hi-tech Park.

An analysis of the unpublished national survey data set on private enterprises in China suggests that being a cadre or having close cadre connections does not confer significant advantage in private enterprise start-up financing. This is not in accordance with power conversion theory. The popular practice of *guanxi* may have contributed to this finding.

At a theoretical level, it is argued that the power conversion theory oversimplifies social capital theory and neglects the subjective dynamics of human beings, by which social capital can be created. *Guanxi* is seen to come from several channels. Some types of *guanxi* come from endowment, and some from saving. If entrepreneurs do not have *guanxi* at hand, they will establish certain *guanxi*, and then invest to develop and maintain *guanxi*. There are two other strategies to have *guanxi*: by subcontracting and linking to the elite.

A particular feature of the thesis is the adoption of a reflective methodology in researching the case studies. In this way, the researcher made use of *guanxi* in the process of field research and thereby offers a contribution to the understanding of *guanxi* and social capital.

For my wife Caiyun and our first child

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Author's Declaration

The work presented in this thesis was carried out in the Management Research Centre of the University of Bristol and is entirely my own work, except where other authors have been referred to and acknowledged in the text. The views expressed in the thesis are totally my own and not those of the university. This thesis has not been submitted for a degree in this, or any other university.

Qihai Huang

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Chapter 1 Introduction

1.1 The under-researched sector

As a witness to one of the most significant outcomes of the reform in China over the last two decades -- the emergence of private sector¹, I was attracted to research China's private enterprises. However, when I started to look at the relevant literature in 1998, I found that the sector was largely neglected, compared to state owned enterprises (SOEs), township and village enterprises (TVEs), and foreign direct investment (FDI). Scholars researching China believe that FDI and TVEs have been the major driving force for China's fast growth in the past, as SOEs have not only performed badly in terms of productive efficiency but also have been a burden on the economy, since the government has to subsidize loss-making SOEs (e.g., Shan, *et al.*, 1997; Chen, 1996; Chen, *et al.*, 1995; Child, 1996; Naughton, 1995; Walder, 1995; Warner, 1995; Woo *et al.*, 1994). However, with the outbreak of the Asian financial crisis in 1997, FDI has been eroded and the export volume of TVEs has plunged. The Chinese economy has now to rely more on domestic capital and private business (*China News Digest*, March 23, 1998; *South China Morning Post*, March 19, 1998).

¹ In this research, private sector is defined as domestic private businesses under the effective control of Chinese citizens. It included 1.2 million private enterprises (*siying qiye*) and 31.2 million individual economy (*getihu*) in 1998, providing about 20 per cent of employment and industrial output of China (*China Statistical Yearbook*, 1998). Private enterprises are the main concern here. See Chapter 2 about the rapid expansion of private enterprises.

1.2 A fundamental question

Initially only allowed on the margin of the Chinese economy, the private sector has grown out of the plan (Naughton, 1995). The private sector has played a more and more important role not only in the economy but also in social life. The development of the private sector has forced changes in policies and regulations (Young, 1995). Wank (1999) argues that private business is widely considered the most far-reaching departure from the Chinese communist order, with profound consequences for economy and polity.

The Chinese literature on the private sector mainly concerns the characteristics of private entrepreneurs and their class character and social status (e.g., Jia *et al.*, 1994; Zhang and Liu, 1995). The Western research on the Chinese private sector considers the development of the sector in terms of the process of reform (e.g., Kraus, 1990), and how this process has affected the outcome for both private business and the course of development in China (e.g., Bruun, 1993; Young, 1995). But neither literature has investigated the very fundamental question: how do private entrepreneurs start up their businesses²?

1.3 The question in its context

It is impossible for the researcher to approach the question of how Chinese private

² Though Wank (1999) does mention start-ups in Chapter 6, when he looks at how commercial advantage in private business is constrained by family background and life experience of particular entrepreneurs, how to start-up is beyond his main concern.

entrepreneurs start up their businesses innocently. As pointed out previously, there is no existing research on China's private enterprise start-ups, and the researcher is therefore likely to be guided by the existing literature developed in other post-communist societies. In practice, there is little existing literature specifically on private business start-ups in other transitional economies, either. Erutku and Vallee (1997) look at business start-ups in Poland, but they simply give a description of entrepreneurs, such as their age, what businesses they are in and what problems they are facing. Although not developed in China, there are, however, theories on other transitional economies that try to explain the development of a private sector and these provide the researcher with an initial research agenda. One main concern of this literature is who these people are and how they take advantage in the transition from socialism to capitalism, and as a result, how this transition will change the social structure of the former socialist societies (e.g., Szelenyi, 1988; Kolankiewicz, 1996; Rona-Tas, 1994). A main stream of the research believes that cadre-related entrepreneurs have an advantage in their business operations. This is termed power conversion theory (Rona-Tas, 1994). Another theory that sounds contradictory to this argument claims that the main beneficiaries of the transition will be those who were in less privileged positions before the transition and that cadres become losers. This is labelled the circulation of elites (e.g., Szelenyi, 1988; Nee, 1989, 1991). Either way, cadre appears as a key concept in both theories.

On the other hand, research on the post-communist countries implicitly uses the concept of social capital. One of my contentions is that this is more or less similar to the notion of

guanxi in China, which, many researchers, in particular non-Chinese ones, seem to occupy themselves with. The thesis has been constructed in such a way as to enable this concern to be addressed.

Looked at in broad terms the logic behind the thesis is as follows. It starts, in this chapter, with a critical examination of the existing literature. After pointing out some deficiencies in the existing research, the question is posed of whether the theories developed in other communist countries can be applied to the China case, which has a different reform approach. In due course this leads us on to look at, firstly, whether cadre-related entrepreneurs have an advantage in business start-up (here empirical data on China's private sector is used); and, secondly, the apparent lack of advantage for cadres to be explained. The second point is itself two-sided. It tries to address on the one hand why cadre-related entrepreneurs do not have a significant advantage and on the other hand how entrepreneurs with different backgrounds actually do start up their businesses. This analysis is supported by both quantitative and qualitative original empirical data.

For a better understanding of the different reform approach and the emerging of a private sector in China, the thesis firstly describes the policy changes and the development of the sector in an early chapter. This also provides the background for the current research (Chapter 2).

This research then examines the origin and the broad usage of the term cadre in the

Chinese setting, arguing that a clear definition is ignored by the existing research. We see that one cadre concept encompasses all personnel with authority or expertise in party, state, army, or units of economic production, be they party members or no (Strauss, 1999). We also see, though, that cadre is sometimes understood as a social class, in contrast to worker and peasant (e.g., Li *et al.*, 1991; Lin and Bian, 1991). Yet again, we see that cadre also refers to someone in certain leading positions (Burns, 1985). Thus a well-defined cadre concept is the precondition to further analysis of whether cadre has advantages in private business operation.

Based on a clearly defined cadre concept, the thesis analyses a unique unpublished national survey data on private enterprises in China (Chapter 3). Such an analysis allows us to see whether as the power conversion theory claims being a cadre or having a close connection with cadres provides the entrepreneurs with any advantage in business start-up. Backed by cadre experience or close cadre connections, the entrepreneurs with cadre background or close cadre social relations should be more likely to have higher start-up capital. Also, they should also appear more likely to finance their start-ups from public funding. We systematically test this hypothesis.

Following the survey data analysis, is an examination of the key concepts to the thesis: *guanxi* and social capital (Chapter 4 and 5). This thesis presents the first systematic research on the relationship between *guanxi* and social capital. After an explanation of the two concepts and their respective usages, it critically applies *guanxi* and social capital to

the question of business start-up. Unlike most available research focusing on existing social capital, the thesis endeavors to investigate of how social capital is brought into being. The available research suggests that being a cadre or being born into a cadre family is important. We see that there can be some other alternative forms of social capital. Social capital is dynamic. It can be created.

The methodology for the case studies of this thesis, which is a chapter of the case studies (Chapter 6), partially demonstrates this. It describes how the researcher conducted his field research by a *guanxi* snowball sampling approach, i.e., exploiting *guanxi* to conduct field research by using the initial *guanxi* to ‘snowball’ and gather additional contacts as informants. This first hand experience is itself unique. The autobiographic account provides a reflective research method, which could offer sociologists the chance to understand the social environment: the *guanxi* network, in which the individuals act as social beings. Moreover, based on the experience, the researcher explores the relationship between him and the *guanxi* ties that helped him roll the snowball. As such, the thesis reveals that *guanxi* and social capital are multi-dimensional. *Guanxi* and social capital in the field research are much richer than the available literature suggests.

As little empirical research on business start-up in other transitional economies has been conducted, this attempt to focus on business start-ups in the Chinese private sector fills a gap and contributes to the literature more generally. With respect to *guanxi* and start-up, an important objective is to examine what *guanxi* ties are resorted to for business start-up

(Chapter 7). It further seeks to tackle the question of how these *guanxi* ties come into being, which is neglected by the existing research on social capital (Chapter 8). The findings in these two chapters seek to justify the assumption in the previous chapters that social capital is dynamic and social capital can be produced in several different ways.

The thesis is not simply about business start-up in China, it focuses specifically, by means of case studies, on start-up in the private IT sector in China. It examines how the private IT companies mobilize social networks for their business start-ups, shedding a light on the so-called new economy.

Today, it seems that 'new economy' has replaced 'knowledge economy' to become the most popular and most frequently used term at international symposiums, within media, and in market analysis. In the so-called new economy, information technology together with economic globalization enables a state of high growth, low inflation and low unemployment. Business cycles are abolished (e.g., Weinstein, 1997). The Federal Reserve Board chairman Alan Greenspan believes that it has become clear that this business cycle differs in a very profound way from the many other cycles before (*Federal Reserve Bank*, 2000). Later, with the soar of Internet stocks, many people labeled information technology and the Internet industries as 'new-technology industries' or 'new-economy industries' (Fan, 2000).

China boasts to have become one of the top ten countries in information technology

industries. In the last ten years, the information technology industries have a very high growth rate, three times the country's GDP growth rate (*Xinhua News Agency*, December 9, 2001). In China, to many, this wave of new economy, the ongoing information and scientific technological revolution will provide China with new opportunities for catching up with developed countries (e.g., Lau, 2000). The CEO of Intel Craig Barrett advised that China's businesses needed to implement e-business strategies to gain a competitive advantage in today's new Internet-driven economy (*China Daily*, October 29, 2000). The Chinese leadership knows that in addition to the wealth generated and jobs created for China by successful new Internet companies, the web can help reform the economy. The Chinese leadership has described e-commerce as the future of business. Wall Street has seized on China and the Internet as a golden combination of the world largest emerging market and the biggest technological revolution in global business (*Financial Times*, August 2, 1999).

The collapsing dot-com stocks have impact on the Chinese IT sector, too. The backlash of the burst dotcom bubble and pronounced worldwide technology ebb stormed Comdex (Computer Distributor Exhibition) China in Beijing in April 2002, leaving a lacklustre turnout, few marque names and innovations, and even fewer freebies at the much-touted computer trade show. Analysts with the China Centre of Information Industry Development (CCID) believe that the lull that the trade show industry is now experiencing points to the downward spiral dogging the IT industry (*China Daily*, April 30, 2002).

The Chinese economy has been closely connected with the world economy. For example, the downturn of the world economy resulted in the declining growth of China's exports in the first three quarters of 2001, a drop from the 33.1 per cent in the same period of 2000 (*China Daily*, December 18, 2001). This is in particular the case for the IT sector (*China Daily*, November 13, 2001; April 30, 2002). It is expected that the terrorist attacks on New York have a negative impact on China's economy. As a major exporter to the United States, China is likely to suffer should a recession hit the United States, as it would weaken purchasing power of US consumers (*China Daily*, September 18, 2001). China finally became a member of the World Trade Organization (WTO) in 2001, after 15 years of arduous negotiations. This means that China will have become much more interdependent on the world business.

There are good reasons, then, to examine those entrepreneurs who operate in the IT sector, which is most market-oriented in China, and find out to what extent China's business system has changed and how it will develop in the globalisation of economic activities.

1.4 Two contradictory theories: literature review

It has been pointed out that researchers on transitional economies put forward two contradictory theories about who will benefit most from the transition and how the consequence will transform the social structure of these societies (Rona-Tas, 1994; Szelenyi and Szelenyi, 1995). The first argument suggest that the main beneficiaries of the

transition will be those who were in less privileged positions before the transition (e.g., Szelenyi, 1988; Nee, 1989, 1991, and 1996). The second theory claims that the old elite in the communist regime can benefit from their advantageous positions and are therefore the primary winners of the transition (e.g., Kolankiewicz, 1996; Rona-Tas, 1994; Staniszkis, 1991). The first theory is termed the circulation of economic elites (Szelenyi, 1988; Szelenyi and Szelenyi, 1995). Rona-Tas (1994) labels the second argument 'power conversion theory'. In Szelenyi and Szelenyi's (1995) words, it is an elite reproduction theory.

Szelenyi (1988) draws on the circulation of elite theory, based on the study of household farming in Hungary. Szelenyi finds that the amount of land held by the head of the household or his parents before the communist came to power had a positive association with the income the household produced on its private land plot in 1980. He concludes that the emerging market in agriculture is a continuation of a long-term historical trend of embourgeoisement, interrupted by the communist revolution. Szelenyi further predicts that a new economic elite will emerge from below, from a group in disadvantageous positions in the communist regime. This is because people most active in private farming were those whose families were already acquainted with market production and who could draw on pre-communist memories of market culture transmitted by their families. On the contrary, the few who became cadres were less likely to participate in market-oriented private farming.

By contrast, according to the second argument (e.g., Rona-Tas, 1994; Kolankiewicz, 1996; Clark, 2000), during the transition from socialism to capitalism, the primary beneficiary of marketisation is the old elite in the centrally planned state economies. Power accumulated during state socialism is converted into assets of high value in a market economy. Cadres are at an advantage not only in starting up but also in operating companies, because they can transfer state assets into quasi or real ownership for business. Alternatively, they can use their social relations (networks) to get access to credit and valuable information. As a consequence, as the argument goes, cadre entrepreneurs are more successful.

For example, it is claimed that in Hungary, being a cadre helps entrepreneurs to start their corporate companies and helps them to be financially successful in terms of their incomes, compared with the entrepreneurs with non-cadre experience (Rona-Tas, 1994). In the Czech Republic, the *nomenklatura* enterprise founders have a privileged position in terms of access to scarce resources, information, knowledge and experience of other members, and money and other material resources that are not generally available. When lacking economic capital for business start-up, *nomenklatura* enterprise founders could use their contacts to sort out Communist Party property for themselves (Clark, 2000). In Poland, private entrepreneurs who themselves have cadre background are also reported to have an advantage in business. Cadres suppressed the official price at which enterprises were marketed and, given the shortage of capital in the country, legally purchased these properties at incredibly discounted prices. Thus a substantial portion of Poland's productive capital fell into the hands of well-positioned insiders. Out of office, the

ex-cadres can still make use of their insider knowledge and personal network endowments as brokers among various key segments and actors of the economy (Staniszki, 1991). According to Kolankiewicz (1996), in Poland, those who have a close relationship with cadres have the advantage, too. *Nomenklatura* networks are mobilised for economic gains.

The rather sparse research on the Chinese private sector also offers two contradictory theses. It mostly draws on power conversion theory. According to Wank (1999), entrepreneurs born into cadre families, have the most supportive ties with officialdom and thick transaction networks. The vast resources controlled by the state were transferred to the primitive accumulation that stimulates business start-up, drives subsequent growth, and provides security. Odgaard (1992) argues that former cadres and party members seem to be able to evade government control and such political backgrounds matter greatly for the development of the largest and most profitable private enterprises.

On the contrary, the market transition theory put forward by Nee (1989; 1991) is in the similar vein with Szelenyi's (1988) argument of the circulation of economic elites. Built on the data for Chinese private family farms from Fujian province in the 1980s, Nee claims that the most privileged class of state socialism, cadre, lost some of their advantages, while those at the bottom of the state socialism hierarchy, the direct producers, such as peasants, benefited. After 1977, Chinese peasants received land, their production targets were less strictly regulated by the government, and they were allowed to sell their products in urban markets. As a result they expanded their production, increased their productivity, and their

incomes and living standard increased. Cadres are relatively disadvantaged, as they have little or net advantage in entering private entrepreneurship.

According to Nee (1989; 1991), this is the result of the reform that changes the mechanisms. Under the state redistributive economy, the price of labour is set administratively by the state, the allocation and distribution benefit cadres, since cadres, as redistributors, tend to favour their own. In contrast, on the market transition, as markets replace state redistributive mechanisms in the allocation and distribution of goods, producers are likely to have more power; if markets operate, there are greater incentives for individual effort in market transactions, while redistributive power is likely to matter less; then entrepreneurship becomes an alternative avenue for socio-economic mobility. Cadres, who are still reliant on the redistributive mechanism, become losers.

Both theories seem to have some plausibility. On the one hand, there is evidence that people connected with cadre enjoy rewards. On the other hand, there is also some evidence that families with entrepreneurs but without cadre connections earn more income (Fligstein, 1996, p1075). Both Rona-Tas' (1994) and (Fligstein, 1996) agree to Nee's (1989) general interpretation. However, Rona-Tas' (1994, p44) makes the criticism that no sociological theory of transition from socialism to capitalism can rely wholly on the experiences of agricultural petty commodity production as suggested by Szelenyi, (1988) and Nee (1989, 1991). Another problem for Nee (1989, 1991) is that he generalises conclusions to large populations (Fligstein, 1996, p1075). In fact, both Szelenyi, with his associates (1995,

1996), and Nee (1991) later admit that some cadres retained their advantage. The continuing cadre power in China is because of partial reform, under which the institutional foundations of a market economy are only partially in place and cadres continue to redistribute resources by virtue of their positional power (Nee, 1991, p268). Power conversion argument is the dominant view of elites in Eastern Europe (Szelenyi and Szelenyi, 1995, p617). In a sense, the power conversion theory sounds more reasonable.

Unfortunately, up to now, in the power conversion theory literature, only Rona-Tas' (1994), Wank (1999) and Clark (2000) have provided some empirical evidence. Thus the evidence supporting the power conversion theory is weak (Nee, 1996, p914).

Clark (2000) builds his argument on five cases of *nomenklatura* entrepreneurs in the Czech Republic he interviewed with the assistance of translators. He therefore wisely acknowledges that the limited nature of these case studies makes it hazardous to draw very general conclusions and suggests that there is a need to compare *nomenklatura* entrepreneurs with those of non- *nomenklatura* background. Clark (2000) himself does not provide such a comparison.

The only systematic empirical study is Rona-Tas' (1994) analysis of Hungarian income survey data collected in the spring of 1989 and 1991. Rona-Tas' (1994) distinguishes two private sectors in Hungary. The first is the private sector for consumer economy, which is operated by self-interested individuals and has existed all the time as the second economy.

The second is the expansive modern sector, which, by the new legal forms of entrepreneurship and the privatization of state property, allows private enterprises to accumulate capital. In the first private sector, cadres have less or no advantage. Ex-cadres are at an advantage in starting the second type of enterprises.

But this does not seem to fit to the case of China. The variable 'income' used in Rona-Tas' (1994) analysis is measured in terms of the summed figures of primary income, secondary income from a second job, contracts, tips, household farming, and rental of an apartment, land, or equipment, and profit from a business enterprise. However, Rona-Tas (1994) realises himself that income of private entrepreneurs will be considerably underestimated, for example, to avoid income tax may be one concern of the entrepreneurs. Moreover, it does not supply any information about the importance of profit from business to the income of the entrepreneurs. Even if self-reported income is valid, there lies a question mark in the use of personal income to value the benefits the entrepreneurs get during transition. In the case of China, according to a survey, 41.4 per cent of the private entrepreneurs do not separate their income from enterprise profit (Hu *et al.*, 1999). In any case, since 'an entrepreneur is an owner or co-owner of a company' after the Law on Economic Association laid the foundation for privatisation (Rona-Tas, 1994, p53), it is profit gains that is the interest of the entrepreneurs (Veblen, 1965).

Another difference between China and East Europe lies in different paths of privatisation. In all East European countries, the privatisation of the public became state policy after

1989, while in China the public sector is maintained (Szelenyi and Kostello, 1996). Where privatisation has been more bottom-up in China, old political connections may count less (Rona-Tas, 1994, p64), as the similar new opportunities in Hungary provided by the privatisation process to buy machines or buildings and as such from state firms, of which individuals can take advantage, did not exist yet in China. On the contrary, as Kraus (1991) finds, at the very beginning of the reform, people in private businesses were from peripheral groups, such as prisoners, the unemployed.

Wank (1999, chapter 6) claims that the social backgrounds of entrepreneurs in China constrain the kinds of paths they operate through. He further argues that for the entrepreneurs born into cadre families, they could transfer the vast resources controlled by the state to the primitive accumulation and business start-up. They are also more successful in subsequent business operations. This can be true. But the ambiguous typology of cadre undermines his evidence and argument. As a matter of fact, none of the existing research on the Chinese private sector has given readers a clear idea about what cadres are. Such research either provides an ambiguous concept of cadre or gives an arbitrary definition of cadre (e.g., Nee, 1989, 1991; Wank, 1996, 1999).

Simultaneously, as pointed out in the previous section, this research begins with an analysis of national survey data on private enterprises in China. It aims to find out if the dominant power conversion theory is tenable in empirical data based on a clearly defined cadre concept. If the power conversion theory is right, the following hypotheses should

hold true in empirical data. 1) Backed by cadre experience or close cadre connections, the entrepreneurs with cadre background or close cadre social relations should be more likely to have much higher start-up capital. 2) The entrepreneurs with cadre background or close cadre social relations should appear more likely to finance their start-ups from public funding. So far, the test of such a hypothesis is not available. Chapter 3 is to fill such a gap.

1.5 Social capital perspective: solving puzzles and bridging the two theories

Fligstein (1996, p1074) comments that the available research presents clues about what is happening in the post-communist societies, but their conclusions raise as many puzzles as answers. In fact, the power conversion theory partially explains the success of the entrepreneurs with cadre background or cadre connections, but largely neglects how those entrepreneurs without such backgrounds start, survive, develop and succeed in their businesses. For example, how did the China's 50 richest entrepreneurs succeed? At least forty of them have neither cadre background nor cadre fathers. Indeed, six of them were peasants when starting their businesses (*Forbes*, November 27, 2000). Also it ignores the fact that some cadre entrepreneurs fail in their businesses. Szelenyi and Szelenyi (1995) in their comparative research on three East European countries find that on the one hand, some of the old elite hold the command positions of the new corporate sector in Poland and Hungary; on the other hand, some of the old elite lost out. For example, about half of those who managed the largest firms in 1988 in Hungary and Poland were out of elite positions by 1993. According to Hanley (2000), only a small proportion of *nomenklatura* members

in Poland have ownership of economic assets, of whom, the vast majority reported ownership of very small businesses. Thus, the argument that the cadre elite converted their old privileges into new ones is too simple (Szelenyi and Kostello, 1996, p1093), as if there are few or no limits to the conversion of cadre status into economic gains (Szelenyi and Szelenyi, 1995, p616).

In these contexts, this thesis attempts to contribute to the literature by examining the Chinese private enterprise start-ups from a social capital theory perspective. It is hoped that it will solve some puzzles and bridge the gap between the two apparently contradictory theories. Such a theory will also be a complement to the existing research.

Figure 1.1 The simple model of power conversion theory

Cadre entrepreneurs → direct access to state resources → business success

‘Social capital is the aggregate of the actual and potential resources that are linked to the possession of a durable network of relationship or mutual acquaintance and recognition’ (Bourdieu, 1986, p248). In ordinary language, social capital is called connections (Bourdieu, 1993, p160). The theory of power conversion is in the frame of social capital theory. Figure 1.1 shows the simple model of power conversion theory. It is partially in line with Bourdieu’s (1986) argument, who points out that dominant social classes can use their privileged access to the three forms of capital, namely, economic capital, cultural

capital and social capital (see Chapter 5), to make strategic conversion of one kind of capital to another in order to solidify their class position.

However, the argument of power conversion mainly looks at the existing cadre background or cadre connections but overlooks the creation of social capital. Bourdieu (1986, p249) has also pointed out that social capital, i.e., the existence of a network of connections, is not necessarily naturally given. Instead, it can be the product of investment by individuals who consciously or unconsciously aim at establishing or reproducing such social relations. Connections from cadre families and cadre experience are two channels to have social capital, if such connections are important and productive. The role of human agency must not be neglected (Wilkinson, 1996). Are there any other strategies to produce social capital?

Furthermore, social capital is not always inheritable (Pahl, 1996). Social capital of the old order is not necessarily useful in the new order. The power conversion argument oversimplifies the process from social capital to economic outcomes as 'simultaneously a cause and an effect' (Portes, 1998, p16). Most of the research begs the question of how social capital is transformed into economic capital, which is indeed much more important.

In China, *guanxi*, a similar term to social capital in the West, is popular, and indeed, it has become a means for business operation. *Guanxi* practice may have countervailed the disadvantage of lacking cadre background. When certain production factors are not

available, it becomes the channel to access the factors demanded. Social capital is one among several factors of production, along with human capital, monetary capital and physical and natural resources (Rose, 1997). Entrepreneurs, in particular those having been cadres, can access resources via cadre connections as Figure 1.1 suggested. In a transitional economy, if there is no other source of credit and capital, the prediction that cadres have preferential access to capital, which is held by government, is reasonable (Walder, 1996, p1069). However, for example, many researchers have found in all socialist economies the second economy—the private sector always exists, even before reform (Los, 1990; Kraus, 1991). This means that resources entrepreneurs access to for business operations are not necessarily in the hands of cadres. It implies that *guanxi* network for access to resources is not limited to cadre connections, on the other hand. In other words, entrepreneurs can resort to different types of *guanxi* for resources needed. These *guanxi* ties may include cadres who have control over resources. But even if cadres who control resources are not members of the network of an entrepreneur, the network can bridge the entrepreneur over to cadres, when needed.

1.6 Structure of the thesis

The thesis is divided into four parts:

Part 1 looks at the background and development of private businesses in China.

In Part 2, a more theoretical part of the thesis, there are three chapters. Chapter 3 aims to test the power conversion theory. It firstly looks at the concept of cadre by examining its origin and usage in other communist countries and China. Then, based on a clearly defined cadre concept, it analyses the unpublished 1995 national survey on private enterprises in China. The analysis focuses on the social backgrounds of private entrepreneurs and their close social relations, their business start-up capital, and the association between start-up and their backgrounds and their close social relations. A surprising finding is that being a cadre or having close cadre connections does not confer any advantage on the entrepreneurs in financing business start-up. It is argued that being a cadre and having close connections with cadres are only two of the channels producing *guanxi*. The widespread practice of *guanxi* has contributed to the finding in the other ways. It is argued that further in-depth qualitative research is needed to investigate how private entrepreneurs start up their businesses.

Chapter 4 examines the concept of *guanxi*. The chapter reviews the available literature on *guanxi* by providing the definitions of *guanxi*, the functions of *guanxi*, the reasons of its emergence, the consequences and the implications of *guanxi*. It is found that there exist different types of *guanxi* and there are some deficiencies in the available research on *guanxi*.

Chapter 5 explores the concept of social capital and the relationship between *guanxi* and social capital. It is argued that *guanxi* and social capital have several aspects in common

and that research on *guanxi* can overcome some deficiencies in the existing research on social capital and contributes greatly to the richness of the concept.

This is followed by Part 3 with four chapters, which take the form of case studies. It extends the analysis on *guanxi* in the previous chapters. Chapter 6 describes how the case studies were conducted. In the vein of autobiographic methodology and self-reflection, this chapter explains how the field research was conducted with the help of *guanxi*. The nature of such *guanxi* is also explored with respect to contingency, reciprocity, obligation of social capital from *guanxi*, and social status. An argument in this chapter is that a cadre *guanxi* network does not always produce positive outcomes. It is contingent upon situations, for example, a change in one's social status can influence on one's social capital. Newly developed *guanxi* can also be useful. This also applies to businesspeople.

Chapter 7 considers how the entrepreneurs in the private IT sector financed their start-ups. It is found that there are different channels of financing, which demonstrate different types of *guanxi* with different rules, for example, different forms of trust. *Guanxi* are thus not necessarily cadre *guanxi* as the power conversion theory assumes. *Guanxi* can be of different types and strengths. The finding in this chapter again points to the complexity of *guanxi* and social capital.

Chapter 8 looks at how the private entrepreneurs found their customers at business start-ups. This chapter reveals that some types of *guanxi* or social capital come from

endowment, and some from saving. If the entrepreneurs do not have *guanxi* at hand, they will establish certain *guanxi*, and then invest to develop and maintain *guanxi*. There are two other strategies to have *guanxi*: by subcontracting and linking to the elite.

Chapter 9 concludes the research. It draws together the threads of the previous eight chapters. Then it discusses some research areas opened up by this research. Further, in a more speculative vein, it suggests that firstly, *guanxi*-based business practice will not diminish its importance in China, and secondly, the Chinese system of business does not seem to be in the transition to the Western model; instead, it indicates the development of network business system.

Part 1

Chapter 2 The Development of Private Enterprises

The emergence and development of a private sector is one of the most significant outcomes of the reform in China over the last twenty years or so. Private business is widely considered the most far-reaching departure from the Communist order, with profound implications (Wank, 1999). The private sector has expanded beyond the marginal role firstly supposed, forcing changes in taxation, licensing, and regulations along the way (Young, 1995). Thus it is essential to look at the policy changes, operation environment and the development of the sector, which in fact are the background of my current research. This chapter aims to provide a background for the thesis. It examines the policy development for the private economy in China, and the growth and contribution of private enterprises to the Chinese economy. In order to demonstrate its dynamics, comparisons with other sectors are also presented.

2.1 The revival of private economy and the recognition of private enterprises

According to Kraus (1991), at the beginning of the 1950s after the founding of the People's Republic of China, there were 7.24 million independent private craftsmen, merchants and industrialists in the cities and towns, with about 40 million employees engaged in private business activities. The private sector produced more than half of China's industrial output. But later the Chinese Communist Party (CCP) set about systematically eliminating private business (the so-called nationalisation), and small-scale production and business were also

increasingly limited and finally annihilated. By the end of 1956, only 160,000 small-scale businesses remained, and the numbers continued to decline. Though there was a brief flurry of individual business activity following the failure of the Great Leap Forward, individual business was attacked by the Cultural Revolution as the “rat-tail of capitalism”. Not until the late 1970s did reform lead to the revival of private businesses, which was mainly due to two reasons.

Firstly, it was part of the reform to revitalize the ailing economy. Byrd (1992) argues that the emergence of the Chinese economic reform was due to pervasive inefficiency in SOES and the need to shift from Soviet-style extensive growth to intensive growth based on improved resource allocation. By 1978, China’s industry was concentrated in urban areas and mostly owned by the state, with its output accounting for 90 per cent of the total and the remainder coming from collective enterprises. The private sector consisted of only about 150,000 individual peddlers, craft-people and repairers (Kraus, 1991). In 1978, 72% of the overall 43.5 million industrial people worked in the state sector, 91.8% of the industrial sector’s RMB 242.37 billion in fixed assets belonged to the state. Despite a high average annual growth rate of 14% for industrial output for nearly three decades, China’s industry suffered from low efficiency levels, using obsolete technologies to produce unwanted products at high costs. Enterprises produced according to the plan set by the government, which did not consider the market demand. When a profit was certain, a higher cost resulted in a higher price. Enterprises simply reported costs and prices to the government without caring about the high costs. This led to massive waste and low

efficiency (Feng, 1995).

The average productivity of capital had declined substantially: in 1957, RMB 100 worth of capital produced RMB 139.3 worth of industrial output, the same amount produced only RMB 95.5 in 1977. By 1977, the average productivity of capital had decreased about 30 per cent. Studies also found stagnating total factor productivity (Chang and Wang, 1994). One possible explanation to the declining productivity is the low degree of workers' commitment in SOEs, as there is a strong relationship between behavioural indicators of worker attitudes and productivity and costs (Norsworthy and Zabala, 1990, cited in Bowles and Dong, 1999, p17). Workers in SOEs work at their own pace, and management implicitly had to negotiate with them to fulfill production targets (Chan, 1994). Similarly, Walder (1989) also describes how managers had to depend on workers' co-operation to get production going.

Secondly, it was the result of the threat from the huge unemployment from both rural and urban areas. In rural areas, with the introduction of the household responsibility system, peasants started to diversify their economic activities, market their products, and invest in non-agricultural businesses. However, townships and villages lacked the resources to develop collective industry to employ the surplus labour released by reform. The household responsibility system itself is a form of private economy, which also became the initial stimulus to develop private economy further to absorb the huge surplus population.

In the urban areas, the ailing SOEs could neither absorb any more employees from the huge unemployment nor meet the demand of consumers, in particular numerous, varied and atomised goods and services. Regardless of the rural areas, in urban areas, unemployment became a severe problem for the government: many of the 17 million “educated youth” began to return, with a residue of young people who had evaded being sent to the rural areas, but who had no jobs; in addition, there were about 3 to 5 million school leavers each year who needed jobs. By 1982, 7 million people were joining the waiting lists for jobs every year. Thus the most important motive for the government to allow the development of private business was the need to increase employment opportunities (Young, 1995).

However, at the beginning of the revival of private economy, it was limited to individual economy (*getihu*), as the communist party emphasised that only very small, simple businesses would be allowable, and that these would be limited by state regulations and their dependence on the socialist public economy. The framework envisaged in this policy still consisted of the traditional hierarchy of state, collective, and individual ownership, with state enterprises viewed as politically and economically superior, and the private sector intended to play a marginal role and to act as a supplement to the state and collective sectors. In line with these ideas, the private sector policy at the beginning of 1980s was aimed at allowing a limited amount of private business to take on some of the small-scale tasks that were difficult for the planning system to perform effectively. Private operators were not issued business licenses if their businesses competed with local state or collective.

In addition, licenses were initially restricted to people who did not have other employment prospects. Kraus (1991) finds that the employees in the private sector came from people looking for work, workers who lost their old jobs and unemployed, and pensioners. The unemployed comprised many different groups, mainly those who, as a result of work disabilities, had been eliminated from the normal work system, and former convicts, who had no chance of getting work in state or collective enterprises.

The policy of promoting a limited private sector was confirmed by the State Council's issuing of a national regulations on urban individual economy in July 1981. The regulations encouraged and supported "unemployed youth" to work in fields whose products "were urgently needed by the masses, but which could not be supplied or only to a limited extent by the state or collectives". Operators were permitted to engage in small-scale handicrafts, retail commerce, catering, services, repairs, non-mechanised transport and building repairs. The regulations specified that individual economy should employ at most two assistants and five apprentices, "The activity of individual business is performed by one person or family. If necessary, one or two helpers may be employed with the approval of the State Administration for Industry and Commerce. Workers with great or unusual technical experience may employ two or three, maximally five, apprentices" (cited in Kraus, 1991, p18). Later in March 1984, the government issued a decree to encourage engagement of individual business in rural areas, more importantly, the previous employment limit of two helper or five apprentices was raised to a total of seven persons. But all these affirmed the role of the individual economy as a "necessary supplement" to

the state and collective sectors, and placed limits on the size and scope of these businesses. Up to now, private economy was equal with individual economy (*getihu*) and it grew rapidly. By 1982, there were 2.63 million individual economy (*getihu*), with employment of more than 3.20 million (Kraus, 1991).

However, the individual economy expanded production and scale, grew out of the set frame especially in the number of employees. Not until October 1987, did there come the breakthrough to full recognition for private enterprises, when the 13th Party Congress of the Chinese Communist Party formalised the theory of the initial stage of socialism. The theory claimed that economic development was the primary goal of the first phase of socialism, and thus capitalistic phenomena such as large private enterprises still had a positive role to play. Private enterprise, i.e., a privately owned enterprise hiring more than seven workers, was accepted for the first time. In April 1988, the revised Constitution legalised the existence and development of private economy, and promised state protection and support.

This was followed by *the Provisional Regulations on Private Enterprises* issued by the State Council in 1988 and *the Rules for Implementation of the Provisional Regulations on Private Enterprises* promulgated by the State Administration of Industry and Commerce in 1989. According to the regulation, private enterprise refers to the economic organisation, of which the assets belong to individuals, with more than 7 employees and run for profit making. By the end of 1988, China had 90,581 private enterprises (*China's Private*

Economy Yearbook, 1994, p168). Currently, the Chinese government defines three kinds of ownership as private enterprises. They are sole ownership, partnership, and a limited liability company.

The status of the private enterprises was given further recognition in November 1993, when the Chinese Communist Party held the third plenary session of the 14th Central Committee and officially declared that it was aiming for a market economy (for some years the official phrase had been “commodity economy”), albeit a socialist market economy. The government regarded the private sector as “an important economic force in developing new productive forces” and an integral part of “socialism with Chinese characteristics”.

Then came the greatest change in the government attitude to private ownership in 1997, when the 15th Chinese Communist Party Congress announced the private enterprises as an important component of the economy and allowed the sales of state owned enterprises to the private sector. Private ownership was amended in the constitution in 1999.

The gradual recognition of private enterprises and private ownership involves changes in institutions and policies. It also reflects the gradual and flexible approach of reform in China (Walder, 1995). Also, reform in China has taken place alongside with a strong continuity in fundamental ideologies and values (Brunn, 1993). This may be the so-called socialism with Chinese characteristics. But with the legalisation of private property right, it is indeed a form of capitalism with Chinese characteristics.

2.2 The rapid development of private enterprises

As it was pointed out previously, private enterprise is the most dynamic component of China's economy. The rapid development of private enterprises is seen not only with respect to the number of firms, registered capital and employment but also with respect to output and their contribution to retail trade and industrial and commercial tax. The changes since the formal recognition of private enterprises are shown as follows.

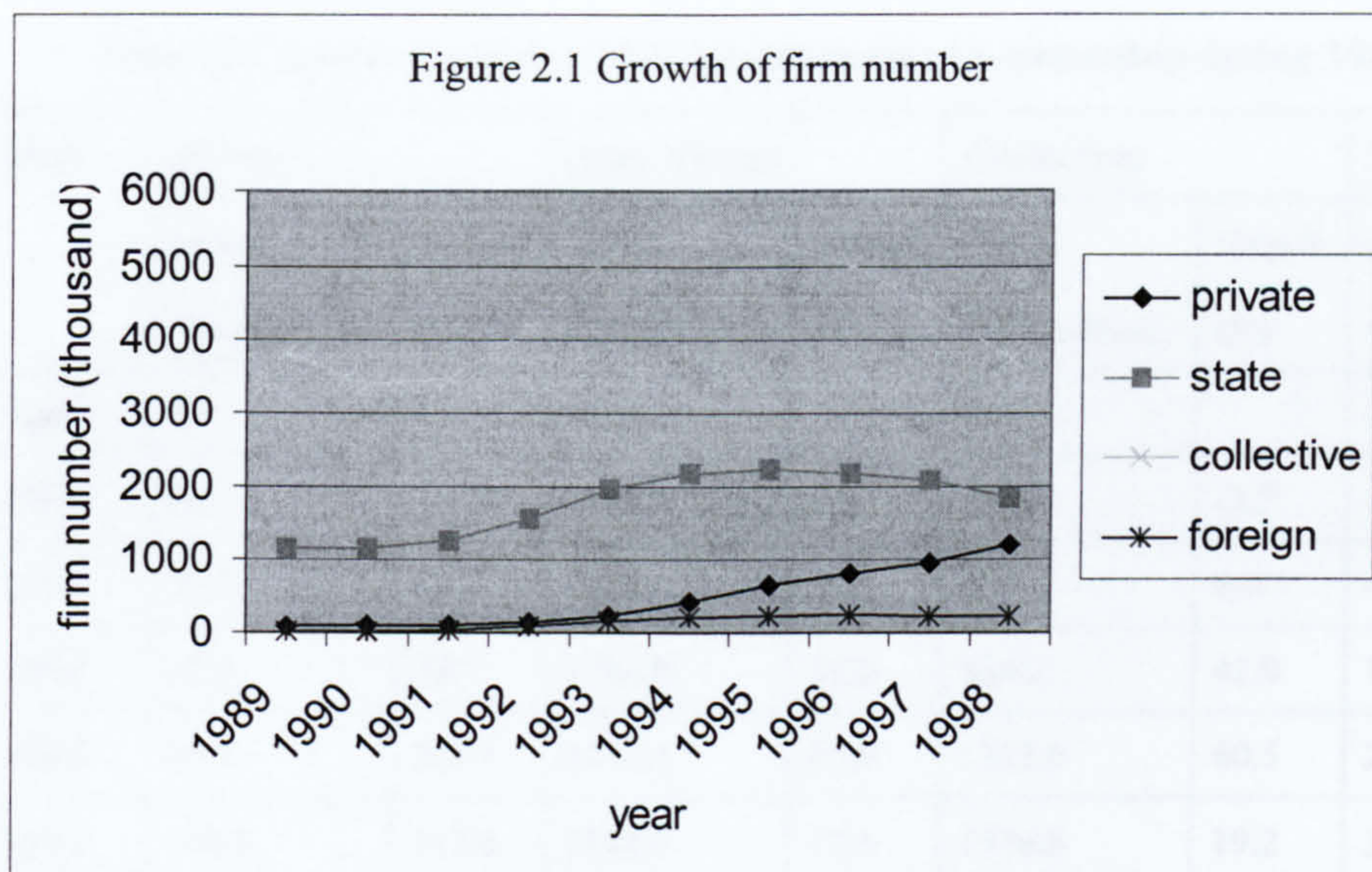
2.2.1. Growing number of private enterprises

The development of private enterprises is reflected in the growing number of private enterprises. Table 2.1 shows the development of private enterprise and compares the development with other ownerships. The number of private enterprises amounted to more than 1.2 million in 1998, which is 13 times of the number in 1989. Between 1989 and 1998, the number of private enterprises grew at an average annual rate of 33.3 per cent, while the growth rates for SOEs, TVEs, and FDI were 5.4 per cent, 0.3 per cent, and 34.4 per cent respectively. Though the average growth rate of private enterprises was a bit lower than that of FDI, it was much higher than those of SOEs and TVES. More importantly, while the numbers of SOEs, TVEs, and FDI started to decrease from 1996 and 1997, private enterprises are still on the tendency of growing. The trend is better shown in Figure 2.1. After the 1992 Southern Tour of Deng Xiaoping, the senior leader, who advocated a bolder reform progress, the Chinese economy boomed soon and every sector grew rapidly. However, with the outbreak of Asian financial crisis in 1997, the numbers of enterprises in the three sectors except the domestic private enterprises declined.

Table 2.1 Numbers of enterprises by ownership during 1989-1998

Year	Private		State owned		Collective		Foreign owned	
	Number (thousand)	Growth (%)	Number (thousand)	Growth (%)	Number (thousand)	Growth (%)	Number (thousand)	Growth (%)
1989	90.6		1146.9		3829.6		15.9	
1990	98.1	8.35	1151.5	0.4	3381.9	-11.7	25.4	59.5
1991	107.8	9.89	1253.7	8.9	3480.0	2.9	37.2	46.6
1992	139.6	29.5	1547.2	23.4	4159.4	19.5	84.4	126.7
1993	237.9	70.4	1951.7	26.1	5156.5	24.0	167.5	98.5
1994	432.2	81.7	2166.3	11.0	5456.8	5.8	206.1	23.0
1995	654.5	51.4	2218.6	2.4	5337.7	-2.2	233.6	13.3
1996	819.3	25.2	2163.3	-2.5	5013.4	-6.1	240.4	2.9
1997	960.7	17.3	2078.3	-3.9	4470.5	-10.8	235.7	-2.0
1998	1200.1	25.0	1836.3	-11.7	3736.4	-16.4	227.8	-3.3
average		33.3		5.4		0.3		34.4

Source: *China Statistical Yearbook, 1989-1998; Statistical Documents of China Industry and Commerce Management, 1991-1998*



2.2.2. Increasing registered capital

Increasing registered capital is another indicator of the growth of private enterprises. The changes in registered capital for private enterprises and the comparison with other ownerships are demonstrated in Table 2.2. In 1989, the total registered capital in private enterprises was RMB 8.4 billion. Ten years later in 1998, it grew more than 85 times to RMB 719.8 billion. The average annual growth rate was 64 per cent. During the same period, the average annual growth rates for SOEs, TVEs and FDI were 12.9 per cent, 11.6 per cent, and 36.9 per cent respectively. The average annual growth in private enterprises in terms of registered capital was much higher than in other ownerships.

Table 2.2 Total registered capital for enterprises by ownership during 1989-1998

year	private		State owned		Collective		Foreign owned	
	capital (RMBbillion)	Growth (%)	capital (RMBbillion)	Growth (%)	capital (RMBbillion)	Growth (%)	capital (US\$billion)	Growth (%)
1989	8.4		1123.2		565.3		27.6	
1990	9.5	13.1	1192.5	6.2	544.4	-3.7	33.0	19.8
1991	12.3	29.5	1368.3	14.8	577.1	6.0	44.7	35.2
1992	22.1	79.7	1794.8	31.2	824.2	42.9	116.0	159.7
1993	68.1	208.1	2546.2	41.9	1322.6	60.5	245.6	111.8
1994	144.8	112.6	2886.9	13.4	1576.8	19.2	312.3	27.1
1995	262.2	81.1	3166.4	9.7	1623.1	2.9	399.1	27.8
1996	375.2	43.1	3284.4	3.7	1726.5	6.4	441.5	10.6
1997	514.0	37.0	3629.4	10.4	1624.4	-5.9	459.8	4.1
1998	719.8	40.0	3488.0	-3.8	1512.5	-6.9	467.3	1.6
Average growth		64.0		13.0		11.7		36.9

Source: *China Statistical Yearbook, 1989-1998; Statistical Documents of China Industry and Commerce Management,*

1991-1998

Meanwhile, the average registered capital for a private enterprise increased very fast, which demonstrates the expanded economic scale for them. From 1989 to 1998, the average registered capital for a private enterprise grew from RMB 92.7 thousand to RMB 599.3 thousand, at average annual growth rate of 23 per cent, compared with 7.6 per cent for SOEs, 11.9 per cent for TVEs, and 1.9 per cent for FDI (Table 2.3). The average

registered capital for FDI seems stagnant, as FDI declined sharply in both 1990 and 1991 after the political event in 1989.

Table 2.3 Average registered capital for an enterprise by ownership during 1989-1998

year	private		State owned		Collective		Foreign owned	
	Reg. capital (RMB1,000)	Growth (%)	Reg. capital (RMB1,000)	Growth (%)	Reg. capital (RMB1,000)	Growth (%)	capital (US\$1,000)	Growth (%)
1989	92.7		979.3		147.6		1733.1	
1990	96.8	4.4	1035.6	5.8	161.0	9.1	1301.4	-24.9
1991	114.1	17.8	1091.4	5.4	165.8	3.0	1200.1	-7.8
1992	158.3	38.8	1160.0	6.3	198.2	19.5	1374.7	14.6
1993	286.2	80.8	1304.6	12.5	256.5	29.5	1466.4	6.7
1994	335.0	17.0	1332.6	2.2	289.0	12.7	1515.2	3.3
1995	400.6	19.6	1427.2	7.1	304.1	5.2	1708.8	12.8
1996	458.0	14.3	1518.2	6.4	344.4	13.3	1836.1	7.5
1997	535.0	16.8	1744.1	15.0	363.4	5.5	1951.1	6.3
1998	599.3	12.0	1899.5	8.9	404.8	11.4	2051.2	5.1
Average growth		23.0		7.6		11.9		1.9

Source: *China Statistical Yearbook, 1989-1998; Statistical Documents of China Industry and Commerce Management,*

1991-1998

2.2.3. Employment in private enterprises

More and more employment in private enterprises is another important indicator. In 1998, private enterprises had over 171 million employees. The figure was not significant

compared that of SOEs and TVEs, but it was higher than that of FDI, 2.9 million, in the same year. It is noted that real number of employees in private enterprises should be bigger, since many private enterprises are operated under the guise of SOEs or TVEs (it is termed “wearing red hat”)³, and there are considerable numbers of individual economy (*getihu*) having more than 7 employees but not registered as private enterprises.

From 1989 to 1998, the employees in private enterprises rose to 171 million, more than 10 times of 1.6 million in 1989. In other words, the employment in private enterprises increased 29.8 per cent every year. This was higher than the average annual growth rate of 22.6 per cent for FDI, and contrasted sharply against the negative average annual growth rate of -0.01 per cent for SOEs and -0.06 per cent for TVEs (Table 2.4). Workers in SOEs

³ Based on a survey of 475 private enterprises in a county, Jia et al. (1994) find that there were many preferred policies if a private enterprise could succeed in registering as a collective enterprise.

- 1) More bank loans. The maximum bank loan a private firm could be granted was 15 thousand *yuan*; while that for a collective firm could be several hundred thousand *yuan*;
- 2) Lower interest rate. The highest bank interest rate for private firms was 11.52 per cent; while the interest rate set for collective firms was only 6.6 per cent, and 6.3 per cent if the loan was under certain limit amount.
- 3) Free administration fees. Private enterprises had to pay Industry and Commerce Bureau 2 per cent of administration fees, while collective firms were not charged.
- 4) Favoured tax. Private firms paid tax at a ten-scale-accumulated-value-added system, while collective firms paid at an eight-scale system, which was lower.
- 5) Other preferences. Collective firms were exempted from product tax in the first year of business start up and from gain tax in the first two years. The policy did not apply to private firms. While private had to pay membership fees to the association of private entrepreneurs, etc.

Similarly, in Fushan county of Guangdong province, where private economy is active, private sector was in unfavored position. A private enterprise had to pay 3 per cent of its turnover and another 3 per cent of its gain as tax, while a collective firm only paid a tax of 1 per cent of its turnover.

and collective TVEs started to be made redundant with the reform in labour. Also, many private enterprises under the guise of collective firms took off their “red hats” and registered as private ownership when private entrepreneurs were assured of private property right by the Chinese senior leader Deng Xiaoping’s speech in 1992. Thus, the employment in both state and collective firms grew slowly or negatively.

Table 2.4 The growth in employment by ownership during 1989-1998

year	Private (%)	State (%)	Collective (%)	Foreign (%)	Total (%)
1989					
1990	3.7	2.4	1.3	40.4	15.5
1991	8.2	3.1	2.2	150.0	1.4
1992	26.1	2.1	-0.2	33.9	1.2
1993	60.9	0.3	-6.3	30.3	1.3
1994	73.7	2.7	-3.2	-32.3	1.3
1995	47.3	0.4	-4.2	23.6	1.1
1996	22.5	-0.2	-4.2	14.1	1.3
1997	15.3	-1.8	-4.4	9.1	1.1
1998	26.7	-18.0	-31.2	-2.3	0.5
Average	29.7	-0.01	-0.06	22.6	2.6

Source: *China Statistical Yearbook, 1989-1998; Statistical Documents of China Industry and Commerce Management, 1991-1998*

More importantly, the private sector has increasingly provided employment opportunities for the workers laid-off from the SOEs. For example, according to *Homeway Financial News* (January 5, 2000), in 1999, an average of 4,000 workers made redundant by SOEs joined the workforce in the private sector every day.

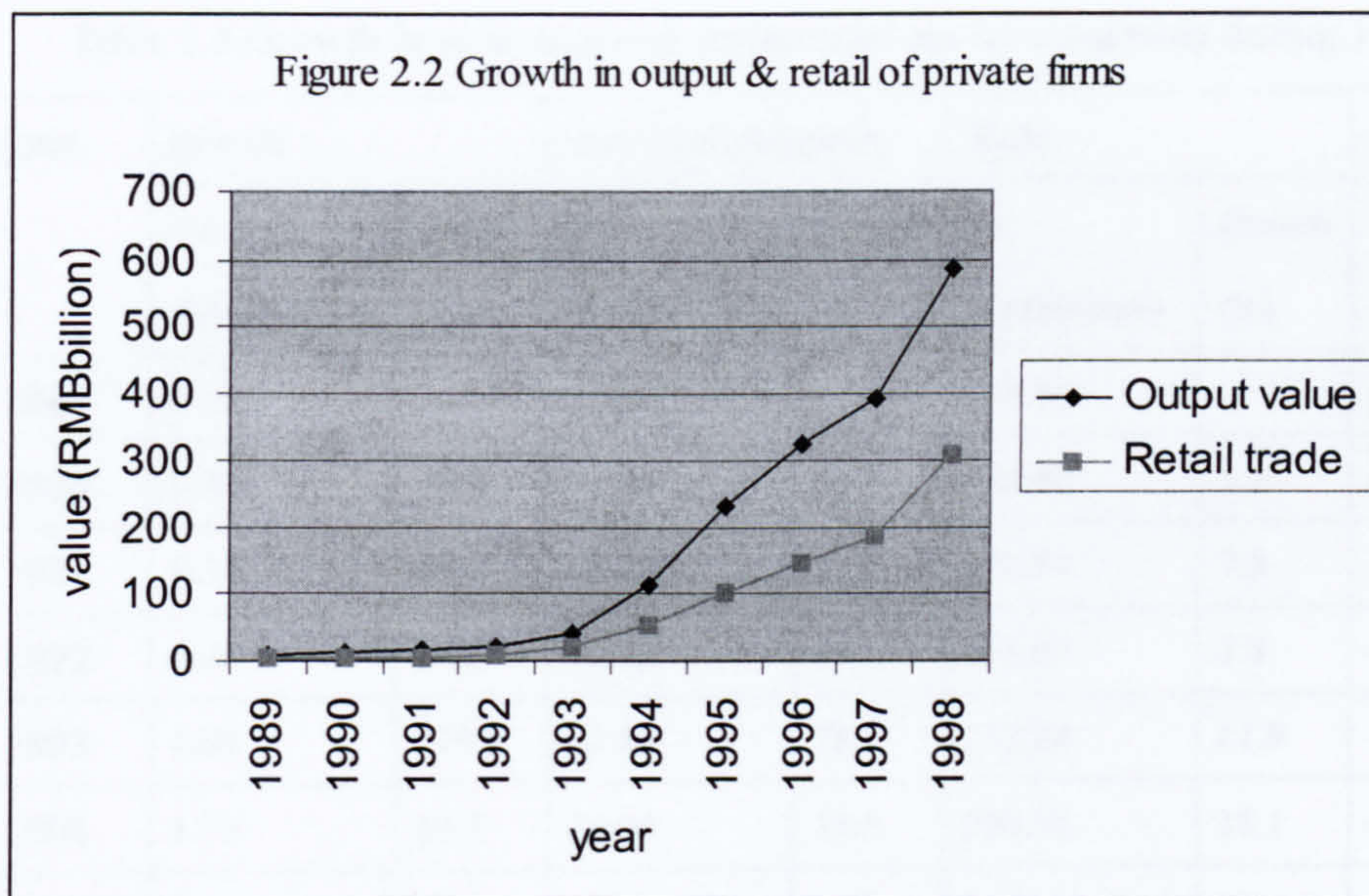
2.2.4. Growth in output and retail trade

The rapid development of private enterprises is also indicated by the growth in output and retail trade. From Table 2.5 and Figure 2.2, it can be seen that the output and retail trade of private enterprises grew rapidly between 1989 and 1998. In 1989, the output of private enterprises valued RMB 9.7 billion, and grew on average 51.9 per cent a year provided price factor considered, amounting to RMB 585.3 billion. During the same period, the retail trade of private enterprises grew from RMB 3.4 billion to RMB 305.9 billion at average annual rate of 57.2 per cent.

Table 2.5 Growth in output and retail trade of private firms during 1989-1998

Year	Output value (RMBbillion)	Growth (%)	Retail trade (RMBbillion)	Growth (%)
1989	9.7		3.4	
1990	12.2	23.7	4.3	23.4
1991	14.7	17.6	5.7	29.2
1992	20.5	34.1	9.1	53.3
1993	42.2	92.7	19.0	94.1
1994	114.0	148.4	51.3	145.9
1995	229.5	86.5	100.6	79.0
1996	322.7	34.5	145.9	36.7
1997	392.3	20.8	185.5	24.3
1998	585.3	51.8	305.9	65.7
Average growth		51.9		57.2

Source: *Statistical Documents of China Industry and Commerce Management, 1991-1998*



2.2.5. The contribution in industrial and commercial tax

The rapid development of private enterprises is also reflected by the growth of the industrial and commercial tax they contributed. Table 2.6 gives the details of the growth in industrial and commercial tax for private enterprises and the comparison with other ownerships. Starting from low base of RMB 0.11 billion contribution of industrial and commercial tax in 1989, private enterprises provided RMB 9.05 billion in 1997. Although the amount itself was still small, the average annual growth rate of 73.2 per cent was much higher than those of SOEs and TVEs.

Table 2.6 Growth in industrial and commercial tax by ownership during 1989-1998

year	private		Individual economy		State		Collective	
	Tax (RMBbillion)	Growth (%)	Tax (RMBbillion)	Growth (%)	tax (RMBbillion)	Growth (%)	tax (RMBbillion)	Growth (%)
1989	0.11		11.96		127.85		43.13	
1990	0.20	78.6	13.20	10.3	134.92	5.5	42.68	-1.0
1991	0.34	69.0	15.08	14.2	144.70	7.3	44.11	3.3
1992	0.46	34.6	17.66	17.2	155.92	7.8	47.81	8.4
1993	1.05	129.9	31.50	78.2	252.24	61.9	83.71	75.1
1994	1.75	67.5	36.04	14.5	298.10	18.1	81.10	-3.1
1995	3.56	103.1	40.13	11.3	329.48	10.5	96.94	19.5
1996	6.02	69.2	39.78	-0.9	295.93	-10.2	99.60	2.7
1997	9.05	50.2	46.05	15.7	386.49	30.6	105.23	5.7
Average growth		73.2		60.8		14.8		11.8

Source: *China Tax Yearbook, 1990-1998*

All the above have demonstrated the rapid development of private enterprises. They have also proved the contribution of private enterprises to the Chinese economy. The importance of private enterprises is more clearly reflected in the following facts. Firstly, while the SOEs, TVEs, and FDI have stagnated (e.g., Warner, 1995; World Bank, 1997; Cauley *et al.*, 1999; *Chinaonline*, 31 May 2000), domestic private enterprises continue to grow rapidly. The private sector has become the main engine of Chinese economic growth (*Financial Times*, 20 July 1998; *China News Digest*, 23 March 1998; *South China Morning Post*, 19 March 1998). Secondly, the performance of private enterprises has been a main catalyst for SOE reform. The Chinese government have addressed the enterprise reform in terms of

property rights and ownership, which opened the door for the transformation of SOEs. A survey (*People's Daily*, 30 July 1998) shows that 62 per cent of private entrepreneurs are eager to buy SOEs to expand their scale of production and economy. Thirdly, all levels of government have started to abandon discrimination against the private sector, allow individual and private economy to compete fairly and develop together with state owned and collective economy, and they have also initiated many policies designed to foster the growth of private economy. (*China News Service*, 8 December 2000). In addition, the government will allow private enterprises to enter most industries that used to be controlled by the SOEs. This produces many new opportunities for private enterprises (*China Securities*, 12 November 2000). Definitely, the output value of private sector is becoming larger and larger, and the role of this sector is becoming more and more important.

2.3 Obstacles to the development of private enterprises

The development of private enterprises is a history of struggle--to overcome opposition and obstruction, survive and grow. Since the promotion of private economy conflicts with the ideology of communism, the growth of the sector was not easy. The barriers come from discrimination from both people and government.

Firstly, people were hostile to private enterprises. The attitude of people may derive from the marginal status of the sector itself in the hierarchical ownership structure, where state comes first, collective second, and the private goes no where (Lin and Bian, 1991, p658).

The initial composition of private business people from marginal social groups, including former prisoners, was another factor contributing to the low social status. Kraus (1991) argues that the hostility to private enterprises was due to not only traditional social hierarchies and political prejudice but also envy of the wealth of the private business people.

Secondly, there are restrictions imposed by the government. The size and business scope of an enterprise were controlled by the government. Private business was not allowed to compete with collective and state owned enterprises. In the planned economy, business premises, labour, raw materials, energy, etc., were allocated by government, private enterprises, excluded from the plan, often found it difficult to obtain these resources (Kraus, 1991; Young, 1995; Wank, 1999). Local government officials often used their control over key inputs as leverage over private enterprises, and also they could block licenses or approvals, cut off access to credit, and add new restrictions on private enterprises' activities (Odgaard, 1992). Moreover, when the government carried out austerity policies, private enterprises were always the target. It was estimated that 15 per cent of private businesses (including individual economy) were driven out of business in 1989 alone (*China Daily*, February 28, 1991).

Thirdly, exorbitant levies and sundry taxes become burdens to the private enterprises, which are regarded a source of government revenues rather than explicit taxes (II and Rose, 1998). These charges are numerous. According to Bruun (1993, p260) there were all

together 20 charges levied on one private restaurant in Chengdu city: industrial and commercial tax, income tax, city reconstruction charge, education charge, city grain fund, provincial grain fund, meat fund, management charge, business administration charge, revenue stamp tax, public order charge, sanitation charge, energy source fund, front-door-cleanliness-guarantees, clean transportation charge, association membership fee, employees' contract charge, and excessive signpost charge. Odgaard (1992) only finds only two of the dozens of charges on private shops, the income tax and the industrial and commercial tax, were imposed by the central government. Many charges are levied by the discretion of local governments.

Fourthly, private enterprises' start-up and capacity for survival and growth are constrained by lack of capital! In the West, capital becomes manageable when an enterprise develops to certain stage. However, in China, capital is not easy to access for the private enterprises at any stage of growth. According to David Machenzie, chief of mission for the International Finance Corporation's China operation, the major restriction for the development of private enterprises is a lack of efficient funding channels. Liu Yong Hao, vice chairman of All China Industry and Commerce Federation, who also runs China's largest feed producer the New Hope Group, confirmed that many private enterprises have difficulties getting funds from banks⁴. The state commercial banks are usually reluctant to

⁴ In June 1999, the Industrial and Commercial Bank, China's biggest lender, reported that 21% of its loans were held by non-state enterprises. But the majority of this was lent to collective and foreign-invested firms. Individually owned and private enterprises shared a minute 0.5% of the funds. Credit managers at the big four state-run commercial banks are still pressured by the government to lend to SOEs. When they do lend to private firms, it is only for the safest projects (*the Economist Intelligence Unit*, 21 September 2000).

lend to private businesses out of concern about their trustworthiness and repayment capability. Fang Haixing, general manager of the Group Co-ordination Committee of China Construction Bank, also admitted that China's banking sector lacks a tier of institutions offering loans for projects in the private sector, on which commercial banks do not want to take the risk. He thus suggested that real private owned banks become a key to the solution, "Only they can understand the real need of the private enterprises" (*AFX*, 27 April 1999; *China Daily*, 2 May 1999). Even in one of the major cradles of private economy, Zhejiang Province, private enterprises are still facing difficulties in financing. The chairman of a private group corporation remarked, the lack of a high-technology risk fund has become a big obstacle to the drive for private enterprises to step in the high-technology industries, because such a risk fund for non-state enterprises exists nowhere in China (*China Daily*, 20 December 1998).

Walder (1991) points out that state banks and official sources of credit generally offer loans more on the basis of political consideration than economic ones. Private enterprises lack the legitimacy and necessary political backing to enjoy reliable access to capital and thus must depend on private and informal sources of credits, which are limited and are available only at substantially higher interest rates.

Although foreign investors, including venture capital investors, have become increasingly interested in the prospects of private enterprises, not until September 1998, did the International Financial Company, a World Bank member, become the first foreign investor

who provided the first loan of US\$6.5 million to a Chinese private company (*China Reform News*, 11 September 1998). It was the first time that private enterprises were allowed to attend the China Fair for International Investment and Trade held in September 1999. However, “(Although) the Ministry of Foreign Trade and Economic Co-operation (in charge of the fair) has not set down any explicit discriminatory policies against private businesses regarding their co-operation with foreign investors, private companies have received unequal treatment in the actual implementation of the foreign investment policy”, claimed Maochun He, deputy director of the World Trade Research Department of the Chinese Academy of International Trade and Economic Co-operation (*China Daily*, 11 April 1999).

Another important capital source is the stock market⁵. In the market economies, stock markets work as a mechanism to allow capital raised for enterprises and a more rational allocation of resources. They channel savings to their most efficient users and act as a pressure for raising firm efficiency. However, according to Dong (1999), China’s stock markets have another important function, that is, serving SOEs reform. Bowles and White (1992a, 1992b) find that in China, bonds and shares have functioned as one instrument in a complex struggle for resources between political, institutional and economic actors. Meanwhile, share issues have in the event been economically unimportant but political important, because they challenge the ideological and institutional underpinnings of a “socialist” economy—ownership. Predictably, most companies listed in the Chinese stock

⁵ China opened its first bourse in Shanghai in December 1990.

markets are state owned and few are non-public. Dong (1999) therefore advocates that more private enterprises should be treated equally without discrimination and allowed to enter stock markets.

China has yet to enact any laws to help finance the private sector, though according to *China Security News* (23 January 1999), the Financial and Economic Committee under China's legislature the National People's Congress (NPC) has planned to submit a draft private enterprise and investment laws to the NPC. The ministry of Finance has begun to draft measures to require local government to set aside part of their budgets as financial guarantees for loans extended to the enterprises in private sector (*China Daily*, 2 May 1999), but the aftermath has not yet been seen.⁶

In sum, all these reflect the difficult conditions for the private sector. As a strategy to outweigh these disadvantages, private entrepreneurs were forced to operate their business under the guise of collective or state enterprises. A survey conducted by the State Industry and Commerce Bureau reveals that 80 per cent of TVEs were in fact private enterprises (*China's Private Economy Yearbook*, 1996). Also, many private entrepreneurs are forced to

⁶ According to *South China Morning Post* (24 July 1999), by May 1999, about 18 provinces and regions had tried the experiment of establishing a credit-guarantee system, but the aim was quoted as "to help small and medium-sized enterprises solve their financial difficulties", instead of private businesses. In terms of size, most of the private enterprises are small and medium. However, compared with the huge number of the dominated publicly owned enterprises, they are "small ethnic minorities".

People's Daily (16 June 1999) seemed to try to propagate such cases that supported private businesses. It reported a magic result of financial injection to a private firm: in April 1999, Fuan City set up the first credit-guarantee company in Fujian Province to help private enterprises. In two months, it helped 24 funding-hungry private enterprises to borrow loans from commercial banks. With loan backing, one private company's monthly output doubled.

cultivate personal connections (*guanxi*) with government officials or state owned enterprises managers for favours. To maintain such connections, the private entrepreneurs have to pay good prices and gifts, and sometimes, even commissions and bribes (Young, 1995; Wank, 1999, Zhu, 1998; Tao and Zhu, 2001).

2.4 Cadres have advantages in private enterprise start-up?

As pointed out in the aforementioned chapter, it is open to question whether being a cadre provides advantage in private business operation. Some argue that being a cadre helps entrepreneurs to start their businesses in East Europe (Staniszki, 1991; Rona-Tas, 1994; Clark, 2000). But some oppose this argument (e.g., Hanley, 2000). It is impossible for this limited research to examine every aspects listed above. This research looks at the most critical stage of business operation, start-up.

Private enterprises largely started their economic activities as individual or family firms (*getihu*)⁷, which were operated by those in disadvantageous positions, such as those eliminated from the normal work system (Kraus, 1991). Also, more and more private enterprises are being registered as such at start-up, after the legal status was granted to private enterprises, in particular after Deng Xiaoping's Southern Tour in 1992. People

⁷ As a result of adjusting to the market and of their growth, the firms have advanced to a point where more than seven workers were required to fulfil production goals. Some families, so called specialised households (*zhuanyehu*), were indeed private non-agricultural businesses and extended far beyond the scope previously supposed possible for private economic activity. According to a survey conducted in 1984 by the Rural Development Research Centre under the State Council, 0.07 per cent of the investigated households had already hired more than seven workers (cited in Zhang and Ming, 1999, p234). It was estimated that by the end of 1988, there were about 500,000 individual economy (*getihu*) that could be counted as private enterprises (Zhang and Liu, 1995, p55).

continue to invest their savings, say, from moonlighting, or borrow money from friends, relatives, to set up their own firms. In 2000, there were 295,300 new private enterprises, which means an average of 809 new private enterprises every day in the country (*China Business Times*, 30 March 2001).

Legal leasing⁸ of public owned enterprises has led to the asset accumulation of individuals. In some areas, 50 per cent of the total collective firms were leased to individuals (Zhang and Liu, 1995, p29).

According to some research, the start-up capital of private enterprises derives from public assets. For example, some private entrepreneurs who were born in cadre families, their business start-ups were financed by public funds, either by bank loans from state banks or as money from public units (Wank, 1999). A state owned firm manager is more than pleased to take bribes from non-state trade partner in exchange for enforcement of contract between the two parties (Tao and Zhu, 2000, 2001). Also, the dual price system⁹ introduced in the early 1980s provided a new way for corrupt officials to milk state property. These “personal savings” became the start-up capital. This can be true in the

⁸ According to Shen et al (1996), there are three types for leasing collective firms: total capital leasing, partial capital leasing and intangible capital leasing. In the last category, a collective firm only “leases” its intangible capital, such as firm title, business license, and credit. One collective firm leased its trademark for an annual payment of RMB 10 thousand.

⁹ The gradual Chinese strategy for moving from economic planning to a market system, which includes 1) opening the free market while keeping state supply unchanged at the (lower) plan price; 2) adjusting the plan price incrementally over time to approach the market price. The supply offered at the plan prices is normally fixed by quota, if not reduced, over time.

beginning of reform, given the absence of a well-built legal system preventing public assets from going to private pockets.

In fact, how private entrepreneurs start up their business is not the main concern of the existing research. However, putting these accounts together, we have some ideas about different paths to start-up private enterprises. From the sparse research mainly based on small case studies, it is still ambiguous who these people are and how they start up their businesses, in particular whether being a cadre makes the advantage in start-up. To fill this deficiency, the next chapter will analyse a large national survey data on China's private enterprises in 1995. It will focus on how private entrepreneurs with different backgrounds financed their business start-ups and whether there are differences between entrepreneurs with and without cadre background in terms of business start-up capital and the main sources of their start-up capital.

Part 2 Theories

Chapter 3 The advantage of being a cadre or having close cadre connections in financing business start-up? A survey analysis on China's private enterprises

This chapter tests the dominant theory of power conversion suggested by some social scientists presented in Chapter 1. Firstly, it examines the concept of cadre in China and gives a clear definition of cadre in this research for the purpose of analysis. Then, based on a national survey data set on the Chinese private sector, the social background of the entrepreneurs, their social relations, start-up finance and the main sources of start-up finance are examined. In order to find out whether being a cadre or having close cadre connections has any advantage at business start-up, the association between the entrepreneurs' background and their start-up finance is explored. Lastly, this chapter offers some explanations for the finding.

3.1 What are cadre and *nomenklatura*?

According to the available research on post-communist societies presented in Chapter 1, the social background and social relations of private entrepreneurs are paramount to the success of their business operation. Backed by cadre experience or cadre family background, their businesses tend to be more successful. Before going into further investigation, one key question must be answered: What are cadre and *nomenklatura*?

Clark (2000) confines his informants to *nomenklatura*, but he does not provide a clear

definition of *nomenklatura*. Instead, he describes what positions the five informants held before the communist regime collapsed. To Clark's (2000, p441) understanding, *nomenklatura* is another term for cadre, which can refer to a very high position, such as a member of the Politburo in Prague in the late 1980s, and also to a low position as "a junior Party member in a middle management position organising holidays and outings for colleagues". To Rona-Tas (1994, p53), the category of former cadre in Hungary includes not only someone at the very top of the communist hierarchy but also everyone who formerly joined the Hungarian Socialist Worker's Party and reached some position of power. Similarly, Hanley (2000, p145) labels cadres in Eastern Europe as individuals who occupied positions of administrative authority during the state-socialist period.

Gazso (1992, p77) defines *nomenklatura* as persons in leading positions, related to the uppermost circle of the party elite, or the main possessors of political power--the executive, the mass organisations and the economic administration. Based on the data from the Hungarian National Statistics Office, the term applies to cadres ranged from central to capital city to county level. To Hanley (2000, p145), "*nomenklatura* lists" for the communist parties in Eastern Europe consisted of those positions that required approval by the central Committee before they could be filled.

Harasymiw (cited in Manion, 1985, p215) gives a broader concept of *nomenklature* and argues that the Russian term *nomenklatura* means a list of positions, arranged in order of seniority, including a description of the duties of each office. It generally refers to the lists

of offices controlled by the various communist party committees. In the glossary of the Soviet Union, the Library of Congress (1997) gives the definition of *nomenklature* as follows:

The Communist Party of the Soviet Union's system of appointing key personnel in the government and other important organizations, based on lists of critical positions and people in political favour.

It also refers to the individuals included on these lists.

While in the glossary of Hungary, the Library of Congress (1997) slightly changes the definition of *nomenklatura* as

From the Latin *nomenclature*. This Russian word denotes an enumeration of important positions and the candidates who are examined, recommended, and assigned to fill them by communist party committees at various levels.

Therefore in the aforementioned research, *nomenklatura* commonly refers to individuals in leading positions of the communist regimes. In other words, leading cadres are *nomenklatura*.

Unlike the common understanding of cadre and *nomenklatura* in Eastern Europe, cadre in China is a confusing term. Probably because of the ambiguity of the term, the research on China's private sector does not give a clear definition what the cadres are. Nee (1989, 1991) does not provide the definition of cadre in his analysis on the survey data on private family

farms in Fujian province in China. Wank (1996) does not clarify what cadre is, either. Then, Wank (1999, p117) uses a term “functionaries” to categorise persons previously employed in public units in white-collar positions, as if this referred to cadres, which is not appropriate. When describing the entrepreneurs’ fathers’ occupations, quite unbelievably, he even counts officials of Kuomintang (the Chinese communist enemy) in cadre category. Perhaps confused by the term, though Odgaard (1992) mentions that cadre category in China is very broad, he does not give a definition for cadre.

Apart from the aforesaid research, many researchers do not define explicitly what cadres are or who cadres are when researching China (e.g., Seymour, 1989). Indeed, cadre is a very broad term used in China. It is sometimes understood as a social class. For example, according to Li *et al.* (1991), in China’s social structure, cadres are the leading class in the social hierarchy, followed by workers and peasants, with peasants on the bottom. Under the Chinese communist regime, the social classes are stratified through three major systems: the household registration (*hukou*) system¹⁰, the unit (*danwei*) system¹¹, and the

¹⁰ The *Hukou* (household) registration system originally came from political and social control, as a critical Chinese communists’ response to dilemmas inherent in China’s development strategy under condition of labour surplus and capital shortage in a predominantly agrarian society in the 1950s. It divides the whole population into two statuses: urban resident and rural resident. Urban residents are the state’s direct responsibility. The state must supply urban area with employment, housing, food, transportation, medical facilities, schools and many other essentials and amenities of life (e.g., Cheng and Selden, 1994; Lu, 1993). The Chinese government has been reforming the system.

¹¹ A work unit is called a *danwei* in Chinese. Whether it be a government department, factory, research institute, or university, the work unit is a microcosm of the Chinese society with its own political hierarchy, networks of personal and professional relationships, services, and, in many cases, living quarters. Together with the Hukou system, the *danwei* system came into being since 1950s as a social control mechanism. It is through the work unit that the Chinese government exerts its influence on the life of the individual, for it is the unit issuing the identification card that marks the bearer as a working member of Chinese society. The unit provide social benefits, such as medical care, and housing (e.g., Lu, 1993). Not until recent years, were the necessities of daily life for a person provided by a unit he or she works.

hierarchical administrative ranking (*jibie*) system. The state has the mandatory power of distribution of resources and social positions, which determine the three classes, cadre, worker and peasant.

On the other hand, cadre is also defined as someone in certain leading positions. For example, Burns (1985) counts all members of basic-level leadership organisations as local cadres. The basic-level leadership organisations include commune (*gongshe*) or township, brigade (*shengchan dadui*) or village (*cun*) management committees, the party branches, the village and party assemblies, and also production team (*shengchan dui*) management committees. Each basic-level leadership organisation, consisted of a hierarchy of authority extending from commune leaders to production team officials, could have numbered four to five hundred members. In his revised paper, Nee (1996, p922-923) defines cadre as holding positional power in local government. All the various ranks of cadres comprising the local administrative elite, from county level officials down to cadres in the natural village, are cadres.

Cadre is termed *ganbu*¹² in Chinese. According to Vogel (1967), in China, cadres firstly

¹² According to Strauss (1999), some state that *ganbu* came into Chinese via the Japanese term *kanbu* (a word in which the kanji is identical to the Chinese characters); while a number of other sources, insist that the term came into China through the Soviet Union. However, all sources agree that the word *ganbu* originates with the French *cadre*, since the Japanese term *kanbu*, in turn, had its origins in the French “*cadre*”. In Russian, the term “*cadre*” connotes “core group” and also “personnel” in the general plural as opposed to an individual. The Library of Congress (1997) defines *cadre* as

Organized group of party activists. A party member who holds a responsible position (usually administrative) in either the party or the government apparatus. In a more restricted sense, a person who has been fully indoctrinated in party ideology and methods and uses this training in his or her work.

emerged in the Guomintang of Sun Yat-sen in the early 1920s. In the communist revolutionary movement, the new type of leader, the ascetic, fearless and disciplined fighter-ideologue, came into its own. A cadre was not an ordinary peasant or worker, but a leader who committed to the cause of communist revolution and moved among the masses to build a revolutionary organisation. When the Chinese communists succeeded and took over power, the role of cadres began to undergo a fundamental change in order to cope with the many complex administrative matters confronting the nation, which required literacy and administrative skills other than fearlessness and bravery. Administrators, scientists, technicians and other specialists joined the cadre contingent. The cadre became a bureaucrat. Prior to 1949, all cadres had been communist party members. However, after 1949, many government cadres were neither party members nor Youth League members.

Cadres are recruited from several channels in China. Firstly, cadres currently available can be re-assigned, who are either army men transferred to civilian work, or graduates of universities, colleges, and technical secondary schools. Secondly, workers in state owned or collectively owned enterprises can be chosen as cadres. Thirdly, people from society at large can also have the opportunity to be recruited, but the opportunities are confined to those who are mainly urban educated youth, unemployed specialised and technical persons, and people with skills acquired through study on their own. The main criteria are loyalty to the communist party, the education background of a senior secondary school graduate or above, and being around twenty-five years old of age (Manion, 1984).

The Chinese Communist leadership began to standardize the term around a much broader set of connotations than existed in Russian in the late 1930s and early 1940s.

Thus in China, the broadly used term cadre carries two different meanings. One cadre concept encompasses all personnel with authority or expertise in Party, state, army, or units of economic production, be they Party members or not (Strauss, 1999). Cadres considered on this basis include the following personnel in government, Party, business enterprises and service establishments: (1) employees from clerical personnel and above (including platoon chief and above among policemen and firemen; non-labouring foremen and above in industry, building, installation and construction work; and shift chief and above in postal and telecommunications work); (2) industrial technicians; (3) agro-technicians; (4) technicians working on the seas; (5) public health technicians of middle level and above; (6) scientific technicians; (7) news and publishing personnel; (8) teaching personnel; (9) personnel in culture and the arts; and (10) translators (*China Labour Statistical Work Handbook*, 1958, cited in Vogel, 1967, p50).

In this version of the cadre concept, the term cadre is mainly understood as experience or social status. It covers occupations in government organisation, the communist party and other organisations, as well as people who work as administrator and management in state entities.

This version of the cadre concept may not be a good variable to indicate advantageous social position, as it does not give information about the power of different positions in the hierarchy, neither does it provide any information in the power of allocating resources. The broad usage of cadre to describe the social origin of the entrepreneurs may have concealed

the fact of the advantage of being cadres or having connections with cadres.

The other concept of cadre is defined as someone reaching some position of power (e.g., Burns, 1985), as many people refer to anyone in a position of power as a “cadre” (Manion, 1985). Rona-Tas (1994) regards the category former cadre not only someone at the very top of the communist hierarchy but also everyone who formerly join the Hungarian Socialist Worker’s Party and reached some position of power. In line with this account, **a cadre in this thesis is defined as someone reaching certain position of power. The cadre category includes not only someone at the very top of the communist hierarchy but also everyone who reached some position of power, ranging from chief prefecture and county level officials down to village heads, who clearly have certain power of allocation of resources.**

To date, analysis about the Chinese private sector based on nation-wide data is not available. Both Bruun (1993) and Wank (1999) carried out research in private commerce business, while Nee (1989, 1991) pays attention to private farming. The existing research only examines private enterprises in a single sector in a certain region. The following analyses fill the gap. By using a national survey data on private enterprises, it looks at what these entrepreneurs are in terms of their background and social relations. More importantly, it attempts to find out if being a cadre or having close relationship with cadres renders advantage in private business start-up in China.

3.2 Source of the data

The following analysis in this chapter is based on “The 1995 National Survey on Private Enterprises and their Owners in China”. The survey was mainly designed by the social scientists from the Sociology Institute of the Chinese Social Sciences Academy and Beijing Academy of Social Sciences. China Society of Private Economy Research (CSPER)¹³ organised the survey, with researchers at local Federation of Industry and Commerce trained as interviewers.

A sample of 3,025 cases was selected from a total of 432 thousand private enterprises registered with the bureau of industry and commerce by the year-end 1994. Based on the register, a probability proportional to size sampling procedure was utilised according to the provincial, urban/rural, and sectoral (industrial) distributions of the private enterprises in the country. Firstly, a proportion quota of enterprises was allotted to each province. Then, within each province, at least three cities and three counties (for province with 10,000 or more registered private enterprises, at least six cities and counties) were randomly selected. In each selected city or county, enterprises were divided into clusters according to urban/rural location and industrial categories. Enterprises were selected from each cluster until the share was met, and at least one enterprise was selected from each cluster. For

¹³ . It is supposed to be a non-government academic organisation, which aims at doing theoretical and practical research on the private economy. Mainly advocated by people from the Chinese Academy of Social Sciences, the Department of United Front Work (DUFW) of CCP, State Industry and Commerce Administration in 1988, it was finally set up in 1993 by All China Federation of Industry and Commerce (ACFIC). The current chairman is a former vice chairman of ACFIC and vice minister of DUFW. It has offices in the building of ACFIC (See Brief Introduction of CSPER, *Yearbook*, 1996:247).

example, out of the 432 thousand registered private enterprises by 1994, 181 thousand, or 42 per cent of the total, were located in the countryside, and 251 thousand, or 58 per cent of the whole sample, were located in urban areas. With the fixed rural/urban ratio, out of the sample of 3,025 cases, 1,261 enterprises from the countryside and 1,764 from urban areas were selected accordingly.

Table 3.1 the Industrial distribution of private firms

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	agn	116	4.0	4.1	4.1
	mining	38	1.3	1.3	5.4
	manufacture	1127	39.3	39.8	45.2
	electri	21	.7	.7	46.0
	construct	161	5.6	5.7	51.7
	Irrigate	1	.0	.0	51.7
	transport	76	2.6	2.7	54.4
	commerce	767	26.7	27.1	81.5
	finance	5	.2	.2	81.7
	estate	17	.6	.6	82.3
	social service	218	7.6	7.7	90.0
	health	13	.5	.5	90.4
	education	11	.4	.4	90.8
	research	72	2.5	2.5	93.4
	other	188	6.6	6.6	100.0
	Total	2831	98.7	100.0	
Missing	System	38	1.3		
Total		2869	100.0		

The industrial distribution of private enterprises is shown in Table 3.1. Private enterprises are mainly in manufacturing (40.4 per cent), commerce (27.4 per cent), social services (7.2 per cent), construction (5.5 per cent), agriculture (4.1 per cent), and transportation (2.4 per cent).

In May and June of 1995, the survey design and sampling procedure together with training

of the interviews were accomplished. From July to September of 1995, face-to-face interviews were conducted with private enterprise owners randomly selected from 334 counties and urban districts out of all the 30 provinces, autonomous minority regions, and municipalities. Interviews were successfully completed for 2869 firms with their owners (private entrepreneurs hereafter), yielding a final response rate of 94 per cent.

The survey investigated both the private enterprises and the entrepreneurs. Enterprise situation includes the capital, employment, profit, internal organisation and the management of the private enterprises. In the aspects of the private entrepreneurs, their social mobility, social relations, family properties, political background, social status and social attitude (class-consciousness) were investigated.

It is noted that there are some limits to the survey. For example, the sample was designed to ensure representativeness, but in reality, the rural/urban and sectoral distributions of the private enterprises vary across provinces. On the other hand, applying national ratios might have narrowed the variability and possibly the representativeness of the sample; over-representation of large enterprises is another problem, which is due to the natural inclination towards the boosting of local industry and commerce bureau officials, who tended to pick their biggest and best private enterprises.

Based on the survey, this research aims to find out whether the social origins and social relations of private entrepreneurs provide them with any benefits in business start-up. Thus,

only the relevant variables are described and the relationships explored, the irrelevant variables are not presented here.

3.3 Relevant variables

As suggested by the available literature, different business outcomes show the importance of cadre experience or cadre family background. Businesses operated by cadre or cadre-related entrepreneurs seem to have better access to start-up capital, and be more successful than non-cadre background entrepreneurs. The survey has five main variables to depict the social background and the social relations of an entrepreneur: 1) the position of the entrepreneur's father, 2) the position of the entrepreneur before business start-up, 3) the position the entrepreneur's spouse, 4) the position of the entrepreneur's closest relatives, and 5) the position of the entrepreneur's closest friends. The variables are what the theorists of power conversion thesis utilise (e.g., Rona-Tas, 1994; Clark, 2000).

In business operations, financing at start-up is critical. To the Chinese private enterprises, financing is most paramount, as it is difficult for them to access capital¹⁴. Therefore, financing is a best indicator to examine if cadre related entrepreneurs have an advantage in business start-up. For start-up financing, variables used are: 1) the registered capital at business start-up; 2) the real assets at start-up; and 3) the main sources of start-up capital.

If cadre related entrepreneurs have advantage in start-up, they should be more likely to

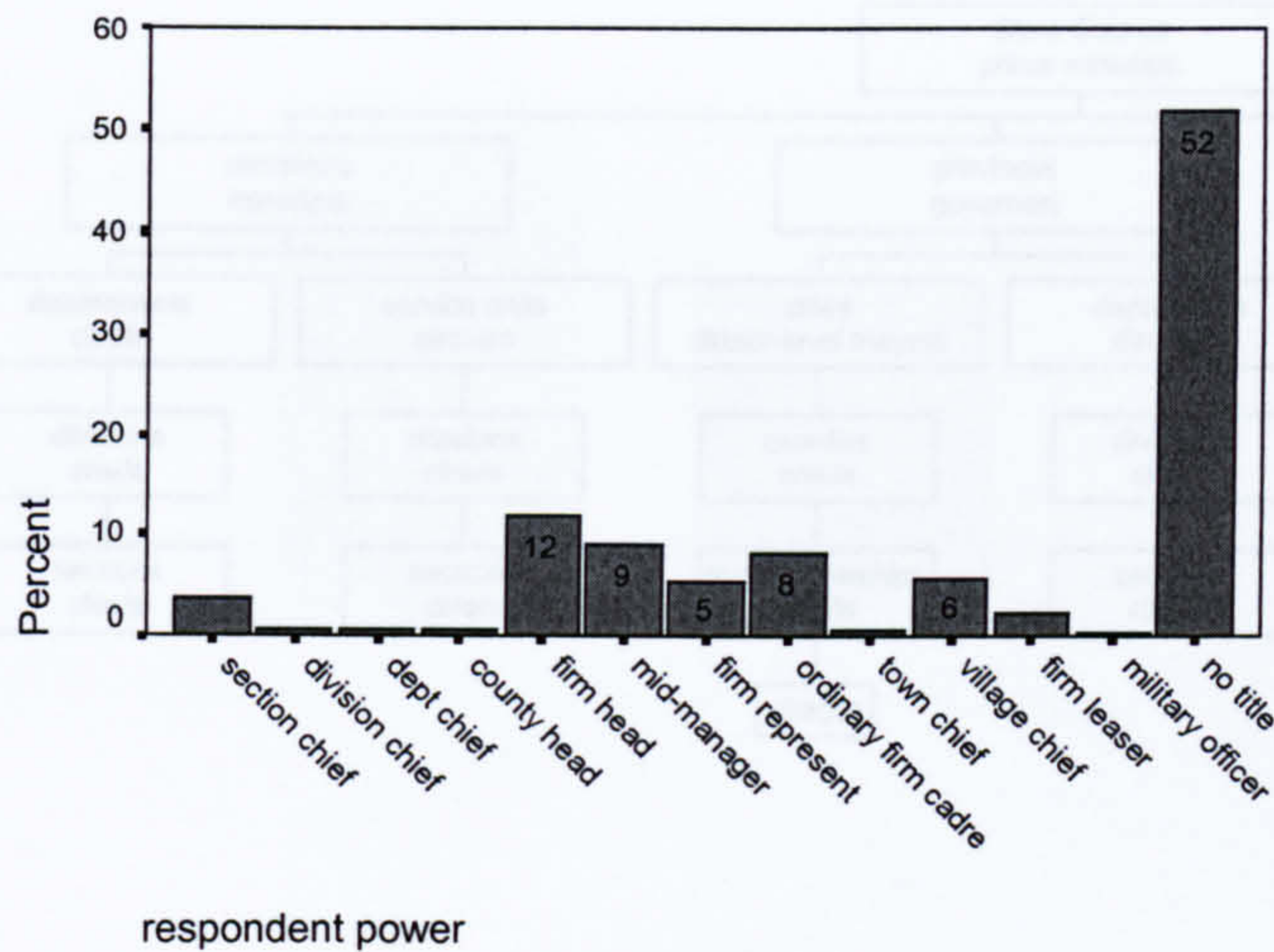
¹⁴ See Chapter 2 for more detailed description about the adverse financial environment for private business.

have higher amount of registered capital and real assets in any given industry at the beginning of business. In other words, entrepreneurs with cadre background should stand in the groups with more registered capital and real assets at start-up, in particular, they should be more likely to have the highest registered capital and real assets. They should also be less likely to have lower than average registered capital and real assets at start-up. Furthermore, as the power conversion theorists suggest, resources controlled by the state can be transferred by cadres to the primitive accumulation that stimulates business start-up, since no one has money after decades of socialism. They should be more likely to rely on public finance, such as bank loans, for their start-up capital (e.g., Wank, 1999; Clark, 2000).

It is noted that many factors have influences on the start-up financing of the private enterprises, such as government policy, location, finance, and education of the entrepreneurs, etc. However, this research doesn't aim to build up a model to examine the functions of each factor. Instead, it hopes to find out if there is correlation between the start-up capital and the related social background variables.

3.4 The entrepreneurs' background before start-up

Figure 3.1.1 respondent's power

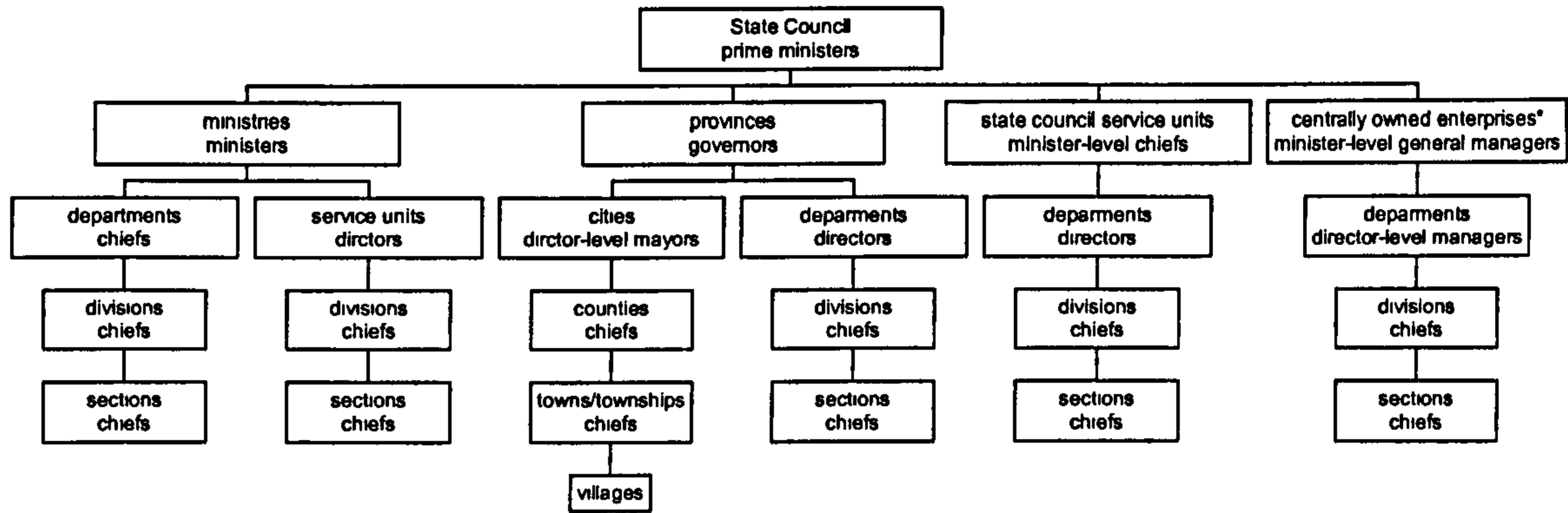


Many interviewed entrepreneurs had been either enterprise managers (11.3 per cent) or

Figure 3.1.1 shows that the entrepreneurs come from a variety of social origins. Some of them used to work in government or party organisations and many of them have been enterprise managers. In the government and party line, 4 per cent of the entrepreneurs had been a section chief or town chief; about 1.7 per cent of the entrepreneurs used to be division chiefs or equivalences or even in higher positions. In addition, 5.7 per cent of the entrepreneurs had been village chiefs before setting up their private businesses. 52 per cent of the entrepreneurs had “no title”, which means they had no power in the official power structure. The hierarchical structure of the Chinese government system is demonstrated in Figure 3.2.

Figure 3.2

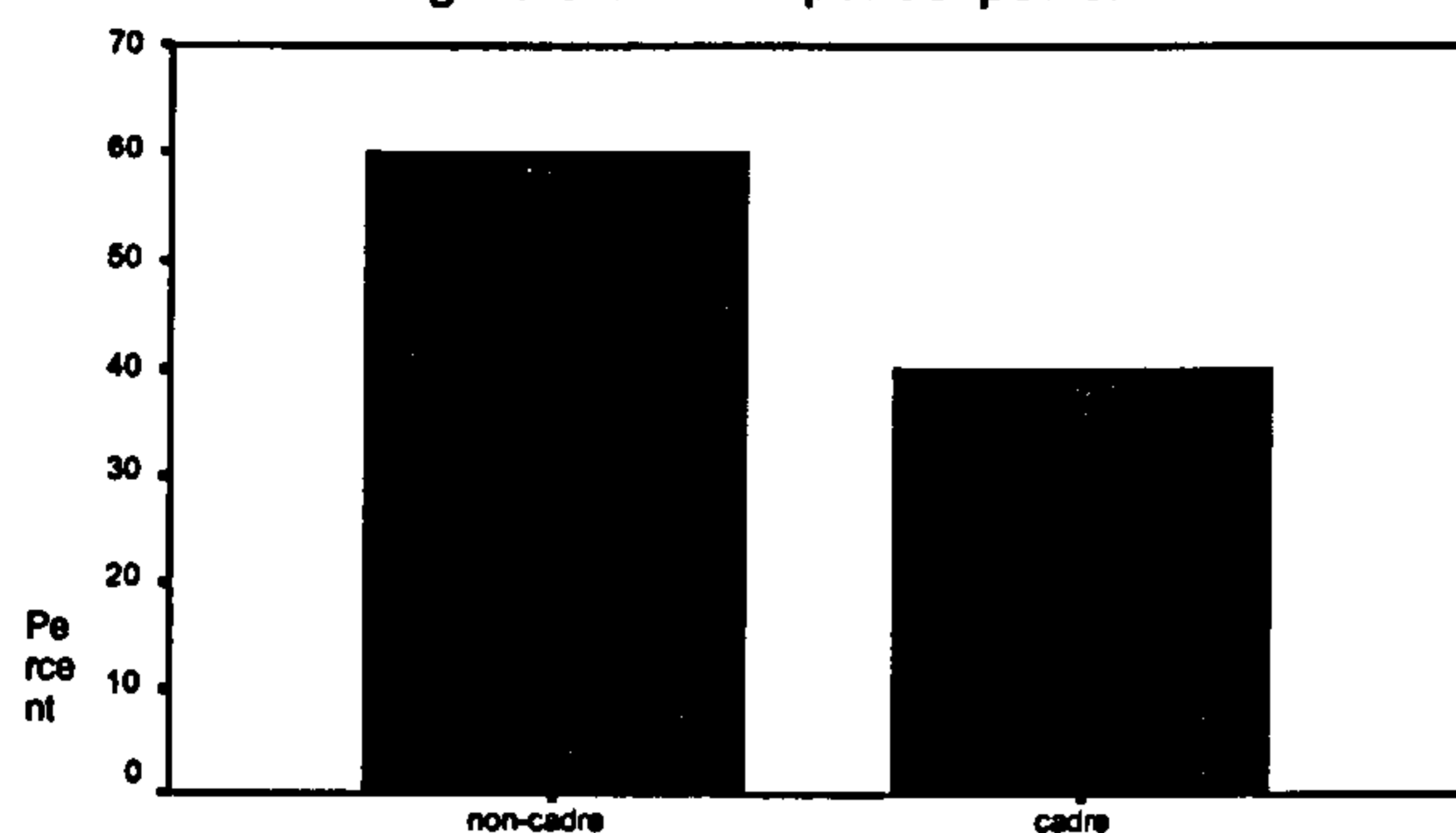
The Chinese government hierarchical ranking structure



Many interviewed entrepreneurs had been either enterprise managers (11.8 per cent) or middle managers (8.9 per cent) or enterprise procurement and supply representative (5.3 per cent). About 2.3 per cent of the entrepreneurs were state or collectively owned enterprise leasers. All the entrepreneurs in these categories¹⁵, 40 per cent of the entrepreneurs, had certain powers in terms of the allocation of resources in the planned economy. They were thus cadres as defined previously in this thesis, which refer to anyone in a position of power (Manion, 1985; Rona-Tas, 1994). Under such a definition, 60 per cent of the entrepreneurs, who were either in non-power positions or had no titles of descriptive power (Figure 3.1.2)

¹⁵ Under such a definition, cadres include persons in the position in the Chinese party/government hierarchy at the level of 1) section chief, 2) division chief, 3) department chief, and 4) the head of a county or a higher entity, 5) enterprise manager, 6) middle manager in a enterprise, 7) enterprise procurement and supply representative, 8) town or township chief, 9) village chief, 10) state or collectively owned enterprise leaser, and 11) military officer.

Figure 3.1.2 Responds' power



3.5 The entrepreneurs' social relations

Table 3.2 The background and the closest social relations of the entrepreneurs (%)

	Cadre	Non-cadre	Total
Respondent	40	60	100
Father	32.1	67.9	100
Spouse	29.5	70.5	100
Closest relative	54.5	45.5	100
Closest friend	73.8	31.5	100
At least one	85.5	-	-
All	97 cases/3.7	243cases/10.9	-

The social relations of the entrepreneurs are examined in terms of their fathers, spouses, and the closest relatives and friends. Table 3.2 shows the distribution of these social relations of the entrepreneurs. About one third (32.1 per cent) of the entrepreneurs come from cadre families; 29.5 per cent of the entrepreneurs' spouses are (were) cadres. Outside family, the entrepreneurs have close connection with cadres. More than half (54.5 per cent)

of the entrepreneurs' closest relatives are cadre. Nearly three quarters (73.8 per cent) of the entrepreneurs' most frequently contact friends are cadre.

Furthermore, 85.5 per cent of the entrepreneurs have at least one connection with cadre, i.e., 85.5 per cent of the entrepreneurs either have at least one of the social relations as a cadre or they were cadre themselves. About 4 per cent (3.7 per cent) of the entrepreneurs have the densest cadre connections, where both the entrepreneurs and all their social relations are (were) cadres.

Generally speaking, the private entrepreneurs have close connections with cadres. Many of them were cadres themselves, and many of them were born in cadre families. Meanwhile, many of the entrepreneurs' spouses hold (held) cadre positions in government organisations or enterprises. Besides these, many entrepreneurs tend to interact most frequently with relatives and friends who are cadres. The social background of the entrepreneurs and their social relations consist a network, which is closely connected with cadres. The high percentages¹⁶ of cadre origin and cadre social relations, i.e., the over

¹⁶ Comparable statistics is not available. The latest relevant data about cadre occupation as the first definition is from *China Statistics Yearbook 1987*, which estimates there were about 8 per cent cadres in employment population in 1987. De facto, the Chinese communist party planned to reform cadre management system with replacement of civil servants in 1987, of which the theme was seen in the speech addressed by then general secretary Zhao Ziyang in the 13th Congress of the party (Chow, 1991). Accordingly, in 1988, the Chinese government stopped using occupation status in statistics; instead, they use figures of employees in sectors.

In 1993, the Chinese authorities established a new civil service system and officially defined "civil servants" as those 5.285 million "cadres" or administrators, managers, and professionals who work for government agencies, and a separate management system has been established for these individuals. The new system excludes all employees of various agencies working in the so-called "non-government" or service unit sector,

representation of cadre entrepreneurs and their social relations in the private sector seems to indicate the advantage of cadre connections. Whether such networks have implications for business operation is thus worthy further investigations.

3.6 Registered capital and real assets at start-up

Table 3.3 Registered capital and real assets at start-up

		start-up registered capital	start-up real assets
N	Valid	2780	2566
	Missing	89	303
Mean		927280.42	1325569.28
Std. Error of Mean		124672.11	131826.05
Median		150000.00	200000.00
Mode		100000 ^a	100000
Std. Deviation		6573425.01	6677741.00
Variance		4.321E+13	4.459E+13
Skewness		24.876	12.604
Std. Error of Skewness		.046	.048
Kurtosis		760.773	198.790
Std. Error of Kurtosis		.093	.097
Range		226999990	149999992
Minimum		10	8
Maximum		227000000	150000000
Percentiles	25	35000.00	50000.00
	50	150000.00	200000.00
	75	500000.00	600000.00
	90	1180000.00	2000000.00

^a. Multiple modes exist. The smallest value is shown

As shown in Table 3.3, the distribution of the start-up registered capital is positively skewed, the range is huge, and the mean is much higher than both the median and the mode. It is also the case for real assets the entrepreneurs had when they set up their

such as education, posts and telecommunications, and health, and employees of state-owned enterprises. Official policy since 1987, however, has called for flexible and appropriate management systems to be established for employees of these systems (Burns, 1997).

businesses. Thus the medians are the better values to describe the central tendency of the two variables.

The average registered capital at start-up was RMB 150,000 (median). Twenty five per cent of the entrepreneurs registered enterprises with the amount of capital of lower than RMB 35,000, half of the enterprises had registered capital of lower than RMB 150,000, and a quarter of the entrepreneurs had more than RMB 500,000 registered capital. One tenth of the entrepreneurs had more than RMB1.18 million registered capital.

The average value of real assets an entrepreneur had at start-up was RMB 200,000 (median), which is RMB 50,000 higher than the average registered capital. Since the mean of real assets is also higher than that of registered capital, it is safe to say that in general, the entrepreneurs already had much more accumulation than registered capital before their businesses began. This is supported by the comparison of the values of the two variables at quartiles.

The average accumulation of real assets is about 40 times the annual income of an ordinary Chinese resident in a city, and more than 60 times of the annual income of an ordinary Chinese citizen living in the countryside¹⁷ in 1997. How did the entrepreneurs finance their business start-up? What is the difference between those who were cadres and who were not cadres in financing? These questions need to be answered.

¹⁷ The average annual income for a city and town resident was RMB 5189, and that for a resident living in the countryside was RMB 2999 in 1997 (*A Statistical Survey of China*, 1998).

3.7 Cadre background, registered capital and real assets at start-up

It has been found both variables of registered capital and real assets are positively skewed. Can data transformation reduce this problem? When variables are positively skewed, we can apply square root transformations for the purpose of improving the normality of variables (Osborne, 2002). Figure 3.3 and 3.4 show the distributions of the two variables after the transformation. Clearly, they are still positively skewed. The transformation has not improved the normality of the distribution.

Figure 3.3 Distribution of the transformed registered capital

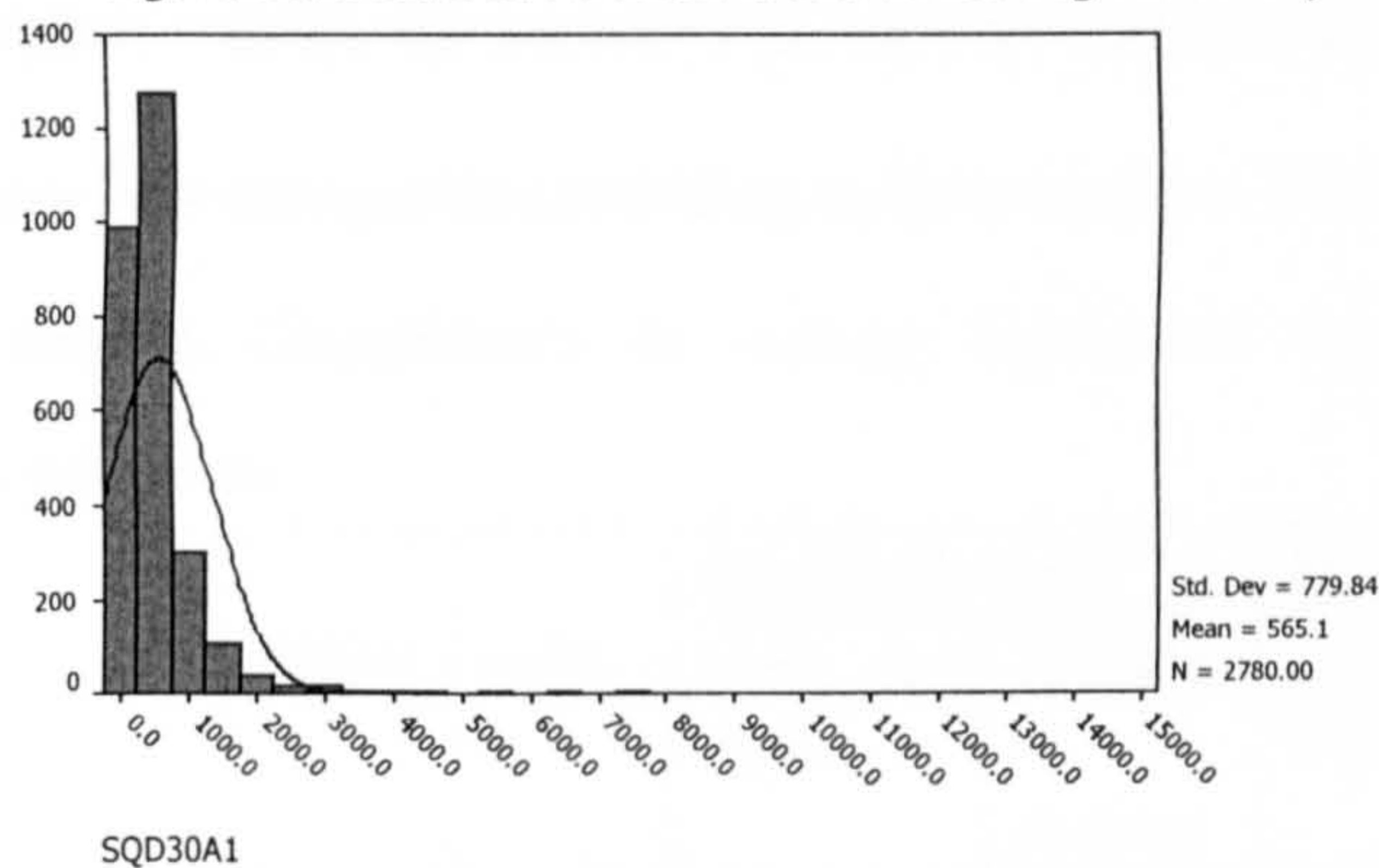
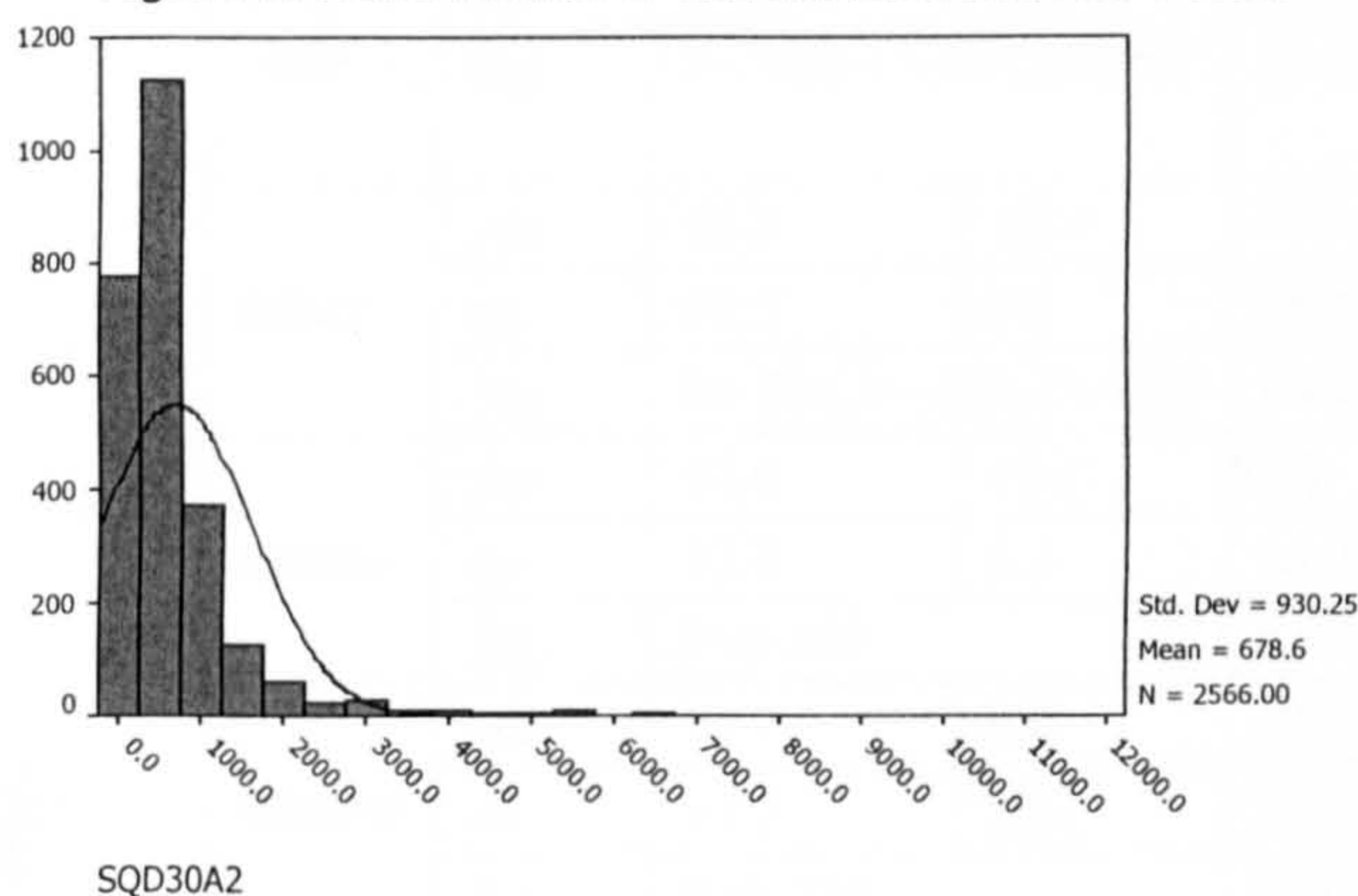


Figure 3.4 Distribution of the transformed real assets



This indicates that we cannot use a parametric test, because the assumption of normal distribution is not tenable (Field, 2000, p49). Non-parametric tests can be applied when

data is skewed (Foster, 1999, p194). Among all non-parametric tests, Chi-square test is the most widely used and it has a wider range of applications than most others (Owen and Jones, 1994, p429). In this analysis, cross-tabulation analysis and the Chi-square test are used to examine the association between the entrepreneurs' background variables, i.e., their social origins and social relations, and business advantage variables, i.e., the registered capital and real assets at start-up, and the main sources of finance. In order to test whether cadre related entrepreneurs have an advantage in business start-up in terms of being less likely to have less than average capital and being more likely to stand in the group with the highest capital, the variables of registered capital and real assets at start-up are collapsed into four categories according to their median, three-quartile and 90 percentile values.

Table 3.4 Comparisons in start-up capital for entrepreneur with and without cadre connections

relation	cadre	Registered capital		Real assets	
		Lower than average	The highest 10 percentage	Lower than average	The highest 10 percentage
Respon- dent	yes	47.4	12.3	48.8	10.6
	no	56.2	8.3	55.9	7.1
	Sig.	P=.000, V=.097, C=.097		P=.001, V=.081, C=.081	
father	yes	46.3	12.0	47.9	9.5
	no	55.2	9.5	55.4	8.3
	Sig.	P=.001, V=.086, C=.086		P=.013, V=.070, C=.070	
spouse	yes	52.6	11.1	51.3	9.6
	no	53.6	8.9	54.2	7.9
	Sig.	P=0.197		P=0.351	
relative	yes	52.7	8.4	53.5	7.5
	no	54.2	10.1	54.8	8.5
	Sig.	P=0.226		P=0.287	
friend	yes	51.1	10.2	50.8	9.3
	no	57.0	7.7	58.8	5.0
	Sig.	P=.004, V=.075, C=.075		P=.000, V=.093, C=.093	

Table 3.4 summarises the results of cross-tabulation analysis examining the association between the entrepreneurs' background/social relations and start-up capital, i.e., registered capital and real assets at start-up. It is found that the entrepreneurs who have been a cadre are less (47.4 per cent) likely to have start-up registered capital lower than the average of RMB 150,000, compared with the non-cadre entrepreneurs (56.2 per cent). Cadre entrepreneurs are more likely to have start-up registered capital of between RMB 150,000 and RMB 500,000. Among the 10 percentile cases with the highest registered capital, the cadre entrepreneurs lead four percentage points at 12.3 per cent, compared with 8.3 per cent of the non-cadre entrepreneurs. Chi-Square tests reveal that there is difference in start-up registered capital for the entrepreneurs with and without cadre background. However, the very low values of Cramer's V ($V=0.097$) and Contingency Coefficient ($C=0.097$) suggest a very weak association between the two variables. The low value of Lambda ($=0.000$) warns that the independent variable "cadre" does not predict the dependent variable "the start-up registered capital" (See Appendix Table A1.1, Table A1.2, Table A1.3, Table A1.4 for detail). The association between the two variables is so weak that further regression analysis is not needed (Siegel and Castellan, 1988, p301; Norusis, 1993, p213; Vaus, 1990; Ke *et al.*, 1996, p255; Zhang, 1998, p196).

Table 3.4 demonstrates a similar result for the association between the entrepreneurs' cadre experience and their real assets at start-up. In other words, the association between the entrepreneurs' background and real assets at start-up is very weak (see also Appendix A Table A2.1, Table A2.2, Table A2.3 and Table A2.4).

3.8 Entrepreneurs' social relations and their registered capital and real assets at start-up

As shown in Table 3.4 (see also Appendix Tables A3.1, A3.2, A3.3, A3.4, A4.1 A4.2, A4.3, and A4.4), entrepreneurs born in cadre families (father as a cadre) are slightly more likely to have the highest (the highest percentile) registered capital and real assets start-up. Chi-square tests find that the differences in these two aspects between the entrepreneurs with and without a cadre father are statistically significant at the levels of 0.01 and 0.05 respectively. Again, however, the low values of Cramer's V ($V=0.086$ and 0.070 respectively) and Contingency Coefficients ($C= 0.086$ and 0.070 respectively) show a very weak association between the dependent and independent variables. The low value of Lambda ($=0.000$) indicates that the independent variable "the entrepreneur's father as a cadre/non-cadre" predicts neither the dependent variables "the start-up registered capital" nor real assets at start-up (e.g., Siegel and Castellan, 1988, p301; Norusis, 1993, p213; Ke *et al.*, 1996, p255; Zhang, 1998, p196).

Table 3.4, together with Appendix Tables 9.1-4 and Table 10.1-4, shows a repeated story when the associations between the entrepreneurs' closest friends and registered capital and real assets at start-up are analysed. In other words, the cadre status of the entrepreneurs' closest friends has fairly weak correlation with both registered capital and real assets at start-up.

Again, the entrepreneurs with cadre spouses are slightly less likely to have less than average registered capital and real assets and slightly more likely to be in the top 10 percentile group of both registered capital and real assets at start-up. However, the

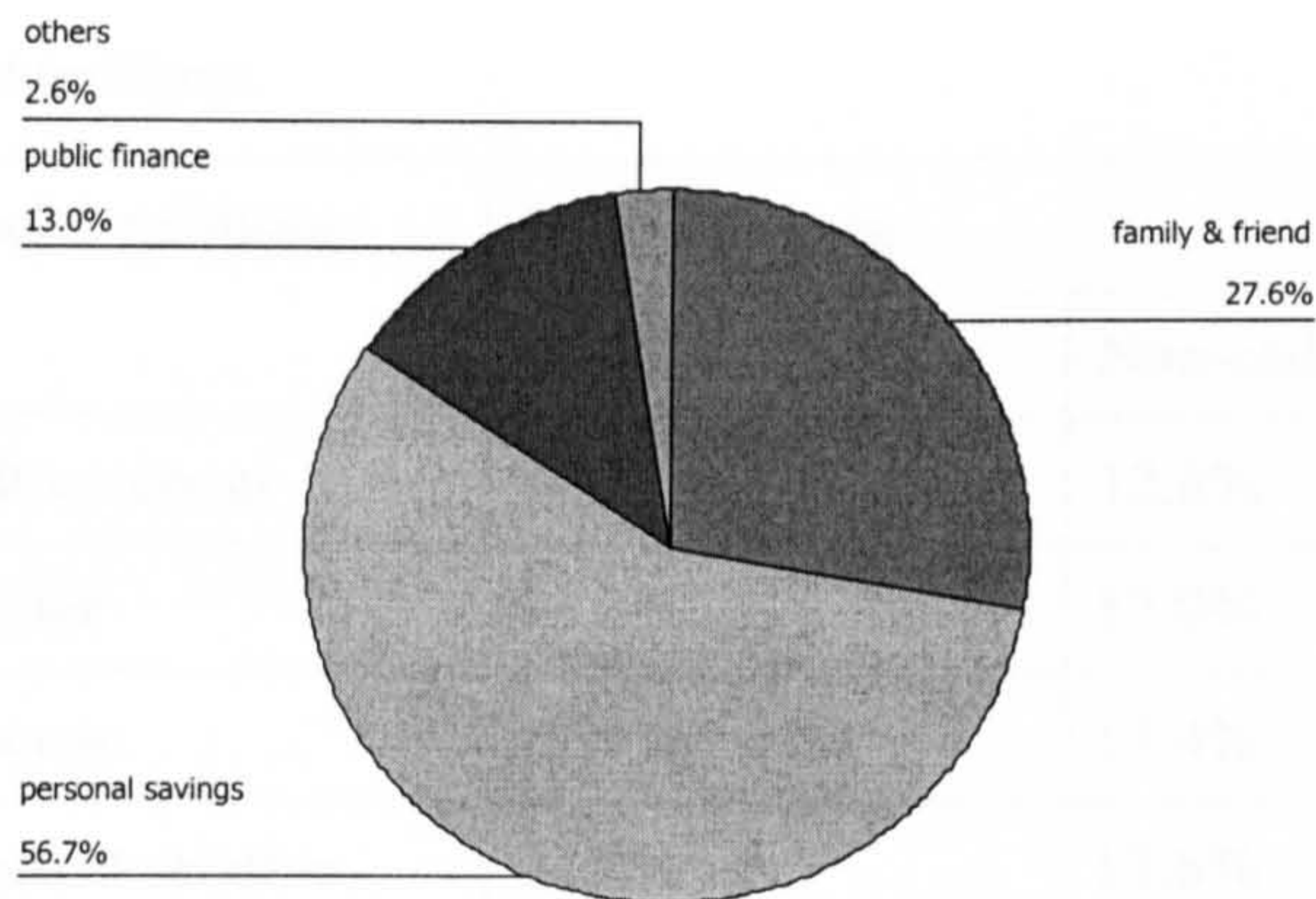
difference between those with cadre spouses and without is not statistically significant in either registered capital or real assets ($p=0.197$ and 0.351 respectively; see Table 3.4 and also Appendix A Tables A5.1, A5.2, A6.1 and A6.2).

Interestingly, the entrepreneurs whose closest relatives are non-cadres are slightly more likely (10.1 per cent and 8.5 per cent respectively) to have the highest registered capital and real assets at start-up (the top 10 percentile group) than the entrepreneurs who have closest cadre relatives (8.4 per cent and 7.5 per cent respectively, see Table 3.4 and Appendix A Tables A7.1, A7.2, A8.1 and A8.2). However, Chi-Square test reveals that the differences are not significant in either start-up registered capital ($p=0.226$) or real assets at start-up ($p=0.287$).

The above analysis indicates that cadre experience or having close social relations with cadres does not provide the entrepreneurs with an obvious advantage in terms of registered capital and real assets at business start-up, although there is very slight advantage for the cadre entrepreneurs. Therefore, the survey data does not support the assumption that being a cadre or having close social relations who are cadres have leading advantage in financing their start-ups in terms of the amount of capital in registered capital and real assets. The reasons will be discussed later.

3.9 The main sources of start-up capital

Figure 3.5 The main sources of start-up capital



There are several main sources for the entrepreneurs to obtain start-up capital as shown in Figure 3.5. More than half (56.7 per cent) of them relied on their own savings for start-up capital. More than a quarter (27.6 per cent) of them obtained finance from their relatives or friends. 13 per cent of them admitted to have loans from bank or organisation, which are what Wank (1999) terms public finance. The remaining entrepreneurs (2.6 per cent) financed their start-ups from overseas and other investment.

This section tries to find out if there is any difference in the sources of start-up finance. As there is discrimination against private enterprises, it is hard for private entrepreneurs to get start-up finance from banks (e.g., Uehara, 1999; *China Daily*, May 2 1999). If the entrepreneurs who have connections with cadres have the strength of “power conversion” (e.g., Clark, 2000; Rona-Tas, 1994), they should be more likely to get finance from bank or other organisations, that is, transferring public funds (Wank, 1999) for their business start-ups.

Table 3.5 Comparison of public finance for the entrepreneurs with and without cadre connections

Social relations	Public finance	
	Cadre	Non-cadre
Entrepreneur	14.1%	12.8%
Father	13.2%	12.9%
Spouse	12.9%	13.4%
Closest relative	12.4%	13.8%
Closest friend	13.1%	13.0%
All	14.7%	11.3%

Table 3.5 compares the percentages of getting public finance between cadre and non-cadre related entrepreneurs. The entrepreneurs who have been cadres (14.1 per cent) and who come from cadre families (13.2 per cent) are slightly more likely to obtain public funds for their business start-ups, compared with the entrepreneurs who have not been a cadre (12.8 per cent) and whose fathers are (were) not cadres (12.9 per cent). But on the contrary, the entrepreneurs whose spouse are (were) not cadres (13.4 per cent) and whose closest relatives are not cadres (13.8 per cent) tend to be slightly more likely to get public finance than those having cadre spouses (12.9 per cent) and closest cadre relatives (12.4 per cent). However, cross-tabulation and Chi-Square tests don't find any significant difference in the sources of start-up capital between the cadre related entrepreneurs and non-cadre related entrepreneurs (see Appendix A Tables A11.1, A11.2, A12.1, A12.2, A13.1, A13.2, A14.1, A14.2, A15.1 and A15.2). Thus the comparisons suggest no evidence of advantage of having connections with cadres in obtaining loans, either from banks or other public

organisations.

In short, the analysis indicates that entrepreneurs who have close connections with cadre don't seem to have an advantage in start-up in terms of registered capital and real assets at start-up. Neither do the cadre related entrepreneurs appear to have advantage in obtain public finance.

3.10 The density of connections with cadre and start-up finance

The above examines individually the influence of the cadre background of the entrepreneurs and their social relations. Connections with cadre do not make any difference in business start-up registered capital, real assets and the main sources of finance.

Do the connections with cadre have collective power? In other words, does the density of connections with cadre account for any difference? There is the possibility that when the connection with cadre is dense, the function of connection with cadre turns up. This section aims at exploring if such a possibility exists.

In terms of the density of connections with cadre in the survey, there are two extremes, on the one end, neither the entrepreneurs themselves nor their social relations are (were) cadres; on the other end, both the entrepreneurs and all their social relations (were) are

cadres. In the former case, the density of connections with cadres is the least; while in the latter, the entrepreneurs have the densest cadre connection. If the assumption that the denser the connections with cadres the more likely the entrepreneurs to have advantage in business start-up is true, the entrepreneurs with the densest cadre connections should appear far less likely to have lower than average registered capital and real assets at start-up, on the other hand, they should be much more likely to have the highest registered capital and real assets at start-up,. In addition, they should have more opportunity to obtain public finance.

Table 3.6 Comparison between all-cadre and non-cadre entrepreneurs in start-up finance

		Non-cadre	All cadres	Significant	Cramer's V	Contingency Coefficient
Registered capital	Lower than average	135 57.0%	45 49.5%	P=0.083	V=0.143	C=0.141
	The highest 10 percentage	21 8.9%	16 17.6%			
Real assets	Lower than average	128 55.9%	35 41.7%	P=0.149	V=0.131	C=0.129
	The highest 10 percentage	15 6.6 %	9 10.7%			
Main sources of capital	Public finance	27 11.3%	14 14.7%	P=0.031	V=0.163	C=0.160

As illustrated in Table 3.6 (see also Appendix A Tables A16.1, A16.2, A16.3, A16.4, A17.1

and A17.2), the entrepreneurs with the densest connections with cadre are less likely to have less than average registered capital and real assets at start-up than those without any connection with cadres. On the other hand, they are about twice more likely to have the highest registered capital and real assets at start-up. Also, they seem slightly more likely to obtain public finance. However, like the findings previously, none of the differences between the entrepreneurs with the densest cadre connections and those without any connection with cadres is statistically significant. In other words, there is no statistical evidence that the entrepreneurs with densest cadre connections have advantage in terms of having more registered capital and real assets and getting public finance at business start-up.

3.11 Does industry affect the difference?

Wank (1999) and Nee (1989, 1991) draw different conclusions from their research, where the former mainly concentrates on commerce, while the latter focuses on farming. Oi (1989) and Rona-Tas (1990) suggest that the advantages of cadres are greater in industry than agriculture. Does this mean that industry matters? In other words, can it be true that cadre entrepreneurs have an advantage in certain industry, such as in the case of Wank's (1999) study in commerce?

It was found in section 2 that private enterprises are mainly engaged in manufacturing (40.4 per cent), commerce (27.4 per cent), social services (7.2 per cent), construction (5.5

per cent), agriculture (4.1 per cent), and transportation (2.4 per cent). If the cadre experience or having cadre connections has advantage in certain industries, the advantage should be found in the main sectors listed previously. Again, the following analysis compares start-up registered capital and real assets and the main sources of start-up capital between the entrepreneurs with the densest cadre connections and the entrepreneurs without any cadre connection.

There are 86 private firms operated by the entrepreneurs without any cadre connection together with 33 firms run by the entrepreneurs with the densest cadre connections in the manufacturing industry. 26 entrepreneurs with the densest cadre connections are in commerce businesses, comparing with 60 entrepreneurs without any cadre connection.

Small numbers make impossible this comparison being conducted in other industries. In the construction industry, 13 entrepreneurs have neither been cadres nor have a cadre social relation. In the same industry, only 4 entrepreneurs have the densest cadre connections. 27 entrepreneurs with the least cadre connection have their businesses in social service businesses; while only 5 entrepreneurs with the densest cadre connections are in the same industry. In the transportation industry, there are 7 entrepreneurs who have the least cadre connection and 3 entrepreneurs who have the densest cadre connections. In agricultural businesses, there are 15 firms operated by the entrepreneurs without any cadre connection. However, no entrepreneur with the densest cadre connections does business in

this industry. Thus, the comparison is confined in the two main industries where the majority of private firms are engaged.

3.11.1 The densest cadre connections versus non-cadre connection in commerce

Cross-tabulation and Chi-square tests find that the entrepreneurs with the densest cadre connections are less likely to have lower than average registered capital and real assets, and they are more likely to have the highest registered capital and real assets at start-up.

The entrepreneurs with the densest cadre connections are about three times more likely than those without any cadre connection to have the highest registered capital. But interestingly, such a possibility declines in real assets at start-up. Also, the entrepreneurs with the densest cadre connections are more likely than those without cadre connection to obtain public finance for their start-ups. This may, to some extent, be understood as the advantage of having cadre connections in terms of greater access to public finance, as suggested by some researchers (e.g., Wank, 1999). However, again, the differences between the two groups of entrepreneurs are not statistically significant (Table 3.7 and also Appendix A Tables A18.1, A18.2, A18.3, A18.4, A18.5 and A18.6).

Table 3.7 Comparison of start-up capital between all-cadre and non-cadre in commerce

	All-cadre		Non-cadre		Significant
	Lower than average	The highest 10 percentage	Lower than average	The highest 10 percentage	
Registered capital	13 50.0%	4 15.4	40 66.7%	3 5.0%	P=0.252
Real assets	11 45.8%	1 4.2%	39 65.0%	2 3.3%	P=0.353
Main sources Of capital	Public finance		Public finance		P=0.180
	3 11.5%		3 4.8%		

3.11.2 The densest cadre connections versus non-cadre connection in manufacturing

Table 3.8 shows the Cross-tabulation and Chi-square test results of the comparisons between the entrepreneurs with the densest cadre connections and those without any cadre connection in manufacturing industry (see Appendix A Table A19.1-6 for details). Unlike the previous findings, the entrepreneurs with the densest cadre connection tend to be more likely to have lower than average registered capital. Another interesting finding is that the entrepreneurs with the densest cadre connection tend to be slightly less likely to have the highest real assets at start-up. Again, the entrepreneurs with the densest cadre connection are more likely to get public finance at business start-up. However, in no case, is the

difference between the two groups of entrepreneurs statistically significant. In other words, there is no clear statistical evidence to support that closely cadre related entrepreneurs have advantage in financing business start-up.

Table 3.8 Comparison of start-up capital between all-cadre and non-cadre in manufacturing

	All-cadre		Non-cadre		Significant
	Lower than average	The highest 10 percentage	Lower than average	The highest 10 percentage	
Registered capital	18 54.5%	4 12.1%	42 48.8%	10 11.6%	P=0.897
Real assets	12 40.0%	2 6.7%	42 51.2%	6 7.3%	P=0.594
Main sources Of capital	Public finance		Public finance		P=0.787
	5 14.7%		9 10.3%		

3.12 Any advantage for connections with high-level cadres?

It might be thought that my analysis fails to confront the fact that not all cadres are the same and that what really matters for business success is not being a cadre – but being, or having been or having had relations with a high level cadre. To test this possibility we compare entrepreneurs with a background of being a cadre at higher than county chief (division chief) level with those without. It should be noted that a person at a level of higher than county chief (division chief) is a high rank cadre.

Table 3.9 Comparisons in start-up capital for entrepreneur with and without high-level cadre connections

relation	High level cadre	Registered capital		Real assets	
		Lower than average	The highest 10 percentage	Lower than average	The highest 10 percentage
Respondent	Yes	36.4	18.2	44.7	13.2
	No	53.0	9.8	53.2	8.4
	Sig.	P=0.078		P=0.654	
Father	Yes	38.9	11.1	48.3	7.8
	No	53.1	10.2	53.3	8.7
	Sig.	P=0.006 (V=C=0.073)		P=0.340	
Spouse	Yes	41.9	14.0	53.3	2.6
	No	53.5	9.5	55.3	8.5
	Sig.	P=0.389		P=0.547	
relative	Yes	57.1	8.7	55.2	6.7
	No	52.9	9.3	54.0	8.1
	Sig.	P=0.602		P=0.858	
Friend	Yes	49.6	11.9	53.6	9.1
	No	53.6	9.0	51.7	7.7
	Sig.	P=0.230		P=0.753	

Table 3.9 reports briefly the comparisons between the entrepreneurs with and without a connection with a high-level cadre in start-up capital and the main sources of start-up capital. The entrepreneurs having been a high level cadre or having connections with high-level cadres are more likely to have the highest registered capital. The entrepreneurs having been a cadre or having a high level cadre as the closest friend are also more likely to have the highest real assets at start-up. But interestingly, the entrepreneurs whose fathers,

spouses and closest relatives are cadres are less likely to have the highest real assets at start-up, compared with those without such connections with high-level cadres. It must be noted that none of these differences is statistically significant (see also Appendix A Table A20.1-6, A21.1-5, A22.1-4, A23.1-4, and A24.1-4).

Table 3.10 compares the entrepreneurs with and without connections with high-level cadres in the main sources of start-up capital. Only the entrepreneurs whose closest friends are high-level cadres are slightly likely than those without to have public finance at start-up (14.4 per cent versus 12.9 per cent). Quite contrary to the power conversion theory's prediction, the entrepreneurs having been a high-level cadre or having high-level cadre fathers, spouses and closest relatives are consistently less likely to have start-up capital from bank or other public organisations.

Table 3.10 Comparison of public finance for the entrepreneurs with and without high-level cadre connections

Social relations	Public finance	
	High-level cadre	Non-high-level cadre
Entrepreneur	11.9%	13.3%
Father	11.9%	13.2%
Spouse	10.9%	13.3%
Closest relative	12.7%	13.1%
Closest friend	12.9%	14.4%

3.13 No strength of connections with cadre?

Generally speaking, the data analysis has not found clear evidence that connections with cadres have advantage in start-up finance. Though cadre related entrepreneurs are more likely to have higher start-up capital in general; in some aspects, non-cadre related entrepreneurs are more likely to have higher start-up capital. In particular, there is not much difference in the possibility of getting public finance between entrepreneurs with and without cadre connections. The finding is not in accordance with some other similar research (Rona-Tas, 1994; Kolankiewicz, 1996; Wank, 1999; Clark, 2000), which believes that cadre related entrepreneurs have an advantage in start-up. Why?

Firstly, there is the possibility that connections with cadre are not important in some aspects. The analysis of the importance of connections with cadre is based on the assumption that the government controls resources and cadres have power in redistributing these resources. Under the traditional central planning system in China, all means of production were under the control of central or local government, across different authorities at different administrative levels. However, with the development of marketisation, the government has fewer and fewer goods to control. The force of market pushes the development of the private sector in China. With the emergence of the market, the central distributor will lose power and direct producers will have more discretion over their goods and services, as a consequence, marketisation will provide new alternatives to bureaucratic advancement. Even in the absence of fundamental change in the political

order, the growth of market institutions causes a decline in the significance of government allocation power (Nee, 1992; 1996). The more complete the shift to market coordination, the less likely that economic transactions will be embedded in the networks dominated by cadres, and the more likely power-control over resources will be located in market institution and in social networks of private buyers and sellers (Nee, 1989).

This is justified by the survey of China's Entrepreneur Survey System¹⁸ (1999). According to the surveys, 54.8 per cent of entrepreneurs assumed that raw materials were over-supplied in 1996. In 1999, 77.3 per cent entrepreneurs had such a belief, an increase of 12.5 percentage. This indicates that China has passed the shortage economy to some extent; it also implies lower control of government over production factors, on the other hand. Therefore, opportunities for gain depend less on the personal discretion of cadres in positional power.

Secondly, compared with Eastern European countries, China has a different reform path, which can lead to a different result. Privatisation of government enterprises has not played a significant role, although a new but small private sector has emerged (Walder, 1995, p965). Where privatisation has been more bottom-up, old political connections may count less (Rona-Tas, 1994, p53). At the very beginning of the reform, people in private businesses were from peripheral groups, such as prisoners, the unemployed (Kraus, 1991).

¹⁸ The survey was conducted by China's Entrepreneurs Survey System, a subsidiary institute of The Development Research Centre under the State Council in 1997. The ownership composition of the sample is as follows, state owned 45.7%, collectively owned 7.7%, privately owned 3.5%, foreign invested 8.6%, others 33.9%. The survey has 3629 valid responses among 10,000 mailed-out questionnaires.

Indeed, even in the same block with a similar privatisation process, *nomenklatura* members in Poland and Hungary have not an identical fate in property accumulation. A much larger proportion gained ownership rights over productive assets in Hungary than in Poland. This is mainly because the two countries have different privatisation policies instituted by post-communist governments, upon which the ability of the *nomenklatura* members to accumulate economic assets is greatly contingent. Only a small proportion of *nomenklatura* members in Poland have ownership of economic assets, of whom, the vast majority reported ownership of very small businesses (Hanley, 2000). Szelenyi and Szelenyi (1995) also disconfirm the power conversion theory and argue that the power conversion thesis is grossly exaggerated.

These point to the possibility that entrepreneurs with cadre connections are not necessarily to have higher start-up capital in China. As resources are not all controlled by cadres, businesspeople do not necessarily rely on public finance. In other words, they can have alternatives for their start-up capital.

Thirdly, the survey only investigates the closest social relations of the entrepreneurs. This is a limitation of the data. Strong ties of course have their strengths. However, strong ties are not necessarily the most helpful ties. Weak ties can also have strength in bridging opportunities (Granovetter, 1973). Social relations can provide individuals with both expressive and instrumental support. The survey data did not specify the closest friend and relative in what aspect or in what sense. The closest relative or the most frequently

contacted friends may provide expressive support, but they may be helpless in business operation.

Fourthly, and more importantly, *guanxi* practice in China is common. Entrepreneurs without available connections with cadres can have alternatives to connect themselves with cadres and access resources, if cadres control them. Thus, it is essential to find out what these alternatives are and how they work. The closest social relationships examined in this analysis are only a form of *guanxi*. *Guanxi* can be a source of sustained competitive advantage for doing business in China (Tsang, 1998), which can be of different types. If cadre related entrepreneurs have an advantage in start-up as found in some situations, the non-cadre related entrepreneurs are able to overcome the disadvantage by *guanxi*. This can explain the similar opportunities in obtaining public finance at start-up for entrepreneurs with and without cadre connections found in the above analysis.

Moreover, the entrepreneurs who have been cadres have no such power any more when they become private entrepreneurs. The change of social status has effects on their social capital. This has been ignored by the existing research. The last two points will be the main concern of the case study chapters.

3.14 Conclusion

The analysis of the survey data on China's private entrepreneurs suggests that being a

cadre and having close connections with cadres provides private entrepreneurs with more possibilities to have higher start-up capital. Such a result may be interpreted as that cadre related entrepreneurs have an advantage in start-up. However, it must be noted that the association between such connections and start-up capital is very weak. Also in some aspects, non-cadre related entrepreneurs are more likely to have higher start-up capital. For example, in manufacturing, non-cadre related entrepreneurs are more likely to have higher real assets at start-up. The power conversion theory claims that cadre related entrepreneurs could transfer public finance for private businesses. However, the comparative analysis in this chapter has suggested that there is not much difference between entrepreneurs with and without close cadre connections in terms of the possibility of obtaining public finance. Therefore, the statistical analysis in this chapter does not support the general argument of power conversion.

It is also worth pointing out that the findings in this chapter should be interpreted with caution. It should be noted that the data analysed was collected in 1995, before the 15th Chinese Communist Party Conference in September 1997, which introduced top-down privatisation by re-organisation, merger, leasing contract operation, joint stock partnership or sell-off, in order to quicken the pace of state enterprises reform (*Financial Times*, December 8, 1997). The advantages of having connections with cadres, such as buying public assets with a low price by cadre related entrepreneurs (Clark, 2000), had not emerged yet. Another limitation of the data is that enterprises run by cadre related entrepreneurs were beyond the investigation of the 1995 survey on private enterprises, if

they were under the guise of state owned or collectively owned firms. Also, the finding that there is no significant advantage for cadre related entrepreneurs is limited to business start-up. It is possible that they can enjoy some other advantages, for example, converting public assets into private, or getting more out of their effort because of their power and connections (Walder, 1996, p1063). It will be rash to make a general conclusion that connections with cadres are not important to the private business in China. Further qualitative research is thus needed.

The theory of power conversion is in the frame of social capital theory, where social capital is “what ordinary language calls connections” (Bourdieu, 1993, p160). Cadres, or connections with cadres, are supposed to convert political power to economic advantage (e.g., Rona-Tas, 1994; Kolankiewicz, 1996; Wank, 1999). However, social capital is not inheritable all the time (Pahl, 1996). Social capital of the old order is not indispensably useful in the new order.

More importantly, close connections with cadres examined in the survey are only a form of social relations, or of social capital. Social capital also involves transforming contingent relations for personal ends. The entrepreneurs could not choose what kind of family to be born in, and they could not choose their former occupations at will under the planned economy. Besides these static attributes of individual entrepreneurs, there are many other social relations they can choose to develop for their business purpose. As Van Duijn *et al.* (1999) find, the anticipation of future benefits is a main consideration of developing

relations, and another person's high social status influences the decision to invest in relations. In other words, social capital can be created and developed. This is what I call the dynamics of social capital. Neglected by the social scientists mentioned above, the dynamics of social capital will be discussed in the following chapters, with the next two chapters examining the two key concepts of *guanxi* and social capital.

Nee (1989) maintains that the more complete the shift to market, the less likely that economic transactions will be embedded in social networks dominated by cadres, and the more likely power – control over resources – will be located in market institutions and in social networks of private buyers and sellers. The IT sector has recently emerged in China, and thus is more market-oriented than the traditional sectors with less government interference. How do private entrepreneurs in this sector start up their businesses? The case studies will shift to analyse the private IT sector and answer this question.

Chapter 4 *Guanxi*

The previous chapter found that there is no statistical evidence to support the power conversion theory, which claims that cadre-related entrepreneurs have an advantage in business start-up. It suggested that the close social relationships examined are simply a form of *guanxi*. Both the entrepreneurs with and without available connections with cadres can practice *guanxi*, which can provide them with an advantage. This chapter is a literature review on the available research on the *guanxi* concept. It examines the definitions of *guanxi*, the importance of *guanxi* and thus the functions of *guanxi*, and the reasons for its emergence, the consequences and the implications of *guanxi*. Also, some deficiencies of the available research are discussed.

4.1 What is *guanxi*?

Guanxi is a term very common in every day Chinese life. Abroad, there is a popular belief that *guanxi* has magic power, which is reflected in the fashion of more and more people talking about *guanxi*. The search engine of the portal yahoo.com shows more than 2000 items, when the key word '*guanxi*' is entered. Most of the pages emphasise the importance of *guanxi* in China. Foreign consultancy companies provide advice to companies with an interest in China. According to them, without *guanxi*, a foreign firm will face a dim future in China. Also, more and more social scientists have paid attention to *guanxi* (e.g., Gold, 1985; Walder, 1986; Solinger, 1989; Wank, 1999), and some researchers have made

guanxi the key concept in their research (e.g., Yang, 1994; Guthrie, 1998; Tsang, 1998; Luo, 2000).

The characters that comprise the word *guanxi* are *guan* and *xi*. *Guan*, as a noun, means a door or pass (as in Shanhaiguan, the place in Hebei province where the Great Wall meets the sea). *Guan* is also a verb with the meaning of “close up”. Both usages have the metaphor of barrier. If we apply this to human relationships, a person inside the barrier is one of us, an insider, while another person outside the barrier has no “relationship” with us, or even can be our enemy, and thus is not of our concern. *Xi* is used both as a noun and a verb. In its verb form, *guanxi* means to tie up or connect (as in the common verb *lianxi*, to communicate); in its noun form, *xi* has the meaning of “a system” or “a network”. Thus *guanxi* conveys something like “tying up interface system” (Li and Li, 2000, p1). However, in the Chinese language, *guanxi* has several different connotations. In the most general sense, *guanxi* simply means relationship, which refers to the existence of a relationship between people or things, for example, the relationship between buyers and sellers, or the relationship between two variables in social science research, can be termed *guanxi*. In this sense, the word does not carry any connotations about how these relationships work.

More commonly, *guanxi* refers to the contact and connection between people, or particular people with whom one has a strong connection. Accordingly, it has been translated into English in different ways, such as, social relationship, personal ties, and personal relationship. However, the meaning of *guanxi* can be more than what can be represented

by the term relationship or connection. For example, *Xinci Xinyu Cidian (New Words and New Phrases Dictionary, 1989, Beijing)* defines *guanxi* as “the use of someone’s authority to obtain political or economic benefits by unethical persons”.

In the social and business context, *guanxi* is a rich and complex concept. A number of researchers have tried to elaborate on this construct, but no universal definition has so far been presented. Tsui and Farh (1997, p56) define *guanxi* as the existence of direct particularistic ties between two or more individuals. To Walder (1986, p162-186), *guanxi* substitutes for impersonal market transactions in a setting where such markets are restricted and scarcity prevails, thus *guanxi* is social relations involving the exchange of favours or a reliance on personal connections or petty corruption to obtain a public or private good. Davies *et al.* (1995, p210) argue that *guanxi* relates to personal relations involving the exchange of favours and the giving of face or social status and that the concept of networking is well suited to capture the key features of *guanxi*. Tsang (1998, p65) simply borrows Pye’s definition of *guanxi* as “friendship with implications of continued exchange of favour”. To Lovett *et al.* (1999, p232), *guanxi* refers to networks of informal relationships and exchanges of favours that dominate business activity throughout China and East Asia, which is an ancient system based on personal relationships.

One of the most frequently cited studies of *guanxi* by Yang (1994, p6) starts with the definition of *guanxi xue* or the art of *guanxi* as follows: *guanxi xue* involves the exchange of gifts, favours and banquets; the cultivation of personal relations and networks of mutual

dependence; and the manufacturing of obligation and indebtedness. Indeed, Yang (1994) does not explicitly distinguish between *guanxi* and *guanxi* practice, where *guanxi* is simply interpersonal relationships; while the use of *guanxi*, these personal relationships; to gain advantages is *guanxi xue*. Gold (1985, p672) makes it clear that the technique of establishing and manipulating *guanxi* is *guanxi xue*. To Luo (2000, p2), *guanxi* is the concept of drawing on connections in order to secure favours in personal relations, whereas *guanxi xue* refers to the practical strategies that best ensure personal relationship building, utilisation, and development.

Putting these elements together, we arrive at a much fuller concept. *Guanxi* involves firstly, personal relations, secondly, the use of personal relations, and thirdly, obligation and reciprocity in exchange. The precondition of *guanxi* is the existence of personal relations. To refer to the use of *guanxi* is to understand *guanxi* as opportunism¹⁹. Obligation and reciprocity imply the norms of *guanxi*.

Firstly, *guanxi* is personal relationship. To understand the personal aspect of the term *guanxi*, the best way is to know how Chinese have relationships with each other. The traditional Chinese social system was not defined in terms of individuals but in terms of dyadic ties between individuals, which reflected the teaching of Confucius. Man is defined as a social and interactive being, rather than an isolated, separated entity. The social

¹⁹ The term is used here in the everyday sense of 'the practice of taking profit from all occasions' (*Penguin English Dictionary*, 1980) rather than in the way it has come to be used in economics since Williamson (1975), who used it to mean making self-disbelieved statements on actions, i.e., lying and cheating.

philosophy of relationships is what Confucius called the principles of *lun*: a differentiated order²⁰. Fei (1992) argues that linkage among the Chinese is ego-centred social space radiating from the centre like ripples from a stone dropped in water. Chinese place people with whom they are interacting into different categories, such as *jiaren* (family members), *shuren* (acquaintances) and *moshengren* (strangers), or *zijiren* (one of us, insider) and *wairen* (outsider). The differentiation implies completely different social and psychological meanings to the parties involved and accordingly the relationships are governed by a different set of interpersonal rules. From this perspective, *jiaren* and *shuren*, or *zijiren*, are *guanxi*, while *moshengren* or *wairen* are not *guanxi*. Thus, *guanxi* is an ego-centred personal relationship.

Closely related, *guanxi* is also private and informal. *Guanxi* exists between individuals rather than organisations; accordingly, *guanxi* is not housed in organisation but in individuals. People establish and maintain *guanxi* through private and informal channels, such as banquets and gifts (Yang, 1994). The government officially discourages *guanxi*. From the communist's point of view, *guanxi* works against the supposed fair comrade interpersonal relationship among people, and thus it contradicts the communist ideology (Gold, 1985). As well, the practice of *guanxi* has negative impact, which has not a very clear boundary with corruption and is labelled deviant practice (Yang, 1994, p63). In this sense, *guanxi* itself can only exist in informal and private settings. Wang (2000, p530)

²⁰ *Lun* is a system of social roles with distinct status differences, which stresses the differentiation between individuals: prince and subject, father and son, husband and wife, elder brother and younger brother, and friend and friend. All these relationships are superiors to subordinates except friend to friend.

points out that informal networks exist in every society, including the most advanced industrialised societies, but the informal *guanxi* networks in Chinese society stand out for three reasons: 1) the degree to which informal networks contradict and undermine formal institutions is extremely high; 2) the influence of informal networks is unusually strong in every aspect of Chinese life; and 3) the level of institutionalisation of Chinese networks is very low.

Secondly, *guanxi* is instrumental. Gold (1985) argues that the pre-eminent characteristic of personal relationship in China today is instrumentalism. The principle that underlies it is *guanxi*, which means connectedness or particularistic ties. Walder (1986, p162-186) also looks at *guanxi* as an instrumental personal relationship, mingling instrumental intentions with personal feeling. It can range from strong personal loyalties to ceremonialised bribery. At the one end of this spectrum is the type of relationship connected with the term particularism, which involves showing favouritism to people with whom one has pre-existing personal ties. In this type of *guanxi*, the affective aspect of the relation is the motivation. At the other end of the spectrum is the type of relationship that amounts to ceremonialised bribery, which involves a straightforward exchange of favour for material gain or a compensatory favour. In this type of relationship, the primary motivation is the instrumental aspect of the direct exchange with a minimum personal element. Between these extremes is a type of relationship termed target cultivation, which is purposeful cultivation of someone in a position of power so that one may benefit. The instrumentalism of *guanxi* is more apparent from the object of the cultivation of *guanxi* that centres on the

factory allocations and socio-political services that are controlled by individuals. The cultivation takes place through the giving of small gifts and the performance of favours for the purpose of future advantage.

Similarly, Hwang (1987) identifies three kinds of interpersonal relationships in social exchange in the Chinese setting, namely, expressive ties, instrumental ties, and mixed ties. Expressive ties occur mostly among family members, close friends, and other congenial groups, which are based on affection. Instrumental ties are based on achieving specific goals, existing between people who interact with each other on a short-term basis, such as a salesperson and a customer. Mixed ties are in between the two. These are relationships between people who know each other and expect to interact with each other on a long-term basis. Moreover, in such situations, people seek to influence others by *renqing*²¹. The mixed ties are typical *guanxi* by their instrumental function. The purely instrumental ties, which are usually short and unstable, are not *guanxi*.

In a *guanxi* relationship, appropriate behaviours are expected in accordance with the norms of *guanxi*, which include reciprocity and trustworthiness. The Chinese people place great stock in the importance of *mianzi* (face), which is one's social image and social status

²¹ According to Hwang (1987) and Yang (1994), there are three meanings of *renqing*. Firstly, *renqing* refers to the emotional responses of an individual in everyday life, which is part of the intrinsic character of human nature; secondly, *renqing* means a certain kind of resource that one can present as a medium of social exchange, which is close to the word favour; thirdly, *renqing* is a set of social norms which require one should keep in contact with relatives, friends, and acquaintances, and offer help to those in need. In other words, *renqing* is also the proper way of behaving oneself in social relationships.

gained by performing one or more social roles that are recognised by others. Both parties in a *guanxi* relationship must obey the implicit rule of reciprocity. Disregard of this can lead to the damage of one's reputation and thus social status (Wank, 1999, p98-109). It might be said, then, that *guanxi* is, in this sense, an instrumental relationship with Chinese characteristics.

Thus, thirdly, *guanxi* is a reciprocal relationship through which people exchange favours. Gold (1985) points out that *guanxi* is based on reciprocity, the traditional concept of *bao*, where one does favours for others as social investments, clearly expecting something in return. The favours exchanged range from providing scarce resources necessary in everyday life (Walder, 1986) to presenting job opportunities (Lin and Bian, 1991) or business information (Solinger, 1989), as well as other kinds of benefits (Yang, 1994). Owing someone a favour only obligates one to return it at a later time, but there is no specification on when one should return a favour. The return of favour will not always be equal. In fact, if one returns a favour abruptly and quickly, this may imply the end of *guanxi* (Luo, 2000, p27).

Since *guanxi* has become more and more instrumental, the line between *guanxi* and bribery is very hard to draw. Walder (1986, p179) labels the straightforward exchange of favour for material gain or a compensatory favour as ceremonialised bribery. Wang (2000, p536-7) insists that there are several distinctions between *guanxi* and bribery. First, *mianzi* (face) and *gangqin* (affection) are not important in bribery, while they are elements in *guanxi*;

second, *guanxi* is based on long-term relationship, whereas favour exchange through bribery is short-term transaction; third, the nature of gift giving is different. In *guanxi*, the symbolism embodied in gifts is often more important than the practical value of gifts, while the monetary value of gifts is the determinant to the grant of a favour. Despite these, in the long run, *guanxi* generally means repayment of favours in one way or another. *Guanxi* becomes the enabler of future opportunities.

Indispensable for reciprocity, trust is an important ingredient of *guanxi*. For example, Child (1996, p13) argues that *guanxi* is reciprocating relationship built on trust and mutual identity. According to Yueng and Tung (1996), 85 per cent of managers whose companies had business in China reported that trust was an essential condition for *guanxi* and that *guanxi* could not exist without trust. Based on mutual expectation among social members, trust is the basic precondition for social interaction (Barber, 1983). Zucker (1986) points out that trust is a set of expectations shared by all those involved in an exchange. With family and kinship ties, which expand the radius of trust, overseas Chinese in Southeast Asia extend credit, pool capital and delegate authority without fearing of default or deceit (Fukuyama, 1995b). Besides family and kinship ties, *guanxi* is another most important source of trust. Trust is available because ‘the community is so close-knit that malfeasance is not only difficult to conceal or execute, but often even hard to imagine’ (Granovetter, 1992, p7).

Therefore, *guanxi* in its utilitarian aspect is a personal relationship accessed for desired

goods based on the norm of reciprocity. Arias (1998) offers a summary of the main characteristics of *guanxi*: (1) It includes the notion of a continuing reciprocal relationship over an indefinite time period, (2) favours are banked, (3) it extends beyond the relationship between two parties to include other parties within the social network, (4) the relationship network is built among individuals not organisations, (5) status matters – relationships with a senior will extend to his subordinates, but not visa versa and (6) the social relationship is prior to and a prerequisite to the business relationship.

But such a concept, a narrow understanding of *guanxi*, has at least three limits. Firstly, family relationships and other expressive relationships, which people can resort to for certain purposes, are excluded. Chinese do not consider family relationships as *guanxi* relationships as defined above. One cannot say, for example, that one has *guanxi* with one's father or that one needs *la guanxi* (pull connection) with one's father. Secondly, the dynamic aspect of *guanxi* is overlooked. When the pre-existence of *guanxi* is not available but needed, there are alternatives, such as establishing and developing *guanxi*. Thirdly, all these kinds of *guanxi* seem based on utilitarian rational calculation, which is not true.

In fact, a broad sense of *guanxi*, which includes both family relations and other expressive relations, overcomes these deficiencies. Table 4.1 compares the two scopes of *guanxi*. Interpersonal relationships can be simply divided into blood or consanguineous relationships and social relationships. The former are family or kinship relationships, including one's family members, relatives, and often members of the same clan. Social

relationships mainly arise from social interaction outside both family and extended family settings.

Table 4.1 Comparison of broad and narrow term of *guanxi*

	Broad <i>guanxi</i>	Narrow <i>guanxi</i>
Types of relations	Consanguineous and social relations	Social relations outside family
Function	Expressive, instrumental	Instrumental
Terms	Expressive ties, mixed ties	Mixed ties
Sources	Endowment, saving, investment, building	Saving, investment, building
Norm	Obligation of affection, reciprocity	Reciprocity, but interest is main concerned

Broad *guanxi* comes from either endowment (*tianzi*), savings (*jielei*) or investment (*touzi*) (Wank, 1999, p123), while narrow *guanxi* does not contain *guanxi* from endowment. *Guanxi* from endowment are social relations by virtue of birth or “congenitally” (*tianshengde*) into a family or a particular economic class or bureaucratic rank. *Guanxi* of savings is acquired through life experiences that predate the entrepreneurial career in childhood, education, work and political experiences. A third route of *guanxi* accumulation is acquired after the onset of the business career by investment. To put it simply, the first kinds of *guanxi* are from family or extended family, while the latter two kinds of *guanxi* exist outside family.

Indeed, most discussions of *guanxi* suppose that it already exists. For instance, Solinger (1989) understands *guanxi* as family, friendship, co-worker, or schoolmate ties. What is the case for the individuals who anticipate the need to request a favour from someone but have not yet such *guanxi* with the person? Those without present *guanxi* can establish such relationships, or try to curry favour with such relationships, and turn the potentials for their personal ends (Hwang, 1987; Fei, 1992). Alternatively, joining certain associations can help to know people and build *guanxi* (Odgaard, 1992). Yang (1994) describes how gifts and banquets help to build and keep *guanxi*. But in fact, these are not enough for maintaining *guanxi*. Also, little research has examined what the bases are for developing *guanxi*. These, together with other strategies of having *guanxi*, will be addressed in Chapter 8.

In summary, many different types of *guanxi* exist in contemporary China. The most common forms continue to be based on kinship, family friendships, shared home area, educational ties, bureaucratic linkages, and so on so forth. On the one hand, all types of *guanxi* invest Chinese morality with a high degree of particularism and reciprocity; on the other hand, each type of *guanxi* has a different connotation and corresponding norm. In everyday life, and also in business, no one can expect in advance only to rely on 'utilitarian' types of *guanxi*. In this sense, *guanxi* is interpersonal relations in the broad meaning.

4.2 The reasons for the pervasiveness of *guanxi*

According to Yang (1989), the art of *guanxi* started to spread in practice about two or three years into the Cultural Revolution. *Guanxi* arose as a social response to the deep penetration of state power into everyday life and the politicalisation of social relationships during the Cultural Revolution, on which people relied to secure everyday survival against the collapse of social order. Since the reform and open policy, *guanxi* has become more and more prevalent. Therefore, the government's attitude toward *guanxi* is that people use *guanxi* to engage in official corruption and *guanxi* has detrimental impact on the good of the whole society. The practices are thus labelled "crooked wind" (*buzheng zhifeng*) and condemned by the official Chinese press, which include the use of public position for private gain, nepotism, patronage, factional favouritism, bribery, the exchange of special privileges of office among officials, and so on so forth. The government and media blame three reasons for the prevalence of *guanxi* practice. Firstly, it is based on tradition, which comes from China's thousands of years of feudalism, under which people had to rely on blood ties and clans for survival. Secondly, the Cultural Revolution forced people to rely on personal relationships to secure everyday survival since social orders were broken down. Thirdly, the practice arose from the influence of the "bourgeois individualism" of the West and "its ethic of self-gain" (Yang, 1994, p58-64).

The ordinary people have similar stance with the government with respect of denouncing *guanxi* practice. However, they admire and even approbate *guanxi*. This is because *guanxi* has the alternative relational ethics: the ethics of obligation, reciprocity, and mutual aid, and the responsibilities of friendship and kinship (Yang, 1994, p64-71).

Hwang (1987) comments that the instrumental use of *guanxi* arose and persisted in Chinese society because of cultural and structural factors. Through historical accident coupled with manipulation by political and cultural elites, in ways we cannot now unravel, the Chinese have developed an elaborate vocabulary for thinking about interpersonal obligations and how they can be won or lost. The structural factor explains why the practice is more popular in China, where a few power figures control major economic and other resources and arbitrarily allocate them; *Guanxi* becomes a useful way to solicit favour from the power figures.

It is true that the use of *guanxi* is in every facet of everyday life. *Guanxi* has become widely used to secure scarce commodities, from food and other consumables to housing and even hospital beds. It can help to obtain employment, to transfer jobs, including geographic mobility, and as well to get promotion (Yang, 1994).

Walder (1986, p187) believes that such a subculture is supported by the economic conditions. In the redistributive socialist economy, low levels of technical development, and poor transportation and communication networks, people have to rely on a bureaucracy of state distributors to dispense livelihood and discipline. Networks of instrumental personal ties are essential to the procurement of goods and services. On the contrary, in the market economies such as Japan and the United States, where commodities exist in abundance, factory officials do not have the wide personal discretion.

When talking about doing business in China, Arias (1998) argues that the dominance of *guanxi* in Chinese society is due to culture and to a lesser degree, institutional weakness and corruption. As a result, the Chinese market is conditioned by the reliance on trust relationships rather than on the enforcement of legal contracts.

In a word, the Chinese culture has a tendency of relying on *guanxi*. While the shortage economy forces people to adopt *guanxi* route for desired goods, unstable institutions foster the popular practice of *guanxi*.

4.3 *Guanxi* in business

Much has been written about the use of *guanxi* to acquire jobs, power, and resources in China (e.g., Gold, 1985; Walder, 1986; Lin and Bian, 1991; Bian, 1994; Yang, 1994). Still, available research on business mainly looks at the benefits of *guanxi*, which is defined as personal relations for favour exchanges based on reciprocity, mainly gift-giving, or bribery (e.g., Solinger, 1989; Bruun, 1993; Young, 1995).

In researching business before the reform era, Solinger (1989) finds that a downgrading of market exchange elevates the importance of non-market dealings. *Guanxi* had already acted as an aid to the informal collection of market intelligence, and eventually to control over goods; *Guanxi* also served sometimes as a supplement, but more often as a substitute, to gift-giving in the barter and bribery that attend the exchange of scarce goods. Since

money and goods are scarce, prices are controlled, and rationing, both formal and informal, dictates the legal distribution of key goods and services, *guanxi* helps to circumvent the restrictiveness of marketing regulations. In addition, in the absence of *guanxi*, exchange is far less likely to take place if one side lacks nothing the other can offer. Thus *guanxi* has facilitated trading.

Under the condition of reform in process, Luo (2000, p41) believes that *guanxi* has economic legitimacy because of high institutional uncertainties in China, which lack many of the mechanisms deemed necessary by conventional wisdom for a functioning market economy. Property rights are not well defined, channels for disseminating information on supply and demand are absent, while the bureaucracy dominates the social order. To deal with the Chinese bureaucracy and to reduce the uncertainties, Chinese people prefer to rely on their *guanxi* in power to get things done. As a result, *guanxi* constitutes a substitute for institutional support for business; it reduces operational uncertainties, including political uncertainty, and enhances economic returns. Also *guanxi* establishes a link for the flow of information on resource supply and demand, reducing information cost, promoting business effectiveness; *Guanxi* can spur the development of new market channels and render protection against contextual hazards.

In the same vein, Tao and Ho (1997) point out that China's private entrepreneurs have to face a highly vulnerable social status, anxiety about unpredictable government policies and the predominant economic opportunities, which profit from a highly versatile and

adaptable subcontracting network. It is therefore critical that entrepreneurs have *guanxi* networks to enhance flexibility and to co-ordinate production. They have to maintain close kinship and regional ties, particularistic relationships and other forms of *guanxi* for economic use to raise funds, to acquire industrial know-how, to gain access to supply of raw materials and to secure an abundant and reliable supply of other resources (Kraus, 1991; Young, 1995; and Wank, 1999). Odgaard (1992) finds that local government officials often used their control over key inputs as leverage over private enterprises, and also they could block licenses or approvals, cut off access to credit, and add new restrictions on private enterprises' activities. Moreover, when the government carried out austerity policies, private enterprises were always the target (Nee, 1989). Furthermore, private enterprises have to face exorbitant levies and sundry taxes (Bruun, 1993). To overcome these problems, many private entrepreneurs are forced to cultivate *guanxi* with government officials or state owned enterprises managers for favour.

Guanxi can bring some other benefits. A survey of Hong Kong Chinese executives found that businessmen believed that once good *guanxi* had been established, a number of benefits would follow, which included the smooth running of routine business operation, information about government policies, and receipt of administrative approvals (Davies *et al.*, 1995). Tsang (1998) asserts that *guanxi* can provide individuals and firms with an imperfectly imitable resource, which renders a distinct competitive advantage over others in doing business in China. Also, *guanxi* based business practices offer certain transaction cost advantages over existing structural alternatives, since where the *guanxi* network is

well developed, the transaction cost advantages of reduced environmental and behavioural uncertainties and opportunistic behaviour are sufficient to warrant the integration of *guanxi* and market based exchange (Standifird and Marshall, 2000)

4.4 Some deficiencies of *guanxi* in research on business

There are several problems with the available research. Firstly, most available research was conducted under the condition of the shortage economy, which has changed through more than two decades of reform; secondly, most research mainly examines *guanxi* with government and government officials, or suppliers, which is only one aspect of *guanxi*, and thus thirdly, other types of *guanxi* are ignored. Fourthly, some research on *guanxi* has led to a misconception of *guanxi*. In a sense, everything can be achieved with *guanxi* and without *guanxi* very little can be accomplished in China (CNN.com, January 19, 1999; Li and Li, 2000). In line with this, Davies *et al.* (1995, p209) claim that without *guanxi*, one simply cannot get anything done in China. In addition, to some extent, the researchers generalize *guanxi*, and go to two extremes. At the one end, *guanxi* is totally instrumental, in a sense, affection does not exist among family members and close friends, and people only have interest in material gains. At the other extreme, with *guanxi* at hand, it seems that rational economic choice is totally out of consideration.

To expand a little on the above points. First of all, most of the research is about *guanxi* under scarce economy, which forced people to use *guanxi* for desired goods. However, by

1993, the system of market allocation had stabilised, shortage had been alleviated (Whitcomb and Li, 1996). People in China can almost buy all what they need in the market. People have a common attitude that giving or paying money for a service is much simpler and more efficient than relying on *guanxi* (Yang, 1994, p163). As a result, money relationship has increasingly impinged on *guanxi* operation.

Secondly, all available research emphasizes *guanxi* with government and government officials who have control over resources. For example, it is believed that the success of Unicom-Sparkice, a joint Internet venture in Beijing, is due to the boss Mr Zeng's strength from his high-power government connections—*guanxi* (CNN, January 19, 1999). Given the many power structures and idiosyncratic, personal, and local nature of law and regulation in China, the importance of various forms of *guanxi* is not to be doubted. In a supplier market, *guanxi* with suppliers is undoubtedly crucial to business operation. That is fine, as far as it goes. However, with the progress of reform and economic development, the roles of government have changed, its political and administrative interference in business have declined. Government officials have not much control over the distribution of resources and products; on the other hand, markets are becoming increasingly competitive. More and more companies have found themselves on their own surviving without government subsidies (Guthrie, 1998).

The third deficiency is connected with the second point: the available research neglects *guanxi* with buyers, who are becoming more and more powerful in the competitive market.

Davies *et al.* (1995) identify four values of *guanxi* in developing business in China's market: procurement, information, bureaucracy, and transaction smoothing. The four factors except the last one are concerned with suppliers, the sources of resources, the information and bureaucratic approval of government. Some researchers have begun to realise this deficiency, and study *guanxi* strategy of marketing, in terms of relationship marketing (e.g., Wong and Chan, 1999). But such research is only a good start in a very general sense.

Also it is important to note that, since *guanxi* in business involves both instrumental and expressive elements, little attention has been paid to how to balance the two. Walder (1986, p179) finds that some kinds of *guanxi* are cultivated steadily over a long period of time and often develop into relationships that entail some human feelings between the parties. Other kinds are more short term, directly instrumental, and initial attempts at cultivation are close to the expected favour. The more distant the favour working and gift giving is from the favour expected in return, the more likely the *guanxi* involved includes *ganqing* (feeling), the less likely is it to appear as crudely instrumental on the part of the supplicant and as corruption on the part of the one who grants the favour.

In addition, according to most research, it seems that *guanxi* always has positive outcomes. But unfortunately, this is untrue. Furthermore, *guanxi* can also have constraints on actions. No researcher has yet clearly put forward this point. To some degree close to this argument, a few researchers discuss dilemma in *guanxi* relations (Hwang, 1987; Chen, 1995).

According to Chen (1995), *guanxi* brings obligations as well privileges, and these obligations can extend to "friends of friends" throughout entire networks. Thus the skilful practitioner of *guanxi* will as often as not consciously try to avoid linking him or herself too intimately with certain others so as to avoid being weighed down with obligations (cited in Lovett et al., 1999, p234). Hwang (1987) points out the dilemma in a *guanxi* relation is mitigated or worsened by the interaction of the three factors, the cost of the resource allocator, the anticipation of the resource petitioner's reciprocation, and social evaluations of other people from the same interpersonal network. In other words, the actions of *guanxi* ties are usually based on the careful weigh of the expected gain and loss. As a result, *guanxi* cannot always have positive outcomes.

Similarly, Chen (1994, p145) argues that in Taiwan, subcontracting is based on "weight of interest and affection". Which of the two elements weighs more depends on *guanxi* between the two parties, the contractor and the subcontractor. In this sense, business *guanxi* is the integration of the most measurable (interest) and the least calculable (affection).

4.5 *Guanxi* as a form of social capital?

In researching business in China, some researchers have started to look at *guanxi* as a form of social capital. Wang (2000, p538) defines social capital as social structure that enables cooperation, of which *guanxi* is a form. Wank (1999, p121) describes *guanxi* as a form of societal capital, which is believed by the researcher broader than social capital. Luo (2000,

p41) also discusses *guanxi* as a form of social capital, which creates economic value. Borrowing Bourdieu's (1986) definition, Luo looks at social capital as obligations, the advantages of connections or social position, and trust.

What is social capital then? Is *guanxi* simply a form of social capital? What is the relationship between social capital and *guanxi*? Literature review indicates that a systematic discussion about the two concepts is not available yet. The next chapter will attempt to fill in this deficiency and give answers to these questions.

Chapter 5 *Guanxi*: Chinese Social capital

The early chapter examined the concept *guanxi* and finds that some researchers have treated *guanxi* as a form of social capital. However, a systematic discussion about the two concepts has not yet been seen. This chapter aims to fill this gap and contribute to the literature. It firstly looks at what social capital is. Then it addresses the relationship between the two concepts, and the implications for research in social capital theory.

5.1 The popularity of social capital

Table 5.1 The increase in academic use of social capital

Year period	Number of articles
1951-1981	2
1981-1990	2
1991-1995	18
1996-2000	318

The term social capital is becoming more and more popular in the academic field. With the publication of *Making Democracy Work* (Putnam, 1993) and *Trust* (Fukuyama, 1995b), the concept has attracted much political and popular attention in North America (Wall *et al.*, 1998). This popularity is illustrated by the dramatic increase in academic use of the concept²² In forty years from 1951 to 1990, the term occurred only four times in the titles of journals. In the late 1990s, the term became fashionable in more and more journal

²² The finding is based on an examination of key words social capital for journal articles and theses written from 1951 to 2000. The library searches were conducted in March 2001 in BIDS International Bibliography of the Social Sciences, with social capital occurring in title/keyword/abstract fields in English language

articles. From 1996 to 2000, the number of articles using the concept increased spectacularly to 318 (Table 5.1).

Narayan and Woolcock (1999) identify a number of research fields in which social capital has featured prominently. These include (1) families and youth behaviour problems; (2) schooling and education; (3) community life; (4) work and organisations; (5) democracy and governance; (6) general cases of collective action problems; (7) public health and environment issues; (8) crime and violence; and (9) economic development. From Table 5.2, it can be seen that social scientists from various disciplines have contributed to the developing concept of social capital (Wall et al., 1998).

Table 5.2 Journal articles from different disciplines using social capital

General journal category	Pre 1981	1981-1990	1991-1995
Sociology/anthropology and related	9	26	46
Economics and business	3	14	21
Education	-	6	22
Development/planning/geography	7	5	13
Agriculture	-	4	2
Psychology	1	-	5
Total by period	20	55	109

Source: Wall et al. (1998)²³

Also, social capital theory has been applied to research on transitional economies. For example, Kolankiewicz (1996) takes contemporary Poland as a case to examine the

²³ Wall et al. (1998) conducted library searches at the University of Guelph in 1996 in the the following data bases: ABI/INFORM, AGRICOLA, ART INDEX, CAB ABSTRACTS, ECONLIT, ERIC, GEOBASE, HUMANITIES, PSYCLIT, and SOCIOFILE. The result was based on an examination of key words for journal articles and these written from 1981 to 1995.

emerging process of class formation attendant on privatisation and democratisation, by using social capital theory. Dinello (1998) examines the social capital of Russian bankers who are perceived as the prime movers of Russia's transition to the market. Clark (2000) proposes an approach from the social capital perspective to examine the socially constructed process undertaken by business founders in the transition of the Czech Republic.

5.2 What is social capital?

An increasing number of social scientists refer to social capital as the information, trust, and norms of reciprocity inhering in one's social networks (Woolcock, 1998). However, the term social capital is subject to a variety of interpretations by users from different trends in dominant thinking and particular perspectives. Schuller (2000) points out that social capital seems to be a flexible term that can be fixed into different settings. Inter alia the popularity of the notion of social capital may be its fluidity, the fact that it can be used in so many different ways and in different contexts. Wall *et al.* (1998) finds that, in the early 1970s, social capital was defined in very tangible ways by economists, namely as physical infrastructure or financial asset. Here, social capital can mean the totality of all forms capital: natural, economic, or human. Other researchers equated social capital with certain expenditures of the state. In sociology and interdisciplinary social sciences, social capital has only been used more recently. For them, it has somewhat distinctive meaning. The following sections examine three main streams of social capital theory in literature.

5.2.1 Social capital according to Putnam and Fukuyama

Putnam's (1993) notion of social capital is most dominant and fashionable in development studies. Putnam (1993) relies on the idea of social capital to address the questions about the necessary conditions for creating strong, responsive, and effective institutions in different regions in Italy. He strongly emphasises the vibrancy of associational life and an informed public as a necessary condition for a healthy civic community. Social capital is measured by voting patterns, newspaper readership, and participation in sports and cultural associations. For Putnam (1993), social capital includes trust, norms, and networks; each enhances co-operative actions, persists in the long run and re-asserts itself under suitable circumstances.

Fukuyama (1995a, 1995b) examines social capital in countries, a broader level than Putnam's (1993) regions. In an attempt to explain why some countries have been more economically successful than others, Fukuyama (1995a, 1995 b) treats social capital as trust, the ability of people to work together for common purposes in groups and organisations. He compares a number of countries in terms of their social capital strength, and concludes that high levels of sociability (social capital) and loyalty make individuals work co-operatively in the corporations that drive the economy and ensure prosperity.

Many researchers (e.g., Leonardi, 1995; Evans, 1996; Knack and Keefer, 1997; Cohen and Field, 1999; Fedderke *et al.*, 1999; Hall, 1999; Hofferth and Iceland, 1998; Kyle, 1999;

Paxton, 1999; Temple, 1998; Temple and Johnason, 1998) are in the same line with Putnam (1993) and Fukuyama (1995a, 1995b). They generally look at social capital as norms of horizontal association or the social and political environment that enable such norms to develop, and trust. In other words, social capital is the norms of cooperative action.

5.2.2 The origin of social capital

According to Wall *et al.* (1998), although social scientists have figured in developing the concept of social capital, the term has only been used by academics in recent times. This is indicated by the fact that the term is not found in any of the following encyclopaedic references: *Encyclopaedia Sociology*, *Encyclopaedia of the Social Sciences*, *International Encyclopaedia of the Social Sciences* and *Survey of Social Sciences*. There is one exception though, in the *Encyclopaedia Sociology*, the term social capital is mentioned under the title of “social network theory”, described as a “prominent theme” in writing about the purposive use of networks. In the newly published *Sociology* edited by Fulcher and Scott (1999), the term social capital is not mentioned; instead, cultural capital is explained.

What is the origin of social capital? Astone *et al.* (1999) argue that the concept of social capital originated in sociology and is being widely incorporated into much current social science. Recent empirical studies using the term social capital almost always refer to a

widely read article by an American sociologist James Coleman (1988), which was later revised and presented in his book *Foundation of Social Theory* (1990). Sobel (2002, p145) finds that nearly all of the papers in the World Bank volume on social capital (1999) cite Coleman's paper (1988 or 1990). It is found that Putnam (1993, p167), an American political scientist at Harvard University, who contributed greatly to the popularity of the concept, in fact borrows Coleman's (1990, p302, 304, and 307) definition of social capital by quoting 'Like other forms of capital, social capital is productive...' and concludes that 'spontaneous cooperation is facilitated by social capital'. But it must be noted that his own concept of social capital goes beyond Coleman's (1990).

In the same vein, Paxton (1999) points out that the term social capital remained obscure until Bourdieu and Coleman popularised it, though a number of authors, from a variety of fields, used it. Therefore, Wall *et al.* (1998, p300) argue that 'social capital has gained currency over the last decade, spurred in large part by the work of James Coleman and Piere Bourdieu.' It is commonly agreed that the concept of social capital was introduced by two major social scientists Bourdieu and Coleman.

5.2.3 Coleman's version of social capital

Coleman (1988) studies a sample of public school students in the USA to establish the links between social and human capital. Based on the assumption that different family structures create different levels of social capital available for children, Coleman

operationalised social capital into six factors. The six factors are the parents' presence in the home, the number of additional children present, the different combinations of parents and siblings, the mother's expectation for a child's education, the mobility of the family, and the church attendance. He finds that school dropout rates are low when social capital is high, i.e., when both parents are present in the home with one sibling, a mother expects the child to attend college, there is little family mobility, and there is a religion affiliation.

Building his theory on the work of Loury (1977), Granovetter (1973, 1974, 1985), and Lin (1981, 1982), Coleman (1988, 1990) defines social capital by its function: 'social capital paralleling the concepts of financial capital, physical capital, and human capital, but embodied in relations among persons.' (1988:s118). The concept of social capital illustrates how the social structure of a group can function as a resource for the individuals of that group. Social capital is productive, making possible the achievement of certain ends that in its absence would not be possible. There are three forms of social capital: 1) obligations and expectations based on trustworthiness of the social environment, 2) information-flow capacity of the social structure, and 3) norms enforced by sanction.

Coleman (1988, 1990) claims that social capital inheres in the structure of relations between and among actors. In family, social capital is the relations between parents and children. Outside the family, social capital is the social relationships that exist among parents. To summarise for Coleman, social capital is obligations and expectations, information, and norms existing between and among social relations.

5.2.4 Bourdieu's concept of social capital

Based on Marxist analysis, Bourdieu introduces a more complex class notion than the concept of class as a system of property rights and seeks to reveal the indispensable contribution that the consumption of symbolic goods makes to reproducing class domination through legitimation and selection (Gartman, 1991). Bourdieu (1986, 1993) introduces a more complex class notion, where he explores social class in terms of volume and structure of capital. Different forms of capital, i.e., economic capital, cultural capital, and social capital are taken into account.

Bourdieu's concept of capital is broader than the monetary notion of capital in economics. Bourdieu (1986, p241-243) defines capital as "accumulated labour (in its materialised form or its 'incorporated', embodied form) which, when appropriated on a private, i.e., exclusive, basis by agents or groups of agents, enables them to appropriate social energy in the form of reified or living labour". Capital presents itself under three fundamental species: economic capital, cultural capital, and social capital. Each of them has its own subtypes.

Economic capital is immediately and directly convertible into money and may be institutionalised in the form of property rights. Economic capital refers to financial resources and assets, in which a good example is monetary income.

As a matter of fact, Bourdieu pays much more attention to cultural capital. Cultural capital in fact should be called information capital to give the notion in its full generality, which itself has three forms, embodied, objectified, and institutionalised (Bourdieu and Wacquant, 1992).

Cultural capital consists of various cultural advantages that can be turned into economic gains. Bourdieu (1986, p246) identifies three forms that it can take: 1) the embodied state, which consists of what Bourdieu calls “long-lasting dispositions of the mind and body”, in other words, this is the culture that we carry around with us in our head, such as knowledge and habit; 2) the objectified state, which is the culture found in "things", existing in possessions, such as books or paintings or clothing; 3) the institutionalised state, which is typically represented in formal education qualifications. Therefore, certain ways of thinking and speaking, or a stock of cultural possessions, or examination certificates can all present people with cultural advantages. The term cultural capital reflects the importance of culture in education, in occupational success, in a word, in social status.

Acquiring cultural capital is not just a matter of passing examinations and gaining qualifications. Bourdieu suggests that correct manners, the right tastes, say, in dress, and an appreciation of high culture are all part of cultural capital. They can be crucial in determining whether someone gets a high status job or gains admission to elite circles.

Social capital is 'the aggregate of the actual and potential resources that are linked to the possession of a durable network of relationship or mutual acquaintance and recognition' (Bourdieu, 1986, p248). Social capital is thus the sum of the actual and potential resources that can be activated through membership in organisations and social networks. Bourdieu (1993, p33) explains that 'one can give an intuitive idea of it by saying that it is what ordinary language calls connections'.

From the above, it is found that the central proposition of social capital theory is that networks of relationships constitute a valuable resource for the conduct of actions, providing their members with collectively owned capital, a credential that entitles them to credit. There are several sources of social capital. Firstly, much of social capital is embedded within networks of mutual acquaintance and recognition. Secondly, social capital is available through the contacts or connections networks bring. Thirdly, social capital can be derived from membership in specific networks, where such a membership is restricted (Nahapiet and Ghoshal, 1998). In short, from the variety of definitions of social capital, it is concluded that social relationships are a common element. As Astone *et al.* (1999) have commented, the use of term social capital to refer to the resources that emerge from one's social ties is exceedingly popular.

5.3 The relationship between *guanxi* and social capital

From the above, it is found that *guanxi* and social capital are two analogous concepts.

The overlap of the two concepts is apparently reflected in the origins of social capital that advanced Coleman's (1988, 1990) theory. Loury (1977) uses social capital as a set of resources inhering in family relations and in community social organisation, which is useful for the cognitive or social development of a child or young person.

Lin (1982) defines his concept of social resources as resources embedded in one's social network, which are accessible through one's direct or indirect ties. Earlier than Lin, Granovetter (1973, 1974) was centrally concerned with how people use their social relationships for instrumental goals. Not surprisingly, their successor Coleman (1988, 1990) identifies social relations in family and outside family in community as social capital. Both *guanxi* and social capital involve social relations, the norms that undergird them, and the positive consequences of having such relations. Nonetheless, this does not mean that social capital is all about *guanxi*, or *guanxi* is another term for social capital. Besides several common aspects, there are some differences.

For instance, social capital is regarded as both the attributes of individuals and organisations by Coleman (1988, 1990) and Putnam (1993); while *guanxi* is mainly about interpersonal relationships, which are rather difficult to transfer into an organisation attribute. The relationship between *guanxi* and social capital, more precisely, the three main streams of social capital theory, can be better understood as illustrated in Table 5.3.

Table 5.3 Comparisons between *guanxi* and the three main social capital theories

	<i>Guanxi</i>	Bourdieu	Coleman	Putnam
Components	<i>Guanxi</i> relations, trust, norm of reciprocity	Networks, obligation	Social relations, obligations, information and social norms	Civic association, reciprocity, and trust
Location	Personal networks	Personal networks	Between and among actors	Organisation (civic association)
Sources	<i>Guanxi</i> networks	Connections	Family & Community	Networks of civic association
Attributes	Individual	Individual	Both individual and community	Organisation (community, region)
ownership	Private	Private	Public	Public
function	Instrumental	Instrumental	Instrumental	Instrumental
How produced	Building, Saving, Investment, and endowment	Mainly endowment, also investment	By-product of investment	By-product of investment
Norm	Reciprocity	Obligation	Reciprocity	Reciprocity
Trust	Particularism	Not mentioned	Part of norm	General
Affection	Involved	Likely	Not concerned	Not concerned

Firstly, both social capital and *guanxi* involve social relations. It is social relationships between and among actors that structure social capital for Coleman (1988, 1990). Bourdieu (1986) explicitly explains that network of social relations are social capital. Membership in a civic association for Putnam (1993) provides its members a form of social relationship. Although Putnam stresses that civic association cutting across social cleavages nourishes wider cooperation, he admits that strong interpersonal social relations, such as kinship ties,

play a role in collective action. Indeed, social capital is popularly defined as the resources that emerge from one's social ties (Astone *et al.*, 1999).

Secondly, both *guanxi* and social capital are instrumental, and they are actually or potentially productive. *Guanxi* is defined as instrumental social relationships. As Gold (1985) notes, instrumentalism is an extraordinary characteristic of *guanxi* in China today. In the available literature, social capital is also described as playing a functional and positive role in outcome. As an instrument, when social capital is present, it increases the capacity for action and facilitates various ends for the members of a group and also the group as a whole. A good example of the productive outcome of social capital is in building human capital (Coleman, 1988). For Bourdieu (1986), social capital is directly usable in the long or short term, and can be converted into economic capital. According to Putnam (1993), social capital of trust and civic engagement foster collective actions and thus institutional success in the broader community or region results, making democracy work.

Thirdly, the benefits of social capital and *guanxi* are reinforced by the norm of reciprocity. Norms define what actions are considered acceptable or unacceptable, and can be seen as the basis of social capital (Coleman, 1990). As argued in the previous chapter, the norm of reciprocity, *bao*, is an essential component of *guanxi*. Like many other theorists, Putnam (1993) suggests that norms are important ingredients of social capital, the most important of which is reciprocity. Together with trust and network, norms enhance co-operative

actions. Without using the term of reciprocity, Bourdieu (1986) implicitly talks about the norm of social capital as durable obligations subjectively felt. Coleman (1988, 1990) points out that obligation, as a form of social capital, depends on two elements, trustworthiness of the social environment, which means that obligations will be repaid, and the actual extent of obligations held. Accordingly to Gouldner (1960), reciprocity is one of the universal norms, and principal components of moral codes. It is a concrete and special mechanism involved in the maintenance of any stable social system.

Besides these similarities between the two concepts, there are differences. One differentiation lies in the different levels of analysis. These result in different understandings of where the good locates. In turn, this leads to two further distinctions, one is how to produce social capital or *guanxi*, and the other is the difference in the nature of trust.

Firstly, theorists have different views of the sources of social capital. Bourdieu (1986) has a similar stance with *guanxi*. Personal networks are the sources of social capital. Unlike Bourdieu (1986), Coleman (1988, 1990) suggests that both family and community provide social capital for individuals; while Putnam (1993) regards networks of civic association as the sources of social capital.

Different understandings of the sources of social capital and *guanxi* derive from different analysis levels by the theorists, to a great extent. To some researchers, social capital, like

guanxi, is a private good that can be used for private purpose. Both Bourdieu and Coleman write about social capital as an attribute of a person. There is some other research in this line that sees social capital as resources for individuals, for example, Anheier *et al.* (1995), Astone *et al.* (1999), Burt (1992, 1997a, 1997b, 1999), Clark (2000), Dinello (1998), Kolankiewicz (1996), Pahl (1996), Rose (1998), and Sanders and Nee (1996).

However, represented by Putnam (1993) and Fukuyama (1995a, 1995b), more theorists consider social capital in a broader sense (e.g., Putnam, 1993; Evans, 1996; Fedderke *et al.*, 1999; Hall, 1999; Hofferth and Iceland, 1998; Kyle, 1999; Knack and Keefer, 1997; Leonardi, 1995; Neace, 1999; Paxton, 1999; Temple, 1998; Temple and Johnason, 1998). Putnam (1993) defines social capital as the attributes of social organisation. Social capital is seen as a macro-sociological phenomenon, or a character of a community, and thus social capital is a public good and a community resource. For the theorists in this line, the whole community, from regions to entire nations, can hold different levels of social capital, which in turn enhance the chances of positive outcomes, such as, development and democracy.

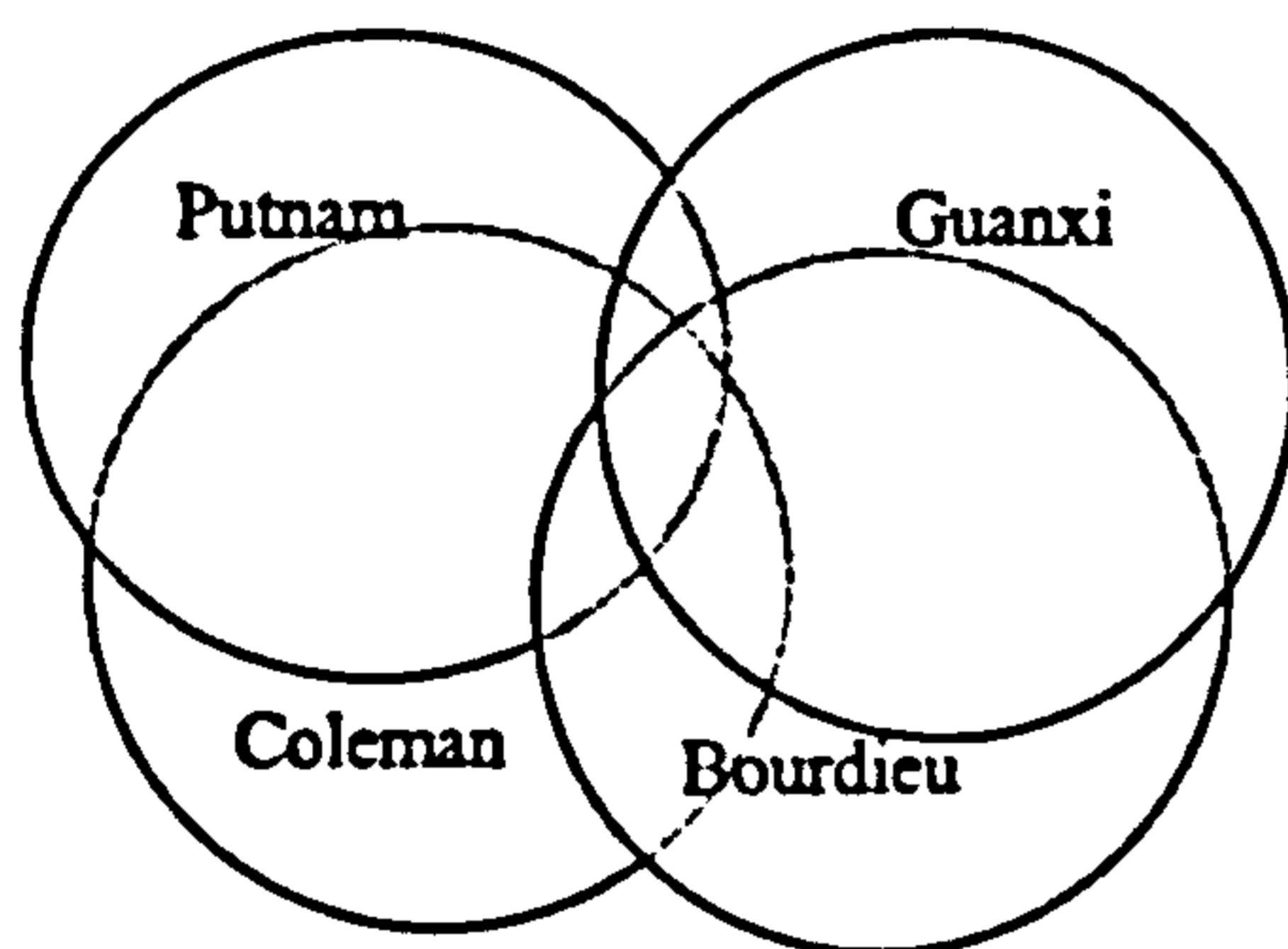
Coleman (1988, 1990) treats social capital as a feature of both individuals and community. For both Putnam (1993) and Coleman (1988, 1990), social capital is a public good that is beneficial to everyone in a community. This diverges from Bourdieu's (1986) social capital and *guanxi*. Like *guanxi*, Bourdieu's (1986) social capital is a private asset that only serves those individuals who hold such connections.

Secondly, in regard to how the intended outcome of social capital or *guanxi* is produced, theorists have different visions. Both Coleman (1988, 1990) and Putnam (1993) believe that social capital, as a public property, is the by-product of other social activities, such as participation in choral societies, sports clubs, etc. Like *guanxi*, social capital of Bourdieu (1986) is not necessarily a natural given; instead, it is the product of investment by individuals who consciously or unconsciously aim at establishing or reproducing such social relations. The investment implies expenditure of time and energy, which in turn means directly or indirectly expenditure of economic capital.

Thirdly, *guanxi* and social capital do not share the same understanding of the nature of trust. Luhmann (1979) divides trust into two categories, interpersonal trust and institutional trust. Interpersonal trust is based on experience, while institutional trust is built on stable and clearly defined institution other than individuals. People rely on institutional trust to deal with unfamiliar settings, to anticipate and make decisions. In the same vein, Paldam (2000) suggests that trust can be simply divided into generalised trust and special trust, where generalised trust is defined as trusting people in general; while special trust is to trust known people or trust in particular institutions. Clearly, both interpersonal trust and special trust can refer to trust from *guanxi*, known people, while generalised or institutional trust is close to Putnam's (1993) concept of trust and Coleman's (1988, 1990) trustworthiness of social environment.

There are two further differences. Firstly, an affective element is involved in *guanxi* exchange. It is also compatible with Bourdieu's (1986) account. However, affection is not the concern of Putnam (1993) and Coleman (1988, 1990). Secondly, *guanxi*, the term developed in the Chinese discourse, has ethical controversy in terms of its blurred boundary with corruption. However, social capital seems to involve no ethical problem; instead, it is a good that promotes positive outcomes, for instance, economic development.

Figure 5.1 Representing overlap between *guanxi* and the three main social capital theories



In conclusion, *guanxi* and social capital are two overlapping terms. They have common ingredients, such as the existence of certain social relationships, the norms of such relationships, and the outcome of them. Nevertheless, *guanxi* is most approximate to Bourdieu's (1986) notion of social capital, which is mainly looked at from the relational dimension of social capital to refer to the actual and potential resources embedded within, available through, and derived from the network of relationships possessed or created by an individual (Nahapiet and Ghoshal, 1998). Moreover, like Coleman (1988, 1990) and Putnam (1993), *guanxi* has also another important ingredient, trust, though they have

different understandings of its nature. This is not of Bourdieu's (1986) concern. *Guanxi* and Bourdieu (1986) are similar in terms of analysis level and the way of producing the property. However, both Coleman (1988, 1990) and Putnam (1993) have different understandings from *guanxi* and Bourdieu in these two aspects. The relationships between *guanxi* and social capital are demonstrated in Figure 5.1. *Guanxi* and the three versions of social capital overlap each other. However, *guanxi* is closest to Bourdieu's social capital and thus overlaps more with it; while Coleman and Putnam have much more in common with each other and may be thought of as a different North American variant (Wall *et al.*, 1999).

5.4 Conclusion

Popular usage of the term social capital has emerged among various social science disciplines. The concept provides a useful analysis tool for social scientists. However, there exist two outstanding deficiencies. Firstly, extensions of the concept in recent writings, from an individual asset to an attribute of communities and even nations, may jeopardise its heuristic value. 'As a property of communities and nations rather than individuals, social capital is simultaneously a cause and an effect' (Portes, 1998, p16). Sobel (2002, p146) has also found that some authors, led by Coleman and Putnam, at times equate the existence of social capital with outcomes obtained using social capital.

Embedded in communities, social capital is mobilised by individuals of the communities who pursue their personal gain; it does not provide each member with the same chance and the same gain. The formal associations, advocated by optimistic social scientists like Putnam (1993), may only be a small factor in the production of social capital or trust (Lyon, 2000). Furthermore, the same strong social ties that help some members of the community also enable them to dominate and exclude others (Mcclenaghan, 2000). Similarly, Sobel (2002) points out that the ability to use network relationships need not be good for society or even for the network. For example, using blockmodeling procedures to analyse data on German writers, Anheier *et al.* (1995) find that in the community of culture fields, significant differences in both culture and social capital distinguish elite from marginal writers.

Communities become the venues for the individuals seeking social resources for their personal ends. The nature of communities has changed and been extended from the traditional locale-based notion of a community. As Falk and Kilpatrick (2000) argue, the life of communities tends to be community-of-common-purpose. Communities, where social capital locates, are a set of personal, ego-centred social networks rather than spaces (Lomnitz, 1999). In many circumstances, these benefits of social capital come at the cost to individuals outside of the group (Sobel, 2002, p146).

Secondly, the bulk of research using the concept of social capital is focused on the consequences of possessing or not possessing an adequate amount of social capital, but

little research has been done on how it is brought into being (Astone, *et al.* 1999). The importance of social capital lies in how social capital helps to achieve personal ends. Social capital is like a kind of precious mine under the earth, without the labour of human beings, its value would never be realised.

It is found that an individual's access to social resources is instrumentally important, and people therefore invest in each other to gain future access to different resources (Lin *et al.*, 1981; Lin, 1982). A high social status of the other person has a positive influence on the decision to invest in relations (Van Duijn *et al.*, 1999). A precondition to building social capital is the existence of sufficient numbers of interactions of a particular quality (Falk and Kilpatrick, 2000). In line with the classic work on the gift by Mauss (1969), Eisenstadt and Roniger (1999) argue that the latent function or purpose of the gifts is to establish the obligation to engage in social interaction and to uphold those obligations entailed in such interaction.

Social capital provides only an instrument for personal gains, how to transfer social capital into the gains is in fact more important (e.g., Astone *et al.*, 1999; Pahl, 1996). In this aspect, both Bourdieu (1986) and *guanxi* can contribute to the richness of social capital. Bourdieu (1986) has pointed out that people will deliberately join certain clubs that provide social capital. Unfortunately, Bourdieu has never put his theory into empirical research. Furthermore, as noted previously, clubs, a form of community-of-common-purpose (Falk and Kilpatrick, 2000), cannot provide their members with equal social capital. For instance,

joining certain associations can lead to knowing people and building *guanxi* (Odgaard, 1992), but this is only a start point for obtaining social capital or turning the potentials for their future use. What are the other bases for establishing *guanxi*? Are there any other strategies that solve the problem of one's own lack of *guanxi*?

In this sense, research on *guanxi* practice, in particular, the creation of social capital, e.g., building *guanxi*, and investment to produce obligations, can contribute greatly to social capital theory. From this perspective, *guanxi* or *guanxi xue* has a great advantage in understanding how social capital comes into being. What are different types of *guanxi* accessed for business start-ups? How do they come into beings? When entrepreneurs do not have available *guanxi*, how do they establish *guanxi*? Are there any other alternatives? These become the main task for the case studies of this thesis.

Part 3 Case Studies

Chapter 6 Self-reflective methodology: *guanxi* approach

The previous two chapters examined the two key concepts of *guanxi* and social capital of this thesis. It further argued that *guanxi* with cadres are not always useful, as most research had imagined. Such *guanxi* have also constraints. In addition, *guanxi* can be built and developed. With an aim to demonstrate these points, this chapter will describe and analyse how this researcher utilised a *guanxi* approach to conduct field research.

The methodology for the case studies is snowball sampling by a *guanxi* approach, i.e., exploiting *guanxi* to conduct field research by using the initial *guanxi* to 'snowball' and gather additional contacts as informants. This was done in Beijing during the five months from early May till late September 2000. Snowball sampling seeks to take advantage of the social networks of identified respondents to provide a researcher with an ever-expanding set of potential contacts (Miles and Huberman 1994; Thomson, 1997). Thus, snowball research methodology is a very good strategy to access "hard-to-research" populations (Atkinson and Flint, 2001). However, none of the above mentioned methodology is about *guanxi* approach.

Yeung (1995) find that the most important issue in research in China appears to be the ability of solving the problem of "getting in", that is, to form relationships or *guanxi*. If one has no referrals or *guanxi*, he or she is not likely to get any insightful information (Davies *et al.*, 1995). However, little research has been done from a first hand experience to

demonstrate how researchers solve the problem. This research methodology fills such a gap.

6.1 Reflective methodology

This chapter is therefore an autobiography of my field research. Biography and autobiography are also closely articulating with the lives of others (Stanley, 1992). "From the (autography or biography of) a person we can recover social process and social structure, networks, social change and so forth, for people are located in a social and cultural environment which constructs and shapes not only *what* we see but also *how* we see it" (Stanley, 1993, p45). Autobiography and biography provide an important source, through which it is possible to see how specific individuals internalise particular social expectations and aspirations. Furthermore, they could offer sociologists the chance to understand the social environment in which the individuals act as social being (Evans, 1993). Similarly, Cotterill and Letherby (1993) point out that autobiography and biography not only record the life of one individual, they are also documents of many lives. Thus they are also relevant to the academic empirical research of sociology.

However, sociology has been slow to use the writer her/himself as a source to develop a reflexive analysis for sociological discussion (Ribbens, 1993). This autobiographical account describes how the researcher used the *guanxi* approach to conduct field research.

Therefore, the research methodology *per se* provides a unique reflective “window” to the understanding of *guanxi*.

6.2 Choosing the field site

I chose Beijing as my field research site mainly for two reasons. Firstly, private high-tech enterprises have become the pillar of Beijing’s economy (*China Daily*, 23 October 2000). Beijing Zhongguancun High-tech Park, where most high-tech firms are located, plays a demonstration role to other domestic Science Parks (Wang, 2000). Secondly and more importantly, I have *guanxi* in Beijing where I have lived for more than ten years. In particular, I have a network of *guanxi* covering many government organisations after several years of work in a central government department. I had thought that these ties would help me to access private entrepreneurs in the field site, as much research suggested the power and control of government departments and private business association over the private sector (see Odgaard, 1992; Bruun, 1993; Young, 1995; Wank, 1996 and 1999). The relationship between private entrepreneurs and government officials is patron-clientelist (Wank, 1999). This proposal was configured by my vision of choices embedded in my *guanxi* structure – my personal relation network in government departments.

6.3 Introduction of Zhongguancun High-tech Park

Beijing, the capital city of China, has a population of 12.4 million. In 1998, its gross domestic product (GDP) was RMB 201 billion (US\$ 24 billion); the industrial output was RMB 171.5 billion (US\$ 20.7 billion). By the end of 1998, there were 61,113 private enterprises, whose average registered capital was RMB 620,000 (US\$ 75,000) (BPIA data, 2000).

Located in Haidian District in Northwest Beijing, Zhongguancun was initially the name of a place adjacent to the campus of Peking University. In the early 1980s, some researchers began to run non-state technology firms in Zhongguancun. Because at the beginning, most of the firms sold electronic products, Zhongguancun got the nickname "Electronic Street". Since May 1988 when the State Council approved the establishment of Haidian Experimental Zone for the development of high and new technology, Zhongguancun has grown up from an "Electronic Street" to a leading hi-tech park in China. On June 5, 1999, the State Council, the Chinese cabinet issued its official written reply on the construction of Zhongguancun. Zhongguancun High-tech Park is now a state level high-tech park.

Zhongguancun covers 68 universities and 213 research and development (R&D) institutions including the Chinese Academy of Sciences, Peking University and Tsinghua University. It makes thousands of R&D discoveries every year (*China Daily*, January 25, 2000). According to *Economic Daily* (May 8, 2000), there are more than 6,600 high-tech²⁴ companies in the park, which include well-known Chinese companies such as

²⁴ China has a relatively systematic and comprehensive listing of high-tech technology products in various sectors with detailed technical definitions. According to *The List of China's High-Tech Technology Products*

Stone, Legend and Founder. Their utilisation of new technologies has contributed to nearly 50% of this industry. There are also more than 1,000 foreign-invested enterprises.

During the past decade, IBM, Microsoft, Intel, Motorola, Hewlett Packard, Mitsubishi and dozens of other world-renowned companies have set up R&D centres in Zhongguancun or its surrounding areas. Domestic companies are also locating their R&D centres in the park. Some famous companies, such as Founder, Legend and Stone, are now devoting an average of 8% of their overall technological, industrial and trade revenues to R&D. Zhongguancun is thus called the Chinese Silicon Valley.

In the past ten years, Zhongguancun has had an annual economic growth rate over 30 per cent. In 1999, its 6,690 high-tech and new-technology enterprises earned RMB 86.41 billion (US\$ 10.4 billion) in revenues. The value of these companies' gross industrial output in 1999 was RMB 52.7 billion (US\$6.4 billion, current prices). The increase in the value of Zhongguancun's gross industrial output was so substantial that it accounted for 70% of that of Beijing in 1999.

Zhongguancun's importance is demonstrated by the fact that it leads China's 53 high-tech and new-technology zones in total revenues. In addition, Zhongguancun's enterprises

released on Sept. 28 2000 by China's Ministry of Science and Technology, the State Commission of Economic and Trade, and the State Administration of Taxation, high-tech products were 2,056 items in 11 sectors. The 11 technological areas are: electronic information, software, aerospace, integrated photo-mechanical-electrical technology, biology, pharmaceutical and medical equipment, new materials, new energy and high-energy, efficient devices, environmental protection, atmosphere and ocean, material utilization technology and agriculture (*Xinhua News Agency*, September 28, 2000).

produce about 10% of Chinese high-tech zones' revenues, gross industrial output and before-tax profits (*Economic Daily*, May 8, 2000).

Beijing's municipal government announced ambitious goals for its Zhongguancun Hi-tech Park²⁵. These goals include Zhongguancun enterprises generating annual revenues of RMB 110 billion (US\$13.3 billion) in 2000 and RMB 600 billion (US\$72.6 billion) within 10 years (*Beijing Youth Daily*, January 30, 2000).

6.4 Proposed paths to access interviewees

As stated in the aforementioned section, the decision to conduct field research in Beijing derived from self-confidence in my *guanxi* accumulated in more than ten years of study and work in the city. The paths to access interviewees were accordingly supposed to be in existence. Before action, I had a brainstorm by going over my old and shabby name and

²⁵ After the new plan on Zhongguancun Hi-tech Park was published, all the hi-tech parks in Beijing are generally called Zhongguancun Hi-tech Park. The new Zhongguancun Hi-tech Park consists of three zones: center zone, development zone and radial zone. The center zone has an area about 75 square kilometers, which is bounded by the Xiwai Street in the south, the Planned Fifth Ring Road in the north, Jingmi Canal in the west, and Badaling Great Wall Expressway in the east. The core of the center zone includes Chinese Academy of Science, Peking University, Tsinghua University, and west zone of Zhongguancun (science & technology business center, sale center, and business & culture service center).

The center zone is the traditionally and popularly recognised location of Zhongguancun High-tech Park, and is the field site for this research. The development zone and radial zone are not of concern in this research, and thus are not given further description. For further details, see Beijing Municipal Government, Ministry of Science and Technology (PRC), "Request for instruction on actualizing the strategy of flourishing country by science and education, and accelerating the construction of Zhongguancun High-tech Park", Beijing Policy file [1999] No.35.

address book, which contains contact details of all my *guanxi*: friends and familiar acquaintances. I wrote down a list of people, who, I thought, could help introduce private entrepreneurs as my interviewees. The proposed paths are shown in Figure 6.1 (see p172).

I started from the “embedded structure”---- government line, where I have a number of *guanxi* after working for more than seven years in a central government department. The first government department I decided to contact was Beijing Policy Research (BJPR). This was based on three considerations. Firstly, it is an influential think-tank body of Beijing municipal government, and thus it can help. Secondly, being responsible for providing policy advice to the municipal government, it may be interested in my research. Thirdly and more importantly, I had dense *guanxi* there: three friends, with A1 as the head of the department and A2 and A3 both as middle chiefs under A1’s supervision.

Soon I found that A3 had gone to Hong Kong to join her husband. A2 had moved to a new post outside the think-tank. A1 is in a very high position of the government’s hierarchy. He is always very busy and it is very difficult to get hold of him. As status matters – relationships with a senior will extend to his subordinates (Arias, 1998), it should be a good path to get me through to the officials in Zhongguancun High-tech Park, who would in turn introduce me to private entrepreneurs under their jurisdiction. In China, which is a rather hierarchical society, if one has rich and influential friends, one can surely draw on more resources (social capital), if it is needed, than if one has poor friends far from the seats of power (Lin, 1995). I thus kept on calling him with a great expectation. I finally

caught him on the telephone and explained to him my research plan. He discussed with me about my research topic for a while and told me clearly,

I know few private entrepreneurs myself as you know we don't have direct contact with them. Yes, I have good *guanxi* with the heads of the research offices under Haidian District (where the high-tech park is located) government and Zhongguancun High-tech Park, but as far as I know they do not have any good means to access private enterprises themselves.

At this point, I gave up this line of enquiry. It may be assumed that government agencies without direct interaction with enterprises would have difficulties in accessing them. Can the officials from government departments in charge of private enterprises help me access private entrepreneurs?

The second proposed paths were Beijing Bureau of Industry and Commerce (BBIC) and Beijing Federation of Industry and Commerce (BFIC)²⁶. It is well known that the Bureau of Industry and Commerce has the power to issue business licences to enterprises, and several friends strongly recommended it as the best route to access private enterprises. I began from the superior of BBIC, the State Bureau of Industry and Commerce (SBIC), where A4 and some other friends of mine are in important positions such as the aide to the minister. However, A4 suggested me not to go to their subordinate,

²⁶ A semi-government organisation under the auspice of the Department of United Front Work (DUFW) of the Communist Party. Nationally, there is All China Federation of Industry and Commerce (ACFIC). The federation is said to represent entrepreneurs, mainly from the private sector.

You know our staffs have only one-time contact with an enterprise, or once a year when the enterprise comes to renew its licence. In general, the frequency of contact is not enough for them to build up intimate *guanxi* with firms. We bet the outcome would be better if you try Beijing Federation of Industry and Commerce (BFIC), which is authorised by the government to administrate private entrepreneurs.

They thus got me through to Mr Shi, the head of the research department of Beijing Federation of Industry and Commerce (BFIC), who was responsible for the 2000 National Survey on Private Enterprises in Beijing area. Mr Shi told me frankly,

I was allocated 100 questionnaires of the National Survey on Private Enterprises from the All China Federation of Industry and Commerce. I assigned them to the 18 districts and counties. I am not very clear about how they will finish their task in detail yet. We do not have full time staff responsible for the survey, and I presume that they will have to fill in the questionnaires in passing when they visit some enterprises. I will go with them to visit some private firms. If you would like to join us, no problem at all. But if you have your own questionnaire for the entrepreneurs to fill in, it will be a bit difficult. You know, we the Federation of Industry and Commerce, aim to unite (*tong zhan*) the private sector. We are supposed to serve private enterprises. Since we cannot help them much, we'd better not trouble them too much. The less, the better. A professor at Chinese Academy Social Sciences gave me 200 questionnaires of another research project. I have no idea yet how to deal with them.

You may try Beijing Individual and Private Economy Association (BIPEA). They may be more helpful, since they have 80 thousand members and we have only 2,000 members representing private entrepreneurs.

From the feedback of Mr Shi, I understood that this was not a realistic way to pursue, although I had prepared three other *guanxi* for the same path, A5, A6, and A7. A5 was the aid to a former vice mayor of the city, while A6 is a vice-mayor at the moment. A7 does research at a Beijing research institute, and also gives advice on the research projects of the BFIC.

Cadre *guanxi*, on which I had great expectations, provided me with no solution to access private entrepreneurs. This is ironic, given the belief of the power of cadre *guanxi* in China. This situation applies very well to Burt's (2000) description of "redundancy of network". Though A8, a department chief in a district, was willing to help me on his own initiative, I declined his kind offer. This is because Zhongguancun High-tech Park is not in his district.

The remaining *guanxi* not yet accessed are individuals without a government background. A9, A11, A13, and A14 are private entrepreneurs themselves, while A10 and A12 are journalists. I lost contact with A14 even after consulting several friends on his whereabouts. A13 is now the acting CEO of a famous brand PAD product. I rang his company twice, the receptionist politely asked me to leave my name and telephone number after apologising

that her boss was either abroad for business or in a meeting. But I have never received his call back.

6.5 Who are those supposed to help?

The aforementioned *guanxi* can be sorted into four categories according to the way I got to know them: 1) university alumni; 2) work acquaintances; 3) friend's friend, and 4) getting to know each other by chance. Eight of them are my university alumni (A1, A2, A3, A8, A10, A11, A13, and A14); Three of them are acquaintances I knew during the years of working in the central government (A4, A5, and A6); Two of them were introduced by a third party friend in the first time (A7, and A9); The last one (A12) is a journalist, whom I came across in a ceremony to receive a national paper award in 1988.

A1 and I graduated from the same university, but he left the university eight years earlier. I did not know him until I met him on a business trip to the city where he served as a deputy mayor in 1996. We felt we were getting close, when we learned we were alumni and talked a lot about the university. Soon, he moved to work in Beijing, which was a new working environment for him. I arranged parties for him to be introduced to a dozen friends from various departments of the central government.

I did not know A3 at the university either, but we began to know each other in 1996 in the process of competing for a scholarship to study in the UK. We helped each other, and both

of us succeeded in securing a scholarship. Later she returned to China to continue her career in Beijing municipal government. I had been very familiar with the other alumni on campus of the university, three of whom, A2, A8, and A10, studied at the same department with me.

I began to know the three persons, A4, A5 and A6, because of our work contact. At the time, two of them (A4, A5) dined out with me sometimes. This is a common way to keep in touch and promote friendship. Besides, we helped each other on many occasions.

I was introduced to A7 and A9. A7 is a social scientist. I had tried to help him do a cooperative research project in the UK. He is willing to help me with my research, which is also his research interest. A9 was indebted to me since I helped her prepare for and pass IELTS (International English Language Testing System) examination.

Though I met A12 by chance, we soon became good friends, as we had common interests. I was very active on campus and I helped him to report university student life. We have kept in contact through the years.

Four out of the fourteen *guanxi* contacts I listed, A9, A10, A11, and A12, helped me access some interviewees. The number of interviewees they introduced can be seen in both Figure 6.1 and Figure 6.2 (p172, 173). I had believed that with *guanxi*, in particular, *guanxi* in government departments, I would have interviewed many cases without a great deal of

effort. However, my background as a middle rank central government cadre and the cadre *guanxi* did not help much in the field research. The fact implies the waning influence of government on enterprises, in particular the private high-tech sector. The fact also illustrates the multi-dimension of *guanxi*. These will be discussed later. Now, the question comes: Who helped me complete the interviews?

6.6 Who rolled the snowball for me?

As the proposed routes to access interviewees were denied in practice, I had to turn to other channels. The Beijing Individual and Private Economy Association (BIPEA) mentioned by Mr Shi gave me a sense of snatching straws. BIPEA is a semi-official organisation under Beijing Bureau of Industry and Commerce (BBIC), fully responsible for the daily affairs of the private sector. All private enterprises and individual economy are required to be members of the association. It sounded an ideal path to approach private entrepreneurs. But my friends in the SBIC seemed not to be able to connect me to the association.

A happy accident occurred which filled the gap, when I was thinking that I was at the end of my resources. I just wanted to call my friend F1 to say hello, and he told me that his brother-in-law used to be the general secretary of the association. Thus F1 became the first person who helped me. He introduced me to a new friend NF1, Mr WYM, and my field research got underway. The progress is shown in Table 6.1.

Table 6.1 Time line for the progress of field research

Time	Friends Resorted	Interviewees Contacted	Interviews Conducted
Week 1	Listing Acquaintances		
Week 2	A1-A14 in Figure 6.1 contacted; A9, A10, & A11, may help	A9 & A11 in Figure 6.1, as F3/C1 & F7/C21 in Figure 6.2	
Week 3	Happy Accident: F1, F2	C3	Visiting NF1 for help
Week 4	Contact NF1 every 2 days	C2	
Week 5	F4 (A10), F5, F6, F8, F9, F10	C7, C5 (F6/C38, F8/C16, F9/C25, F10/C17)	C1, C2, (C7)*
Week 6		C4, C6, C7, & C9	C3, C4, C5
Week 7		C8, C11, C19	C6, C7
Week 8		C10, C12, C14, C24	C8, C9
Week 9		C31, C20, C13	C10, C11, C12
Week 10		C15, C23	C13, C14, C15
Week 11	F11, NF2	C18	C16, C17, C18
Week 12	F12, NF3	C22	C19, C20, (C21)*, C22
Week 13		C26, C28	(C23)*, C23, C24
Week 14		C29	C25, visit NF3
Week 15		C27	(C26)*, C27
Week 16		C30, C32	C28
Week 17		C36, C37	C26, C29
Week 18		C33, C34, C35, C36	C30, (C72)♦
Week 19			C21, C31, C32
Week 20			C33, C34, C35, C36
Week 21			C37, C38

Note: Only the first time of contacting with an interviewee is recorded in this table. Most cases were interviewed after several times of contact, which are not demonstrated here.

- * These are cases that were not finished in the first visit and a second visit had to be paid.
- ♦ This is the case invested by a Taiwanese and thus not included in the research.

From Mr WYM's line, I interviewed five cases, the 2nd, 7th, 11th, and 19th, plus a case introduced by the 7th informant. Though Mr WYM was the first person who promised to help me, and I had hoped to make many interviews through his referrals, the number of informants he provided is disappointingly low, and it took me a long period to wait for the

interviews. This can be seen from Table 6.1 and the case order I interviewed in Figure 6.2 (p173).

The second friend F2 to help me was another happy accident. He has his own business in the IT sector in Xiamen. Since he lives far away from my field site in Beijing, I had not thought of him until I met his wife who came to Beijing for a tour and mentioned her husband had some friends in Beijing doing computer related businesses. F2 introduced me to a friend as my 3rd informant. It is the 3rd informant C3 who helped me to roll the snowball. From this line, I interviewed 11 cases all together, the biggest snowball in my research.

In fact, the third friend F3 became the first case C1 I formally interviewed. She was a partner and vice manager of a palm computer company. She was waiting for a visa from the Canadian Embassy in China to immigrate to Canada. Since she was preparing to leave for Canada, I did not bother her further to introduce me to someone else. In fact, interviewing her in a friendly and relaxing atmosphere gave me a good start and warm-up in the field research.

A 4th friend I resorted to for help is Mr CLH, a journalist of an IT magazine. I had hoped to rely on him for more private IT bosses, but his strength lies on big firms with *guanxi* with their media or propaganda departments. These big firms are mainly state owned or collectively owned, beyond my research interest in the private sector. He promised to

contact private bosses, but he only succeeded in helping me interview a vice general manager of a big company as my 5th informant. Nevertheless, he provided me with information of two friends of ours in the IT sector, F8 and F9, with whom I had lost contact after years of being abroad. Both of them became my informants as case 16 and case 25 respectively.

F8 mentioned the name of a department-mate NF2, Mr YJJ, but without telephone at hand. I managed to get his mobile number. Unfortunately, Mr. YJJ was always unavailable for interview; he suggested that I interview his classmate, Mr. WZH, who was coded as the 27th interviewee. In a party organised by F9, I met another friend F10, who became the 17th case.

Friend F5 helped me to access case C10. In turn, C10 offered me a snowball of seven other interviewees. They are C13, C26, C28, C32, C36 and C37.

Although friend F6 was the sixth person I contacted to do an interview, he became my last interviewee C38. He also arranged for me to interview C29.

Interviewing the 7th friend, Mr HJC, was postponed several times by telephone because he had unexpected trips out of Beijing. It was coded the 21st case. But when the interview was in process for about half an hour, he was called away for an emergency meeting. Though coded as case C21, it was actually completed for the second time around the last few days

before I left for the UK. Before leaving me for the emergency meeting, Mr HJC made me an appointment with one of his friends doing PC business. I visited his friend Mr WXQ the next day as the 22nd informant.

Then an 11th friend helped me to interview the 18th informant in the biopharmaceutical sector.

The 12th friend, a journalist of an important daily newspaper of science and technology, got me through to a 3rd new friend NF3, Mr. WDL, the boss of a private consulting institute. Mr. WDL told his department manager, Mr YQZ, to arrange me several cases in high-tech. Mr YQZ gave me a list of five entrepreneurs. I visited four, because the last one's headquarters is in Tianjin City, about 200 miles away from Beijing. One of the four cases I investigated is a Taiwanese, which was thus not counted in my 38 cases.

All together I mobilised 12 friends to help access 38 cases. Only four of the proposed *guanxi* are among these who helped. *Guanxi* in government did not help. The failure of the proposed paths provided me with a chance to introspect *guanxi*.

6.7 Why did the proposed paths fail?

I asked myself why government *guanxi* didn't work? There may be several reasons.

Firstly, the government has not much control over individual entrepreneurs. As found in Chapter 3, with the development of marketisation, resources at the hands of government become fewer, entrepreneurs are no longer economically, politically and socially dependent on the government as Walder (1986) describes. Instead, entrepreneurs stay away from the government organisations and resort more to the market. The connection between individual entrepreneurs and government is thus becoming weaker. As the research conducted by the International Finance Corporation (2000) finds private entrepreneurs have to pay the private entrepreneur association fee but the latter can provide nothing to the former. The relationship between them exists as member fee.

Also, with the development of private business and the progress of reform, the restrictions imposed on the private sector by the government have been lifted as suggested in Chapter 2. Furthermore, the government has to promote the private sector to maintain its economic growth. Not only have the restrictions been lifted, but also some favourite policies have been promulgated. To get rich is glorious (*Economist*, January 17, 2002). The belief in the government's influence over private entrepreneurs, on which my proposed research paths were based, proved to be out of date. An interviewee argued,

All companies could snub the government agencies if they had not broken law, though it would be necessary to keep good relations with government in case they may "pick shell from eggs" (They can always find your problems if they wish).

Secondly, bureaucracy may impede the effect of *guanxi*. The relationship between a government department and the semi-government organisation under its auspices is subtle and complicated. Wank (1995) sees conflicts among Xiamen Bureau of Industry and Commerce, Xiamen Private Enterprise Association and Xiamen Association of Commerce. Even in the same tax bureau, the branch for local revenues and the branch for central government revenues are not treated equally by the local government, and they are at odds with each other (Liu, 2000).

A4 in the State Bureau of Industry and Commerce (SBIC) promised to find a way to put me in contact with the IPEA. But the delicate relationship between BIC and IPEA may have constrained him from doing so. He does not know the officials at IPEA himself. In order to help me, he must resort to officials at Beijing Bureau of Industry and Commerce (BBIC), which can help to introduce him to the BIPEA. The SBIC does not have strong influence over BBIC, since the officials at BBIC are not appointed by the SBIC; instead they are under Beijing municipal government's auspices. I would not like to embarrass my friend, and thus I did not urge him to help.

The SBIC is superior to BBIC merely in terms of professional guidance. The argument that relationships with a senior will extend to his subordinates (Arias, 1998) needs further contextual examination. Local governments are becoming more and more independent. This fact is reflected in many reports on local protectionism or localism, and as a consequence, some argue China is on the way to a federation of states (e.g., Wu, 2002).

Similarly, some sociologists put forward the term of regional corporatism or local state corporatism and argue that economic reform is decentralising power to local governments by enhancing their control over resources in their jurisdiction (e.g., Oi, 1995).

Thirdly, the development of high-tech sectors has somehow changed the relationship between the private enterprises and both government and semi-government organisations. Mr. WYM admitted that members from the traditional industries dominated the BIPEA and thus he did not know many private entrepreneurs in the high-tech sectors. The private high-tech sectors, in particular the IT sector, are dynamic in the Chinese economy, and have a certain influence on the economy. The Chinese government realises the potential of the knowledge economy, where the IT sector is one example²⁷. As Ms. Tan Haiyin, Chief Operating Officer at Eachnet.com (China's largest private online auction site), puts it, "We are already helping the government -- the regulator -- figure out what's important and what should be done." (China's Online Future, *Time*, May 15, 2000, p 20-22.).

Fourthly, it is possible that some *guanxi* ties I resorted to did not do their best to help me. Both Arias (1998) and Hwang (1987) point out that status matters in *guanxi* relationships. Tsang (1998) argues that the value of *guanxi* depends very much on the status of the partner with whom the *guanxi* is maintained. In fact, the status of both parties involved in a

²⁷ It is argued in China that China has lagged far behind in the first chance of development: industrialisation. In the era of knowledge economy, China has been provided with a new opportunity to catch up with the developed. And many believe that the gap in the IT between China and the developed is narrow. Great expectation has been put on the development of IT, the sector has thus won more attention and more support from the government (e.g., Fan, 2000; Lau, 2000).

guanxi is important. Bruun (1993, p98) gives a good example of the importance of the recipient by arguing that class and education determine one's *guanxi* power and the officials do not respect individual businesspeople when they lacked formal education.

Hwang (1987) argues that the favour allocator will judge the *guanxi* in the first step, "What is the *guanxi* between us? How strong is our *guanxi*?" (Hwang, 1987, p749). Social status labels the pay-off ability, which is one factor to the considerations of the favour allocator. But neither Arias (1998) nor Hwang (1987) has realised the dynamic aspect of status. Learning about my frustration that I did not get much help from government friends, a close friend of mine complained, "You now know what is meant by the saying: 'When you leave your position, your tea gets cold.'" What he meant is that the change of my social status from a young promising central government official to a poor student has devaluated me in *guanxi* relationships. I have become a less worthy *guanxi* tie to certain people, who would thus be reluctant to help me, since I seem to have limited pay-off ability to reciprocate favours. Chen (1995) thus points out that there exists avoiding *guanxi* in *guanxi* relations (cited in Lovett *et al.*, 1999, p234).

Although I cannot verify this speculation on my own case, there is some relevant evidence. For example, Case 21 mentioned their *guanxi*, government officials, on whom they relied to sell their products would be useless once they retired, since they cannot provide social capital any more. Similarly, Tsang (1998) finds that with the downfall of the former

Beijing party secretary Chen Xitong, any individuals or companies with good *guanxi* with him and his ring lost their investment.

6.8 My relationship with those who helped me access informants

As explained in the preceding section, four of the proposed *guanxi* paved the way to some informants. They are A9, A10, A11, and A12 in Figure 6.1, which are marked as F3, F4, F7, and F12 respectively in Figure 6.2. Who are the other eight?

Both F1 and F11 are my former colleagues. F11 is my peer in terms of rank in the government hierarchy. F1 used to work in a sub-department under the central government ministry where I worked, whose rank was higher than mine. He had quit the job and is in business now.

F2 and F6 are my *laoxiang* (fellow townsmen). I know them because we come from the same county and we studied in Beijing, but we lost contact after graduation. F6 has just come back to Beijing to develop his career. I had pretty frequent contact with him because of the proximity of our campuses. F2 does his own business in IT in Xiamen, a southern coastal city. I met him in a banquet in Xiamen organised by another friend, where I was conducting pilot research. The relationship between us can be labelled as a “weak tie”, which has its strength (Granovetter, 1973). The 3rd interviewee provided by F2 rolled the snowball to 11 cases altogether.

F5 is a university alumni and a staff at the university where I got my bachelor degree. We started to know each other on campus when I was active in several university societies while he was responsible for the administration of these societies.

The 12 friends helping me access interviewees can be categorised into four groups, alumni, colleagues, fellow townsmen, and friends known from other channels. There are 6 alumni, 2 colleagues, 2 fellow townsmen, and 2 other friends.

6.9 How were the interviews conducted?

All interviews were arranged in advance by at least two telephone calls. Most interviews were started by an exchange of pleasantries. Questions were raised according to the pre-designed questionnaire²⁸. The questionnaire includes both open end and closed end questions. However, I did not always start an interview from the first question in the questionnaire; instead, I varied my line of enquiry according to the circumstances. My goal was to get them to relate their true stories and anecdotes of business life. The interviews were best managed as conversations between two friends so that the interviewees would tell their stories in a relaxed atmosphere.

28 cases studies were conducted in the entrepreneurs' office. 5 of these entrepreneurs dined me out after the interviews and provided me with extra interesting information. One

²⁸ The original questionnaire for fieldwork indeed contained more questions. As this thesis focus on business start-up, Appendix C presents only the relevant questions to start-up and the irrelevant are not shown.

case was carried out in the entrepreneur's home and one interview took place in my former employer's office. The others 8 cases were done either in a restaurant or a cafe bar.

I spent at least one and a half-hour on an interview. Most of the interviewees did not ask how long the interview would take. Though in some cases, the interviewees would accept a quick talk of not more than an hour, in fact in no one case did it take less than one and a half hours to finish the interview, since we had a good time and we discussed some more issues.

6.10 What is essential to the success of field research?

Though experiencing difficulties and frustration, I managed to interview 38 cases. In terms of the quality of field research and finding, it is a success. What is essential to the success?

To conduct field research, firstly, it is essential to find an appropriate approach to solve the problem of "getting in" (Yeung, 1995). I would not have interviewed 38 without certain *guanxi*. A number of those interviewed stated clearly that it was their *guanxi* with a third party that led them to accept being interviewed.

However, *guanxi* does not guarantee success. *Guanxi* led me to the right door, though it sometimes misled me, too. Some *guanxi* did more than open the door for me, while some *guanxi* stopped at the door; the success of opening the door depended on myself. A good

example is in the case of F2, who provided me with one informant, and I managed to enhance the snowball effect by increasing the referrals to 12 cases. In general, the importance of *guanxi* lies in the opportunities it provides.

How to grasp the opportunities provided by *guanxi*? The point comes to the second essential, proper performance, which implies the interactive relationship between the interviewee and interviewer. Thus Gold (1985) argues that the technique of establishing and manipulating *guanxi* is *guanxi xue*. Similarly, Luo (2000) points out that *guanxi xue* are the practical strategies that best ensure to gain advantages in personal relationship.

This is demonstrated in the case of visiting Mr. WDL. I arrived at NF3 Mr. WDL's office at 11:00 on a Saturday morning. His manner toward me was neither hot nor cold at first so that I had wondered if he would help me. After we talked for a while about my research and my understanding on entrepreneurship, a smile appeared in his face, when he raised his voice, "Now, we have the same opinion, which is at odds with the mainstream theory dominated by professor A (at Peking University)". He later helped to arrange several interviews.

This is performance based social capital (Cohen and Field, 1999). If I had not performed reasonably well, that is, if I had nothing the informants could learn, they would not have bothered to introduce me to their friends further. Before leaving for the field research, I equipped myself with broad knowledge in business. Besides attending many courses with

MBA students, I forced myself to read some more books on business administration. Being interviewed, the informants did not simply waste their time telling me their stories, they discussed business in general with me, and some of them sincerely asked me for advice. Many of them admitted that I impressed them and they learned something from me. Good impression is social capital (Wank, 1999).

Some *guanxi* only provides information, a form of social capital (Coleman, 1988). How to transfer the potential into reality is crucial. Thus thirdly, the researcher needs to be persistent.

My friend F8, Mr. CSL mentioned the name of NF2 Mr YJJ, a business tycoon in Beijing, but he did not have Mr YJJ's telephone number. I finally managed to get his telephone number from Beijing Federation of Industry and Commerce, where he is a member. Learning from the lesson taught by A13's receptionist, I rang his mobile phone. But I had to get my courage up before calling,

Hi, YJJ. My name is Huang Qihai, an undergraduate enrolled in 1986 in *our* department (I emphasised "our"). I am currently reading a PhD in management at a university in the UK. I heard that you have done quite well in your business. I would like to learn from you if you could arrange a time to see me...I know that you are very busy. I can go over to meet you wherever you say. Yes, I will be available at any time.

His attitude was warm. He said he was rather busy and would like to have a chat during a dinner with me, “It is I who can learn from you, and need to learn from you. I can treat you and have a talk next week when I have time.” When I called him later several times, he was sometimes on a business trip far away from Beijing, sometimes in a meeting. The last time when I rang him, he said, “I have a headache with my business now and I am terribly busy. Could you interview my classmate Mr WZH? He has done pretty well, too. He must have time, I can give you his telephone number and I can tell him in advance.”

I called Mr WZH the next day and mentioned what Mr YJJ said. But Mr WZH said, “No, he did not ring me. But it doesn’t matter, since we are alumni. You can call me tomorrow morning to arrange a meeting, when I may have time in the afternoon.” Mr WZH became the 27th interviewee.

As a matter of fact, few interviews were organised smoothly after one phone-call. I had to persistently phone most entrepreneurs before they agreed to an interview. The above description gives an example of how an opportunity was turned into a successful interview.

6.11 The nature of the paths and *guanxi*

6.11.1 Private and personal *guanxi*

Chapter 4 has pointed out that *guanxi* is a private and personal relationship. *Guanxi* exists between individuals rather than organisations; hence, *guanxi* is not housed in organisations but in individuals. Government relationship with entrepreneurs is fragmented (atomised). In essence, the relationship is a personal relationship between an official working in the government and individual entrepreneurs, in particular activists (Walder, 1986). Mr. WYM stated that the informants he introduced were his “own savings”. Although my friend F1 assured that Mr WYM would do his best to help me, his effort was confined by the atomised structure, because the number of *guanxi* entrepreneurs he knows is limited. This is the weakness of strong ties (Granovetter, 1973)

6.11.2 The constraints of *guanxi*

Guanxi is important in general, as many informants acknowledged that without the introduction of *guanxi*, such an interview would not have been possible. However, this does not mean that *guanxi* has strength with no constraints. Unfortunately, this point has never been addressed. The failure of my proposed paths via government *guanxi* demonstrates the disadvantageous side of *guanxi*. The embedded structure actually confined my vision on the possible paths, and hindered my progress of research at the very beginning.

Social capital is not always instrumental for individuals; rather, it may become a constraint to individuals' actions and choices (Portes and Sensenbrenner, 1993). An individual's

action is both facilitated and constrained by the structure and resources available in social networks in which they are embedded (Granovetter, 1992).

This is also justified in business operation. For example, entrepreneur Mr. CFY (informant 2) argued some close *guanxi* had hampered his business. For instance, the official in charge of drug wholesale would give an unfamiliar retailer good prices and would take for granted to accept some benefits from the retailer for the good prices and quick process of supply. But being a former colleague of Mr. CFY, he did not feel comfortable all the time to accept kickback from the entrepreneur. When a drug was in high demand, the official would supply the unfamiliar retailer for good returns and simply told the entrepreneur that the drug was out of supply. Geertz (1963) offers another example of the constraint of social capital: one abdicated king in Bali acknowledged that firms were turned into relief organizations for close social relations rather than businesses (cited in Granovetter, 1992, p7).

6.11.3 The context of *guanxi*

Mr WYM would like to introduce me more informants, but his effort was constrained by the weakness of strong ties, i.e., limited number of *guanxi* entrepreneurs. This example highlights the difference between the willingness to help and the ability to help. As pointed out earlier, the change of the social status of a person has an impact on the social capital of the person's *guanxi* network. The two situations demonstrate that *guanxi* is contextual. In

other words, *guanxi* provides cooperation, social capital, in specific contexts. Burt (1997b) finds that social capital is not defined by network form alone in all settings. In some circumstances, the social capital value of a network is a function of both form and content.

My status as a PhD student at a UK business school may not be of the interest to the government *guanxi* I resorted to, but it can be attractive to the business *guanxi*, who would like to learn “Western” business ideas. Well prepared, my performance in an interview convinced an informant, who felt that a talk with me was not wasting time and was willing to pass me to a next informant. In such a context, I interviewed many cases with the introduction of new *guanxi*.

Rose (1998) argues that understanding the significance of social capital requires attention to networks in specific situations. This is because the outcome of the network depends on situation. For example, networks used to maintain health produce different outputs than networks that produce food or house repairs.

6.11.4 The contingency of *guanxi*

The other side of contextual *guanxi* is its contingency. It must be noted that *guanxi* merely provides chances for success rather than success itself. To know somebody is a starting point. Social capital may become a constraint to individuals’ actions and choices (Portes and Sensenbrenner, 1993). This is the contingent value of social capital (Burt, 1997a).

It was shown that the proposed paths via government *guanxi* did not work out, while some happy accidents had much better results. The consequence of possessing *guanxi* can be either intended or unintended. My friend F2 would have never believed that he had the “greatest amount” of social capital in terms of helping me in the field research, while I had never imagined the possibility of the failures of my government *guanxi*. In my case of doing research by the snowball method of conducting interviews, I have strength in knowing many people who “might” help me to access interviewees, though this strength is not so decisive that an intended outcome follows. Burt (1999) finds the more people without redundancy a manager knows, the more chances for him to succeed in business.

6.11.5 Obligation of *guanxi*?

Bourdieu (1986) notes obligations subjectively felt, such as feelings of gratitude, respect, and friendship, make social capital transferable for certain ends. But the question is “Where does the obligation come from?” It may be taken for granted that parents have obligation to raise their children, but why, for instance, in the cases of Mr. YJJ and Mr. WZH, did they help? We had no prior relationship of what Bourdieu (1986) calls mutual acquaintance and recognition. Accordingly, there should exist no social capital. But the background of studying at the same university did generate potential social capital. The social capital is based on mutual identification of the university and the fact that we are alumni. Fevre (2000) thus advocates paying attention to social identities in introducing the idea of social capital, as norms and social networks are complemented by social identities.

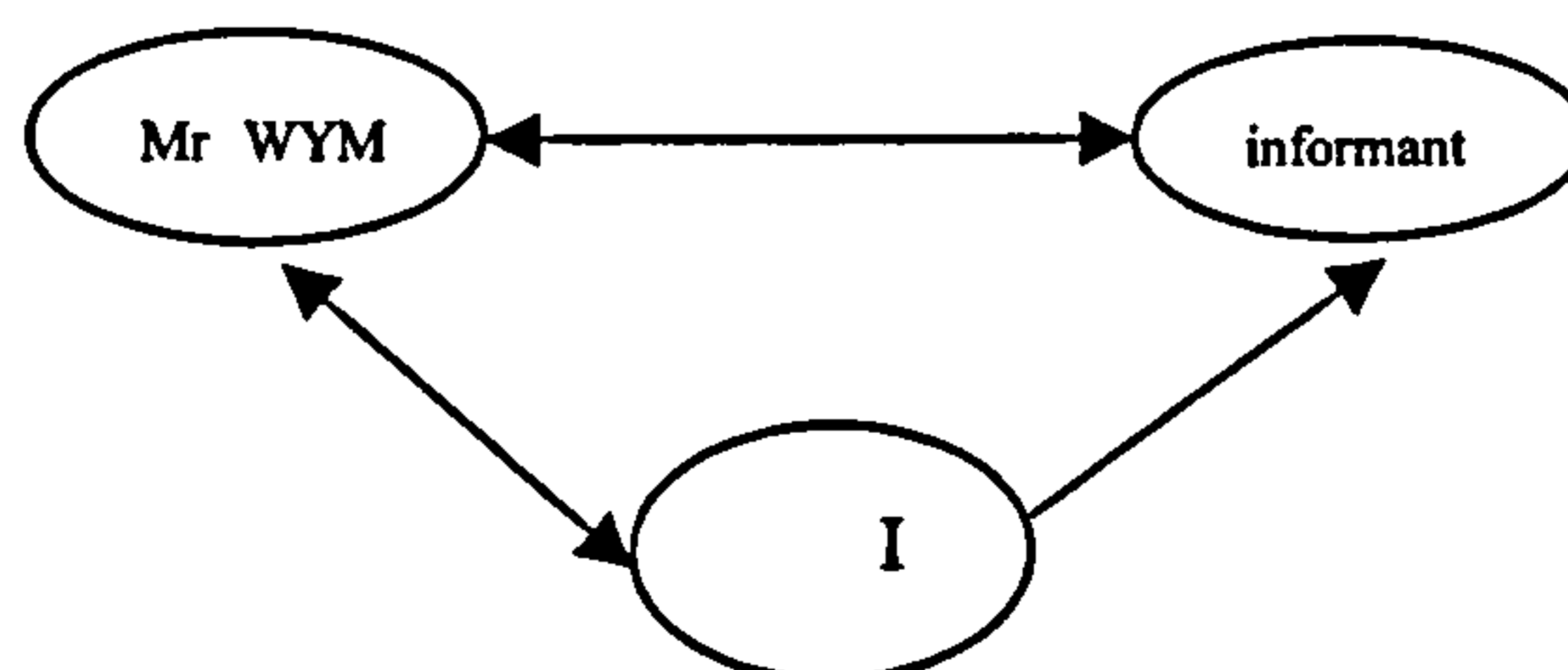
In the interaction with Mr. WDL, appropriate performance turned potential into the reality of help. How to actualise potential social capital is of no small importance. The effort is subjective dynamics. Social capital is a static substance. Like gold under the earth, its value does not come true until it is found, mined and fined. The subjective dynamics is more than the obligation of social capital, which is worthy further research.

6.11.6 Reciprocity of *guanxi*?

The interviewees admitted that they accepted me for the sake of the third party who introduced me. Clearly, *guanxi* between the third party and the informants can be conveyed (Arias, 1998) to the researcher. The fact implies that the exchange of *guanxi* is not necessarily dyadic. For example, before I entered, the relationship between an informant and Mr. WYM is reciprocal as shown below,



When I was involved, the relationship was changed as follows.



Mr WYM passed me to an informant, who received me because of *guanxi* between them. I owe Mr. WYM for the help, but I do not necessarily owe the informant. The relationship between Mr WYM and me is reciprocal, and so is that between Mr WYM and the informant, while that between the informant and me can be exempted. In other words, I do not necessarily reciprocate the informant; instead, I am expected to reciprocate Mr WYM for his help, while a favour of Mr. WYM is due to the informant for my sake. It must be pointed out that the introduction by Mr WYM and the interaction with the informant have provided both of us with the base to establish *guanxi* with each other. The establishment of *guanxi* will be examined in Chapter 8.

6.12 Conclusion

The self-reflective snowball sampling methodology describes the first hand experience of conducting research, and reveals the relationship between the researcher and those who paved the way for the researcher. The use of *guanxi* enables the researcher to 'get in' and roll the snowball. The methodology has some inherent problems. The criticism is one of bias caused by closeness to the subjects (Yeung, 1995). However, the analysis of the paths to access research is itself intriguing. In addition, it provides a self-reflective perspective to consider the concepts of *guanxi* and social capital.

This chapter reveals that my existing cadre *guanxi* did not help me much in my field research. It indicates that having a *guanxi* network does not necessarily produce intended

outcomes. *Guanxi* is contextual and contingent. Also, a change in one's social status has an impact on one's social capital. *Guanxi* network, or, social capital is not simultaneously a cause and an effect. Thus it is unwise to equate having a *guanxi* network with an intended outcome.

This is the case for businesspeople, too. Having cadre-related *guanxi* does not guarantee entrepreneurs to have advantage in business start-up. As pointed out, the contingent value of *guanxi* is contextual and situational. The social capital value of a network is a function of both form and content. On the other hand, entrepreneurs without existing *guanxi* with cadres can develop new *guanxi* as this researcher has experienced. There may be, to some extent, difference between *guanxi* that helped the researcher conduct fieldwork and *guanxi* that is useful for business. For example, obligations in the former are less than the latter. *Guanxi* for business may involve risk and interest consideration, and thus needs longer time to build up. Nonetheless, this experience points to the potential for entrepreneurs to outweigh the possible disadvantage of having no cadre *guanxi*.

Both the concepts of *guanxi* and social capital found in the field research are much richer than the available literature. For example, *guanxi* is contextual and contingent. *Guanxi* has constraints on actions. These are for the first time addressed in this thesis. In the following chapters, some other rich contents of *guanxi* and social capital, in particular how *guanxi* and social capital comes into being, will be discussed.

Figure 6.1

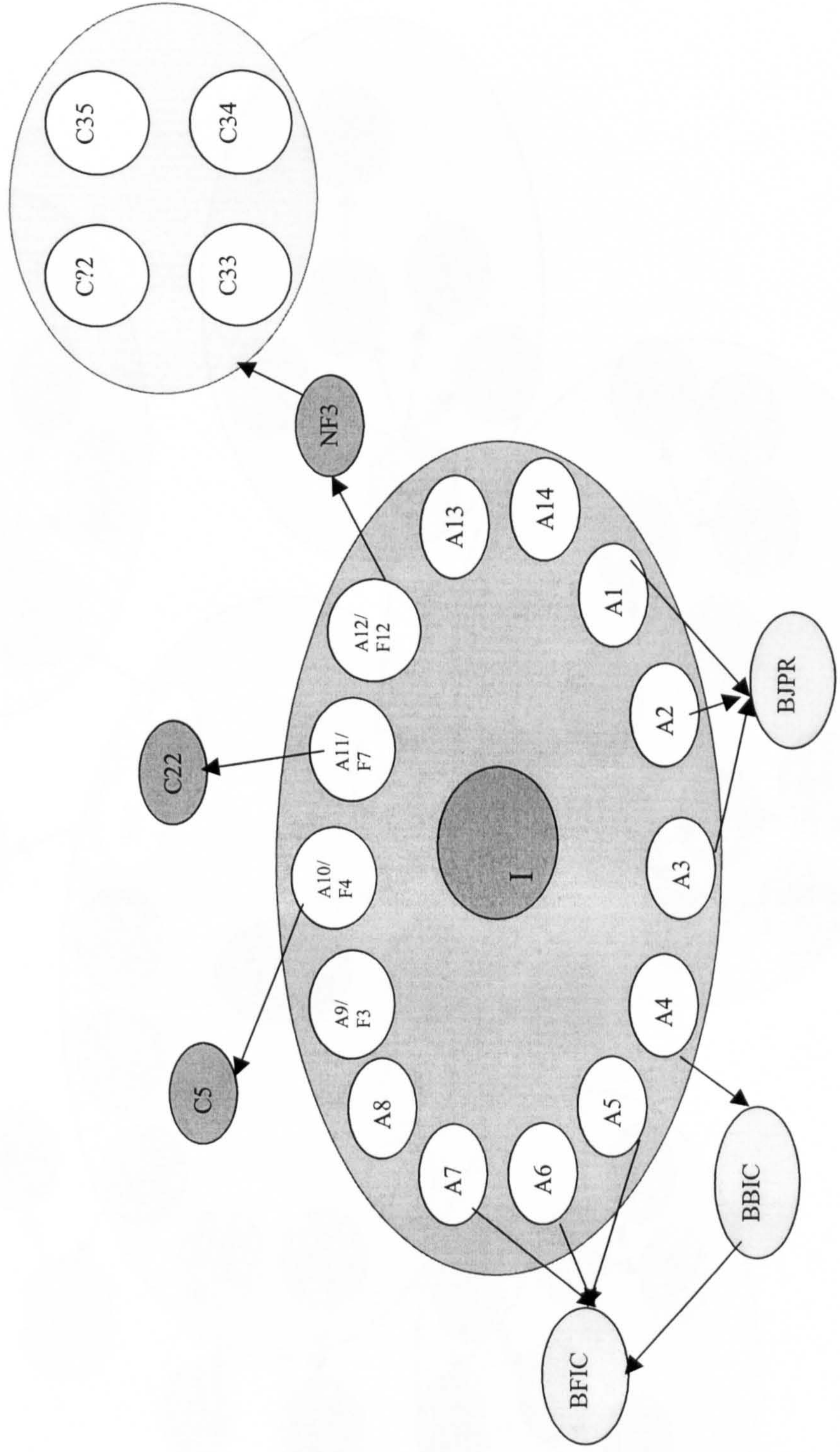
The proposed paths to access interviewees

A= acquaintance, N=acquaintance number; F=friend (numbered as in Figure 6.2)

BPR= A Beijing Think-tank

BBIC=Beijing Bureau of Industry and Commerce

BFIC=Beijing Federation of Industry and Commerce



Chapter 7

The Enterprises, their entrepreneurs, and their start-up capital

Chapter 3 found no statistical evidence to support the power conversion theory, which claims that cadre related entrepreneurs have an advantage in business start-up. It suggested that further qualitative research is needed. This chapter investigates in depth how private entrepreneurs in the IT sector financed their business start-ups. It firstly looks at what businesses the interviewed entrepreneurs are in. Then it examines the backgrounds of the entrepreneurs. Lastly, it investigates the main sources for start-up capital and the underlying different types of *guanxi*. The preceding chapter described how the case studies were conducted. It argued that having cadre related *guanxi* does not necessarily lead to success; instead, newly developed *guanxi* can be useful.

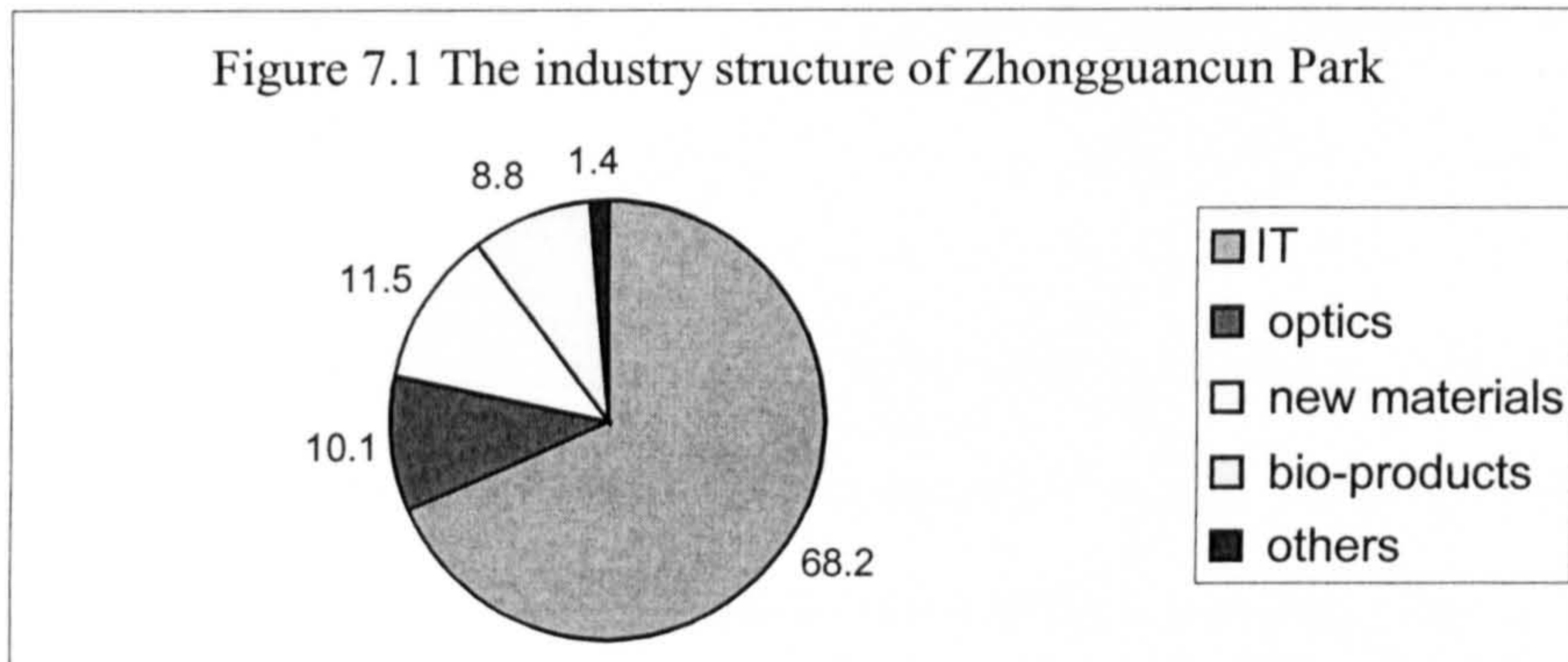
7.1. What businesses are the enterprises in?

The thirty-eight firms interviewed can be divided into two groups: IT²⁹ and non-IT. The majority, thirty cases³⁰, of the interviewed companies are in the IT sector, and the other eight are in other high-tech sectors. This happens to be consistent with the industry structure of Zhongguancun high-tech park (Figure 7.1). In Zhongguancun, information technology industry accounts for 68.2%; optics-machinery-electronics integration

²⁹ IT (information technology) encompasses all forms of technology used to create, store, exchange, and use information in its various forms (business data, voice conversations, still images, motion pictures, multimedia presentations, and other forms, including those not yet conceived).

³⁰ There are two cases in this category whose main businesses are not in IT, Case 2 and Case 30. I was introduced to visit them for their businesses in IT. Case 2 is mainly a pharmacy retailer; however, it has invested and developed software in drug shop management. In Case 30, Mr YJH invested RMB 1,500,0000 earned from his main business in restaurant in an on-line property service company in 1999. As a director to the Internet company, the entrepreneur is not optimistic about its operation and has started to concentrate himself on a newly opened restaurant named localfood.com. Conversations with them were focused on their business in IT, but topics about their main businesses could not be avoided all the time.

industry takes up 10.1%; new materials, new energy and environmental protection industries constitute 11.5%; bioengineering and new medicine industries make up some 8.8%; and the others share is 1.4%. IT industries of Zhongguancun hold a big domestic market share. The sale volumes of hardware, software and IT service took up 5.5%, 40.0%, and 46.9% respectively of the total in China in 1997 (Luo and Zhao, 1998).



Source: Luo, and Zhao (1998)

The thirty-eight cases do not distribute evenly in all the high-tech sectors and may not well represent every sector of high-tech. Since IT industry takes the lead in Zhongguancun High-tech Park, this analysis will focus on the thirty cases in the IT sector. IT is categorised into hardware, including PC, PC components, and PC peripherals, software, networking security, e-commerce, and communication³¹. The distribution of the cases is given in Table 7.1.

³¹ How to categorise the sub-areas of IT can be enlightened by the 16th International Federation for Information Processing World Computer Congress, whose theme was “Information Science and Technology after 2000”. The congress' topics were focused on communication, chip design automation, information technology in education and business, software, signal processing, intelligent information processing and information security.

The International Federation for Information Processing World Computer Congress was hailed as one of the most prominent events of the international information technology society, The 16th World Computer Congress was held in Beijing from August 21 to 25, 2000. International Federation for Information Processing (IFIP), founded in 1960 under the auspices of UNESCO, now has nearly 100 members including the United States, Britain, Germany and Japan. The Chinese Institute of Electronics joined the IFIP in 1980 (*China Daily*, November 25, 1999; August 21, 2000, and August 22, 2000).

Table 7.1 The distribution of the cases

Distribution of the cases in sectors	IT					Non-I
	28+2					T
Distribution of the cases in the IT	Hardware	Software	Network security	E-commerce	Communication	
	10	10	2	5	3	

There are ten companies in hardware³². They do manufacturing and trading business in PC and PC peripheries.

Another ten interviewed companies are in the software business. Two of them develop and install integrated circuit card (IC) systems, and as well manufacture IC cards. The other eight of them design application software from learning, property management, multi-media software for estate display, to restaurant management, government information management, and enterprise resources planning software.

Two companies do network security business. They have products for network safety, such as firewall.

Five companies are engaged in e-commerce business. Two of them provide online car sales and car-related services. One within this category is mainly a sport portal, which also supplies technological support to some other web sites. One of them is an online housing broker. The last one in this group builds online platforms for drug transactions.

³² The categories are based on the current main businesses of the companies in terms of revenue. Most companies remain in the same businesses as start-up. However, some companies have changed.

Three of the interviewed enterprises do business in the communication area. One of them designs and installs railway signal system. Another enterprise provides network access and backbone infrastructure design; it also offers implementation for telecommunication services. The last one is engaged in optic fibre products for communication.

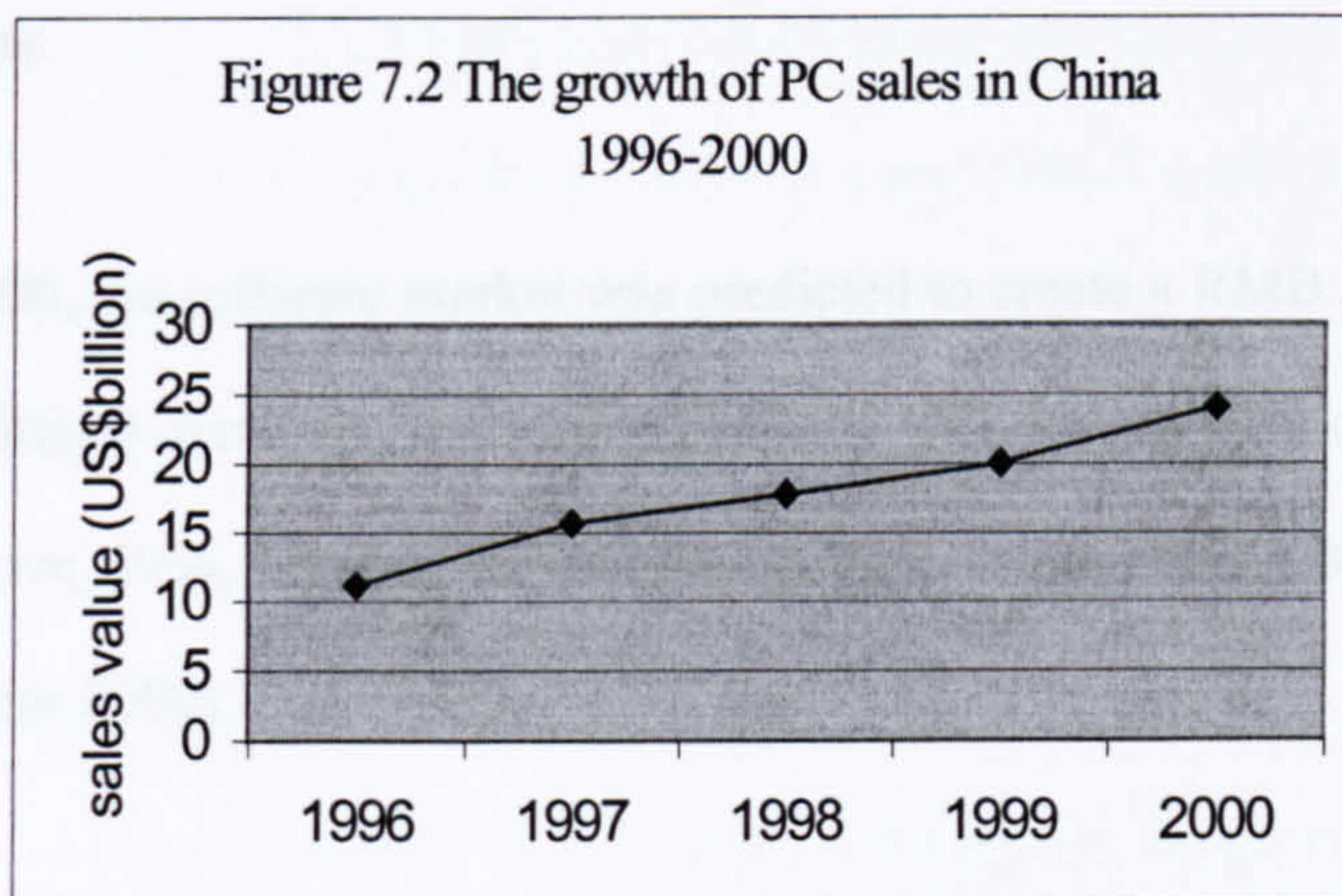
7.2. Fast growth of the IT sector

Stable economic growth and a large population make China a prominent market in the world. The vast domestic market has played a key role in supporting the high-tech industries. Compared to leading technologies in the world, the Chinese new and high technological level still falls behind. However, by developing technologies that fit in with the demands of the domestic market, the Chinese high-tech industries have survived and are robust.

Expanding rapidly from its humble beginnings, the Chinese IT industry has grown tremendously over the past two decades. The increase in computer sales and computer related product sales are the best evidence. During the 1991-1997 period, the rate for sales volume jumped by more than 40% every year.

As the overall economic growth rate decreased in 1998, the growth rate of computer sales slowed down to 13.8% (see Figure 7.2). The total sales volume of PCs grew about 26 times from RMB 5.6 billion (US\$ 670 million) in 1990 to RMB 170 billion (about US\$ 20 billion) in 1999, an increase of 14.9% from 1998 (*China Daily*, 20 October 2000). In 2000, the figure was expected to increase by 17.6% to reach RMB 200 billion

(about US\$ 24 billion).



Data source: China Software Industrial Association (1998), "Chinese Software Industry and Market" and chinaonline.com

Table 7.2. Software and Information Services Market in China (1996-1998)

		1996	1997	1998
Software	Total sales (US\$100 million)	11.1	13.5	16.8
	Increase (%)	35.3	21.7	23.2
Information Services	Total sales (US\$100 million)	13.6	17.8	22.5
	Increase (%)	46.8	31	26.4
Total	Sales (US\$ 100 million)	24.7	31.3	39.2
	Increase (%)	41.4	26.8	25

Source: China Software Industrial Association (1998), "Chinese Software Industry and Market".

The software market in China is growing at a rapid pace, too, along with the PC market.

The total Chinese software market is growing by 20-30 percent per year. In 1998, the

rate of increase of software and information service was 23.2% and 26.4% respectively, which is higher than the 13.8% rise in the computer market (details are shown in Table 7.2). It means the importance of software and information services is growing in the IT market.

In 2000, the software market was predicted to create a RMB 20 billion-plus (about US\$ 2.4 billion) demand. Application software will occupy 60% of the market with systems software 10%, leaving the remaining 30% to supporting software (*China Daily*, 20 October 2000).

Beijing is China's largest market for IT products with a good market build-up effect. Many enterprises in Zhongguancun are known for their scientific and technological products with good quality. The famous "Electronic Street" in Zhongguancun is the largest collection and distributing center of IT products in northern China. The software sales of Zhongguancun constituted 40% of the total sales in the whole country in 1997 and 43% in 1998.

The growth of the interviewed IT companies has also been rapid. Most of the interviewed enterprises started up with low capital and developed rapidly. They all have expanded their assets to over RMB one million, except some newly established companies. In several cases, the enterprises have assets of more than RMB 10 million. The explosive expansion of Case 5 is a good example.

Case 5 is a leading provider of total Internet infrastructure solutions and software products in China. Initially, three Chinese technology expatriates set up an ICP (Internet content provider) company in 1993 in the USA, with the aim at bridging information

between the West and China. In 1995, its operations were moved to China with \$US 500,000 venture capital as its start-up capital. By March 31, 2000, according to the company's report, they had net revenues of US\$5.5 million in the first quarter, representing a 77% increase over net revenues of US\$3.1 million for the same period in 1999. Software revenues for the quarter were US\$1.8 million, representing 33% of total net revenues and a 33% increase over the same period in 1999. Network solutions revenues were US\$3.7 million, an increase of 118% over the same quarter of 1999. Gross revenues were US\$22.9 million during the first quarter, a 340% increase over gross revenues of US\$5.2 million of the same quarter last year. In March 2000, the company announced its initial public offering in NASDAQ. The 5,750,000 shares issued by the company raised a total of US\$138 million (Table 7.3).

Table 7.3 Rapid Expansion of Case 5

Categories	Net revenues	Software revenues	Network solutions revenues	Gross revenues
Revenues of the first quarter of 2000 (US\$ million)	5.5	1.8	3.7	22.9
Growth since last year	77%	33%	118%	340%

7.3. Who are the entrepreneurs?

7.3.1. Family background

Among the thirty entrepreneurs interviewed in the IT sector, only five were born in Beijing. All the other twenty-five are immigrants from other areas across the country. In terms of family background, five of them come from peasant families, thirteen are from

cadre families, and the other twelve come from worker families. Among those from cadre families, three entrepreneurs have middle rank cadre parents (Table 7.4).

Table 7.4 family backgrounds of the entrepreneurs

Peasant	worker	cadre	
5	12	13	
		ordinary	middle
		10	3

More than half of the entrepreneurs (seventeen out of thirty) come from peasant and work families, who do not seem to have much social capital from endowment (Wank, 1999). Do the other thirteen from cadre families have some advantage from their family background? The answer will be clear later.

7.3.2. Young male entrepreneurs with higher degrees

Twenty out of the thirty firms are comparatively new, set up in the 1990s. Four of them were established in 2000. The remaining two enterprises set up before 1990, Case 2 in 1986 and Case 33 in 1988 respectively, were not in the IT sector when their businesses began, instead, one was in restaurants and the other in drug sales. They recently stepped into the IT sector when they had been successful in the traditional sectors. Consistently, the entrepreneurs are fairly young. Twenty three of the interviewees are in their thirties, with most of them in their early thirties. The other seven are younger than thirty years old.

The entrepreneurs have good educational backgrounds. Only one entrepreneur, who firstly started up his shop in drug retail in 1986, has education at college level. Thirteen of them have bachelor degrees. The rest hold degrees higher than bachelor, with thirteen master degrees, two doctorate degrees, and one doctorate degree candidate who dropped out for business. Twenty of the entrepreneurs studied engineering subjects, four majored in sciences, and the remaining six were trained in art and social sciences.

Among the thirty interviewed entrepreneurs, only one is female. This does not deviate from the 1995 national survey on private enterprises analysed in Chapter 3, which finds that 90.6 per cent of entrepreneurs are men. The gender division in the private sector is still significant.

Table 7.5 Comparisons of Age and education

		Entrepreneurs in IT (case study)	Entrepreneurs in private sector (1995 survey)	Entrepreneurs in general (1999 CESS survey)
Age	<30	30.4%	8.4	n.a.
	30-40	69.6%	37.7	n.a.
	>40	0	52.9	n.a.
Degree	< Middle-school	0	81.6	15.3
	College	3.3	13.1	40.1
	Bachelor	43.3	4.5	34.8
	Master & Doctorate	53.4	0.8	9.8

Comparisons with some similar surveys indicate that the IT sector tends to be dominated by well-educated young men (Table 7.5). About 96.7 per cent of the interviewed entrepreneurs hold bachelor or higher degrees. The national entrepreneur survey (CESS, 1999) finds that 44.6 per cent of the entrepreneurs across all types of

ownership have such degrees, and only 6.3 per cent of the entrepreneurs in private sector hold such degrees (1995 Private Enterprises Survey). The education opportunities for the new Chinese generation are rising, but for those who are older than thirty, struggle for university education was commonplace. This is verified by the figure for 1997, when there were only 25.7 college students per 10 thousand of population (*A Statistical Survey of China, 1998*).

It may not be appropriate to generalise the education background for all the entrepreneurs in the IT sector from this small sample case study. However, the comparisons above suggest that the entrepreneurs in the private IT sector have far better education than the general run of entrepreneurs in the private economy. It also can be true that entrepreneurs in IT are better educated than entrepreneurs overall. Education provides the entrepreneurs human capital, which is created by changes in persons that bring about skills and capabilities that make them able to act in new ways (Coleman, 1988), or, cultural capital in both objectified state and institutionalised state (Bourdieu, 1986). Perhaps equally importantly, the education background provides them social capital in terms of trust for their businesses, in particular in getting start-up as discussed later.

The entrepreneurs in IT are much younger³³ compared with all entrepreneurs in the private sector. All those entrepreneurs interviewed in IT are under forty years old, while more than half of the entrepreneurs in the private sector are over forty years old. The

³³ The advantages of age and education are also reflected by the enthusiasm of young and well-educated people in the Internet. According to a CNNIC survey (China National Network Information Centre, 1999), the majority of the Internet subscribers, 77.5 per cent, are younger than thirty years old, only 6 per cent of the subscribers are over forty years old. In terms of education, nearly sixty per cent of the Internet subscribers have degrees of bachelor and above, only fourteen per cent of them received below or equivalent to higher school education.

age advantage is more significant when compared with the entire population of entrepreneurs across all sectors. According to the national entrepreneurs survey (*CESS, 1999*)³⁴, only 9.4 per cent of the general entrepreneur population are less than thirty-five years old, with about 32.5 per cent of them aged between thirty-six and forty five years old, and nearly 60 per cent of surveyed entrepreneurs older than forty-five.

7.3.3. Work experience

Five entrepreneurs directly entered private business right after walking out of campus, but all of them had done some part time work related to their current businesses while they were studying. The rest, twenty-five of the 30 entrepreneurs had worked before starting up their own businesses. Among the twenty five, six have experience in government departments, with four as government officials, and two working in government financial institutions before going for business, and the remaining nineteen having experience in companies or research institutes (Table 7.6). With their education background mainly in engineering and sciences, most entrepreneurs were engineers.

Table 7.6 Work experience for the entrepreneurs

Government	6
Non-government	19
No work experience	5

Seven out of the 30 interviewed entrepreneurs had done moonlighting before they started their own businesses. Among them, two were full-time state employees; the

³⁴ Because *CESS (1999)* has different age cohorts from the 1995 national private enterprise survey and my case study, the data is not appropriate to be list Table 7.5.

other five were full-time university students. The five student entrepreneurs actually spent more than half of their time on their businesses before graduation.

7.4. How private entrepreneurs in IT financed their start-ups

According to Churchill and Lewis (1983), finance is extremely important at the start. However, as was found in Chapter 2, in China, the private enterprises' start-up and capacity for survival and growth are constrained by lack of capital! None of the formal financial channels is available to the private sector. The following sections examine how the private IT companies financed their business start-ups under such an adverse situation.

Two of the thirty firms were set up in the 1980s. Four were set up lately in 2000. The rest twenty-four firms were registered in the 1990s. Although several companies were registered as collective or state owned firms ("wearing red hat") at the beginning, they had changed their ownership since the government issued a regulation requiring all the red hat firms to show their real private ownership by 1998. Among the 30 interviewed companies, only one is registered as a sole proprietorship business, the other 29 are corporate limited companies. The registration itself implies that such a firm does not belong to a single person. It also indicates that the investment came from more than one person. The concern is thus focused on the most important sources of start-up capital here.

7.4.1 The average registered capital for IT companies

Among the interviewed firms, the lowest registered capital at start-up was RMB 30,000 for case 2, which was registered as individual economy (*getihu*) in 1986 (Its current registered capital is RMB 500,000). The highest registered capital is RMB 30 million of a company set up in 2000. The medium of registered capital is RMB 2 million. The mode of registered capital is RMB 500,000.

In general, companies in hardware and software businesses tend to have low registered capital. The registered capital of most cases in hardware and software businesses is close to the mode. Companies in e-commerce seem to have much higher registered capital. The two companies with the highest registered capital are in this group.

7.4.2 Where did the registered capital come from?

Table 7.7 The most important source of registered capital

	Number of cases	Average registered capital (mode)
Personal savings	9	RMB500,000
Help from relatives or friends	6	RMB500,000
Investment from others	15	RMB1,000,000

There are various sources for registered capital. Table 7.7 shows the most important sources of registered capital for the entrepreneurs. Nine entrepreneurs claimed that they had their own savings as the registered capital. Six entrepreneurs admitted that their relatives or friends helped them with the registered capital. In the remaining fifteen cases, the registered capital was investment from other channels, which includes investment from other partners of their businesses, such as, relatives, friends, and other

partners. In these fifteen cases, the entrepreneurs hold some percentage of shares in their companies either for cash contribution, or technology/management contribution, or the mixture of the two.

No case was found to have loans from a bank. The finding from the field research convincingly supports the argument about the difficult financial situation for private enterprises.

The firms with investment from others tend to have higher registered capital than the other two sources, with a mode of RMB 1 million, compared with the same mode of RMB 500 thousand for those relying on help from friends and relatives and self-savings. Moreover, the companies with more than RMB 1 million and the highest registered capital are all in the group of investment from others. In contrast, companies with less than RMB 500 thousand and the least registered capital cluster in the former two groups.

7.4.3 Gap between registered capital and real capital

Theoretically, registered capital should be available at business start-up. How could the entrepreneurs have such high start-up capital? This seems particularly problematic for the entrepreneurs relying on self-savings, because the average income for Chinese is low. Even for the lowest start-up capital of RMB 30,000 in case 2, it is 6 times of the average annual income for a city and town resident, which was RMB 5,189, and 10 times of the average annual income of RMB 2,999 for a resident living in the countryside in 1997 (*A Statistical Survey of China*, 1998). As they are generally young,

it is unlikely that most of them have large accumulations for registered capital. How did they obtain such a huge amount of capital then?

Further investigation finds that there is a gap between registered capital and real available capital at business start-up for most cases. This is in particular true for the fifteen entrepreneurs who depended on their own savings and on the help from either friends or relatives. As pointed out previously, in these cases, they tended to have lower registered capital. As a matter of fact, they also had much lower manageable capital at hand when they started up their businesses. In some cases, available capital was very significantly lower than the registered. In case 31, the entrepreneur had about RMB 20,000 of his own at hand when he started his business, however, the registered capital for his company was said to be RMB 300,000. The registered capital is 15 times of the real capital in this case.

Most of the other fifteen companies with investment from others did not have this problem and they had similar amounts of manageable capital and registered capital. However, in some cases, registered capital was also exaggerated. For example, in case 30, the entrepreneur obtained RMB 150 thousand investment to start his business, but his firm was said to have RMB 1 million registered capital.

7.4.4 How to fill the gap?

The question arises, why does this gap exist? The government had a minimum requirement for registered capital, RMB 300,000 for a company, and RMB 500,000 for a trading company. To meet the registration requirement of the government is the first

step of business entry. Furthermore, the amount of registered capital has also a symbolic implication to the size and trustworthiness of a company. According to the entrepreneurs, to their understanding, the more registered capital, the bigger a firm looks like, and thus the trustworthier it appears.

How did the entrepreneurs manage to register without sufficient start up capital? A common tactic used by most of them is termed “passing the account”, i.e., one entrepreneur borrows money from friends or relatives and deposits it into his own accounts. Then, after finishing the registration procedure, he returns the money immediately. A second method is to borrow some notes from friends or relatives as assets, which can be considered as part of registered capital. That is the reason when talking about the sources for registered capital, I used “help from friends or relatives” instead of “money from friends or relatives” in Table 7.7. A third method is to take some valuable goods, such as computers, into account as registered capital.

To have enough registered capital is an important step for a business. This helps to get a license from Bureau of Industry and Commerce that grants a firm legal status to operate a business. However, registration is like a ticket for entry, whether he or she will win or lose in the business field is far from known.

In a sense, registered capital is a game between the entrepreneurs and the government administration agency. Though not all the entrepreneurs had as much registered capital as required by the government, they did start up their business and develop quickly. It is not strange that most of the entrepreneurs don't think registered capital so important to business. This implies generally low entry requirement in the IT sector, and accordingly

low start-up capital. Indeed, several of them had start-up capital of RMB several thousands. As informant 21 admitted, "As long as your business opens, you will eventually have revenues. In general, return is high. You can reinvest the profit. Though sometimes slowly, your business rolls ahead." This is in particular true for the companies engaging in contracted projects, such as software system design and integration. When a contract is signed, they will get the first installment of payment by the customer. It is not essential to have a big sum of cash for business start-up.

Such a reality has led to the change in the requirement for start-up registered capital. For According to *China Economic Times* (May 11, 2000), Beijing lowered registered capital to RMB 30,000 (US\$3,628) for establishing high and new technology enterprises in its Zhongguancun High-tech Park. The city also relaxed substantially its restrictions on the ratio of invisible assets. Beijing municipal government published a series of relevant policies, including the following:

- 1). High and new technology limited companies will be allowed to register if they have more than RMB 30,000 in registered capital. They will be allowed to transfer this registered capital into China in installments over two years.
- 2). The ratio of invisible assets as capital will be increased. Industrial property rights and non-patent technologies assessed as capital now may account for up to 60 percent of a company's total registered capital. In the past, the maximum percentage was only 35 percent.

7.4.5 Help from relatives and friends

In the six cases with help from relatives and friends, there are two forms of help. One is as described earlier, friends and relatives provide the entrepreneurs with money only for the purpose of registration, i.e., to meet the registered capital requirement by the government. In this case, the entrepreneurs do not actually use the borrowed money in business. After the registration procedure is over, the entrepreneurs return the money. The procedure is termed “passing account” (*guo zhaing*). Three entrepreneurs operated in this way. Unlike the passing account strategy, the other three entrepreneurs used the borrowed money for both registration and operation at start-up. This is the other form of help from relatives and friends.

In terms of the relationship between the entrepreneurs and the lenders in the six cases, there are two types of *guanxi*. In five cases, the entrepreneurs had long-term close *guanxi* with the lenders before business. Traditional Chinese values, such as filial piety, paternalism, and personalism, help maintain extended family structure and strong family bonds, which can be used to pool resources for the start-up and survival of business (Redding, 1990; Zheng, 1997). Unlike the five cases, in the remaining one case, the entrepreneur Mr. ZG did not have long term and close relationship with the lender, an estate boss. Mr. ZG only started to know the boss, when he worked for AT & T to build a network system for the boss. This means that Mr. ZG had known the boss for less than one year when he borrowed money for “passing account” to register his business.

Table 7.8 Two types of *guanxi* in helping start-up registered capital

<i>Guanxi</i>	Time	Rule	Trust	How to produce
Family and friend	Long term	Affection, obligation	Characteristics-based	Endowment, Saving
Mr ZG case	Short term	Trust & investment	Performance based	Investment and saving

The two difference types of *guanxi* between the entrepreneurs and the helpers in fact denote two forms of social capital as shown in Table 7.8. In the five cases, help was due to affection and obligations, a form of social capital (Coleman, 1988). In the cases of Mr. ZG, apparently, affection and obligation were not the lender's prior concern since they had not had a close relationship in advance. Instead, it is trust and investment that were considered. On the one side, Mr ZG is trustworthy. The trust came from the interaction between Mr ZG and the boss. More accurately, the performance of Mr ZG in conducting the programme for AT & T and further interactions that followed gave the boss the impression of his trustworthiness. This is so-called performance based social capital (Cohen and Fields, 1999), or process-based trust, compared with characteristics-based trust (Zucker, 1986) in the other five cases. Mr ZG's educational background with a master degree from a reputed university also grants him trust and social capital from restricted membership (Nahapiet and Ghoshal, 1998). Social capital serves as a kind of collateral, which those who have no access to the ordinary capital markets can use (Loury, 1977). On the other side, for the boss, lending him money to register a company is an investment to produce obligation credit, a form of social capital (Coleman, 1988). Such an investment seems, to some extent, to take the risk of Mr ZG's default in repayment. But in fact, the risk is very low, since the relationship between Mr ZG and the boss is not a simply dyadic one between him and the boss; instead it involves a

network, including the company colleagues whom Mr ZG used to work with, which potentially sanction him from opportunistic behaviour (Coleman, 1988). Trust can dramatically reduce what economists call transaction costs—costs of negotiation, enforcement, and the like (Fukuyama, 1995a). Mr ZG is indebted to the boss, for as Arias (1998) points out favours are banked.

7.4.6 Sources of real capital

It was found that three entrepreneurs in the group who relied on help from friends and relatives for registered capital borrowed money simply for the sake of registration procedure and did not actually put the money into the business. In reality, they relied on self-saving for real start-up capital. The finding thus requires further investigation into the sources of real capital at business start-up, which is more crucial to business operation. When talking about the most important source of available real capital at business start-up, only two entrepreneurs depended on money from family and one entrepreneur relied on borrowing from friends; altogether twelve entrepreneurs confessed that they had to rely on themselves. Fifteen entrepreneurs received investment from others (Table 7.9).

Table 7.9 The most important source of real available capital at start-up

Personal savings	Borrowing from friends & family	Investment from others
12	3	15

Much research (e.g., Bhide, 1992; Bourke, 1994; Mulholland, 1997; Kellard and Middleton, 1998; Redding, 1990; Wong, 1985) suggests that family is a most important

source of finance for business start-up. But the field research suggests that family finance does not appear so important in the Chinese private IT sector. Only two out of the thirty cases actually depended on family finance for start-up. This implies the need to research beyond family, because most Chinese families do not have extra accumulations of wealth after decades of socialism (Wank, 1999; Clark, 2000).

Further, between the two entrepreneurs relying on family finance, one comes from a peasant family; the other is from an ordinary cadre family. An entrepreneur might be able to raise some money from Auntie Li -- a rich relative with a soft spot for her entrepreneurial cousin -- but this requires that the entrepreneur is really lucky enough to have someone like that in the family. In this field research, no hard evidence supports the assumption that cadre family background provides advantage in start-up finance.

7.4.7 Personal savings for start-up

Table 7.10 How to accumulate for start-up

The source of accumulation	Number of cases
<i>Getihu</i> (Individual economy)	3
Working in companies	5
Moonlighting	4

There are several ways for the twelve entrepreneurs to accumulate capital as shown in Table 7.10. Three entrepreneurs accumulated their start-up capital from *getihu* (individual economy) operation. Five entrepreneurs saved money from their work in companies. The remaining four entrepreneurs' accumulations mainly came from their

moonlighting³⁵ activities, which occurred while two of them were working at state units, and the other two were studying at university.

Interestingly, three out of the four moonlighting entrepreneurs operated businesses by using the licenses of collective enterprises before formally registering their own firms. The entrepreneurs paid certain fees for the use of business licenses. The activities are in fact a form of leasing³⁶. But they did not have a contract for the leasing. Contract for such leasing is impossible and illegal, since the three entrepreneurs, as formal public employees or full-time students, were not eligible for leasing. But *guanxi* relationships between the entrepreneurs and the heads of the collective firms helped to arrange such transactions without a contract. From the providers' perspective, they could trust these entrepreneurs because they had known each other before. Informal institutions, such as particularistic social relationships (North, 1981) can supplement or substitute for legal structures in ways that reduce uncertainties and costs in economic transactions (Kollock, 1994). For the entrepreneurs, with such licenses at hand, their business operation became legalised. Moreover, their businesses were run under the guise of either collective or state owned ownership, which provide a form of social capital, trust from customers, within the environment of general discrimination and distrust against private businesses. In this sense, for the entrepreneurs with rented licenses, the availability of *guanxi*, with which the licenses were bound, is crucial to their accumulations of capital for start-up.

³⁵ According to a survey conducted by the Urban Survey Team of the State Statistics Bureau of China, more than half of the income of city residents was from moonlighting, while job-related income made up 44.5 per cent of their total income in 1999 (*Hua Sheng Overseas Chinese Newspaper*, April 3, 2000).

³⁶ According to Shen *et al.* (1996), there are three types for leasing collective firms: total capital leasing, partial capital leasing and intangible capital leasing. In the last category, a collective firm only "leases" its intangible capital, such as firm title, business license, and credit.

7.4.8 Investment from others

In the 15 cases that had investment from others as start-up capital, *guanxi* between the entrepreneurs and the investors can be sorted into two categories. Nine of the entrepreneurs had already known their investors before business start-up, the remaining six entrepreneurs only started to know their investors for the purpose of investment with the introduction by friends (Table 7.11).

Table 7.11 *Guanxi* between the entrepreneurs and the investors

Known before start-up				Introduced by friends for investment
9				6
relative	colleague	customer	other	
1	3	2	3	

In the six cases, *guanxi* between the entrepreneurs and the investors can be termed weak ties (Granovetter, 1973), but linked by common third parties. The intermediaries are social capital for the entrepreneurs, providing them with the information of capital source, and more crucially, verifying their trustworthiness to the investors.

Nine entrepreneurs already had *guanxi* with their investors. One entrepreneur obtained investment from his relatives, three entrepreneurs had investment from their former colleagues, and two entrepreneurs transformed their customers into investors. Among the remaining three entrepreneurs, one attracted investment from a fellow-townsmen, with one from former classmates, and the last one from friends.

These nine cases have one thing in common with the six cases that received help from

friends and family, i.e., the existence of *guanxi* prior to their business start-up. However, there are several differences. As was pointed out previously, the companies with investment from others tend to have much higher registered capital. More importantly, since it is investment, rational consideration is the main concern for the investors; on the other hand, the investors have to share the risk of business with the entrepreneurs. This contrasts sharply to borrowing from relatives and friends for start-up capital, where affection and obligation are the main factors that influence the decision of the lenders. The investors want the lowest possibility of risk and the highest possibility of return. While for the lenders, their concern is whether the borrowers will return the money. Though both settings involve trust, the nature of the trust is different. To the lenders, trustworthiness of the borrowers is the most important. However, to the investors, it is not only the good intent and credibility of the entrepreneurs that allow the investors to trust in them; the entrepreneurs must be perceived as being competent as well. Mishra (1996, cited in Nahapiet and Ghoshal, 1998, p252) puts four aspects of trust: (1) belief in the good intent and concern of exchange partners, (2) belief in their competence and capability, (3) belief in their reliability, and (4) belief in their perceived openness. Because *guanxi* is based on known people, reliability, morals and capability are known. Social networks functions as a lens or prism through which the qualities of actors are inferred by potential exchange partners (Podolny, 2001). This is in particular true in the two cases where the entrepreneurs obtained investment from their former customers, who themselves are operators of big private businesses. One of the entrepreneurs clearly said, "He (the investor) sees that our cooperation can make money, and I am able to make money for him. Thus he invested in this company."

7.5. Conversion of public finance?

Wank (1999) believes that money and other commodities, and the resources shifted from the public for commercial profit constitute the prime accumulation for business start-up. Entrepreneurs who have influential family background were advantaged in deriving start-up assets from public resources, either receiving start-up financial capital by bank loans from state banks or as money from public units, or accumulating financial capital by leasing wholesale firms. Field research does not find such cases of transferring public finance backed by family background. There is one case, which is more or less close to Wank's (1999) account. Before formally registering his own firm, Mr WZH in case 27 had done moonlighting with a computer trading company. Later he and his former classmates set up a collective company under the Chinese Academy of Sciences. They got a financial injection indirectly from a state owned company, where his classmate's father served as the general manager. The father invested a sum of money in another big collective enterprise, from which, Mr WZH's firm "borrowed" part of the investment as working capital. Although they returned the total amount of money they borrowed, such an injection was clearly important to the business of Mr WZH and his classmates. When Mr WZH formally set up his own firm due to a dispute over business with other partners in 1993, he invested his own savings as registered capital. No doubt, besides his moonlighting income, the accumulations in this "collective" business contributed mostly to Mr WZH's start-up.

The stories of the fifteen cases receiving investment are more complex than Wank's (1999) finding. According to the ownership of investment, the sources of investment in the fifteen companies can be divided into two groups: private and public. Eleven

companies had investment from private finance, i.e., from private businesspeople that sought new opportunities for their money; while the remaining four companies obtained public financial support from state owned enterprises. The fact that the majority of the cases obtained investment from private channels reflects the importance of private capital³⁷ in the IT sector. More importantly, the accumulations of private property demonstrate the development of the reform and its consequence, the emerging of a wealthy class (Liang, 1997), which in turn will have political economy implications for the Chinese society that need further research.

Table 7.12 compares the difference in private and public sources between the fifteen entrepreneurs with government experience and without. Four out of the six entrepreneurs with government experience received public investment, and the remaining two received private finance. This contrasts sharply to the entrepreneurs without government experience, none of whom received any public investment. Simply looking at the association between the sources of start-up finance and the background of the entrepreneurs, the first impression is that this confirms an obvious advantage in converting public resources.

Table 7.12 investment channels and work experience

	Government	Non-government
Private	2	9
Public	4	0

³⁷ According to the projections of the Chinese government, the total of China's private capital is expected to account for 66.5 percent of the nation's overall investment during 2001-2005 (*China Reform News*, March 3, 2000). Further, China has enormous potential for private investment. The saving deposits of residents amounted to RMB 6 trillion, in addition to RMB 1 trillion in cash, compared with about RMB 3 trillion saving deposits of enterprises in 1999 (*China Reform News*, January 12, 2000).

This source investment can be termed informal finance. There are some other forms of informal financing, such as usury found in my pilot research, and credit association (see, for example, Tsai, 2000).

However, one case shows a contrary story to Wank's (1999) conversion of public finance. When expanding in 1996, case 29 received 40 per cent of its RMB 10 million-registered capital, that is, RMB 4 million, from a state owned company. But later the entrepreneur was at odds with the general manager of the state owned company in how to operate the business. In 1998, they went to court, and the entrepreneur had to pay RMB 5 million to the state owned company. The two-year "interest" the entrepreneur paid for the RMB 4 million "loan" is RMB 1 million!

In fact, in all the four cases with investment from public finance, the ownership of capital is clearly defined. Moreover, the percentage of public capital investment is less than fifty percent. This can be understood in the context of progress in China's reform. Because of the regulations imposed by the government, state owned enterprises must be responsible for their own gains (Guthrie, 1998); on the other hand, mixed ownership has emerged, which was not imaginable before and in the beginning of reform, when there was clear boundary, and indeed, strict hierarchy between the private and the public.

7.6. Conclusion

From the field research, it is found that there are several channels of finance for the private enterprises in the Chinese IT sector. Compared with the general population of private enterprises discussed in Chapter 2, private firms in the IT sector are less likely to rely on personal savings (12 out of 30, 40 per cent, compared with 57 per cent for general private firms) and family (only 3 out of 30, 10 per cent, compared with 28 per cent for general private firms). Though like general private firms, they still have difficulties in access to formal finances, such as bank loans, they have more

opportunities to obtain investment (15 out of 30 cases, 50 per cent), which was only 2.6 per cent for general private firms in the 1995 survey.

Without formal channels of finance available to the private entrepreneurs, the private entrepreneurs have to resort to informal channels via *guanxi*. All the paths to get finance, whether investment was from other entrepreneurs, from personal savings, or from borrowing, have one thing in common, i.e., money was transferred through certain *guanxi*. In all the fifteen cases that got investment from others for start-up, the entrepreneurs either knew the investors themselves, or knew the investors via introduction by some friends. In the cases where the entrepreneurs had savings from moonlighting, they operated with leasing licenses from *guanxi*. During the enterprise registration procedure, though the entrepreneurs had to rely on themselves for real working capital, help from relatives and friends was essential. All these point to the importance of informal financial arrangement via *guanxi*. To some extent, it is *guanxi* that provided almost all the entrepreneurs with registered capital, as well savings for some, and investment for the others.

Different types of *guanxi* resorted to for start-up finance define the relationships between the parties involved, on the one hand; they also denote the application of different norms to such *guanxi*. Some types of *guanxi*, such as family relations, close friends, offer financial support mainly because of affection and obligation; while other types of *guanxi* take actions based more on rational consideration than obligation, which are what some researchers term “instrumentalism” (Gold, 1985). Nonetheless, all types of *guanxi* provide the entrepreneurs with certain forms of social capital.

As a form of social capital, trust is not only the credibility and good intent of the parties involved; it is also about the ability to be relied upon. Accordingly, trust is produced in different ways, such as performance-based trust and characteristics-based trust. All these findings enrich the social capital concept.

Further, in response to the discussion about power conversion theory, it is found that *guanxi* resorted to for business start-up finance is not necessarily cadre *guanxi* as the power conversion theory assumes. Furthermore, family, including cadre families, does not play a very important role in financing private IT company start-ups. There is evidence that the entrepreneurs with government experience have greater access to public financial source. This can be interpreted as the advantage that cadre entrepreneurs take, as the power conversion theory argues. However, this is not the simple conversion of public assets as some research suggests. Although the entrepreneurs without government experience seem to have disadvantages in this aspect, they receive finance from private channels, as an alternative. The different channels may partially be due to the different embedded structures (Granovetter, 1985) of the entrepreneurs, where the entrepreneurs with government experience are more likely to have contacts with state owned firms, and thus their seeking of financial capital is confined in the state sector, while the entrepreneurs without government experience tend to sort their problem out outside government in their private domain.

The finding in this chapter again points to the complexity of *guanxi* and social capital. *Guanxi* can be of different types and strengths. *Guanxi* are thus not necessarily cadre *guanxi*. For example, customers can become trusted *guanxi* and investors. Different norms underlie different types of *guanxi*, which are another variable contributing to the

contingent value of *guanxi* and social capital. Thus *guanxi* or social capital is not a static property of an individual; instead, it is dynamic. The existence of *guanxi* will not automatically produce an advantage, equally, for entrepreneurs with and without cadre *guanxi*.

This chapter looked at different types of *guanxi* used for start-up finance. The next chapter will examine the role of *guanxi* in finding customers at business start-up. More importantly, the dynamic aspect of *guanxi* and social capital, i.e., how different types of *guanxi* are brought into being is the main concern.

Chapter 8 *Guanxi* in finding customers

The previous chapter considered how different types of *guanxi* helped in financing business start-up. All these social relationships provide the entrepreneurs with social capital. This chapter examines another most important aspect of business start-up: finding customers. It looks at how the entrepreneurs found their customers via different types of *guanxi* at business start-up. How different types of *guanxi* come into being, or, how social capital is produced, is the focus of this chapter.

8.1 The importance of customer at business start-up

Customers are critical to every business. Even in e-business, customers are becoming ever more demanding of products and service (Treleaven, 2000). Like finance, customers are another most important aspect for business start-up (Churchill and Lewis, 1983). According to Bevan *et al* (1989), getting/finding clients were among the greatest worries for people setting up businesses in the UK. Also, it is the most feared for entrepreneurs in Poland and constrains their business development (Erutke and Vallee, 1997).

8.2 The main sources of customers at start-up

How did the private entrepreneurs in the IT sector manage to deal with this most important aspect of business operation at their start-ups? Again, *guanxi* played a vital role in finding customers at the beginning of business. The main sources of customers for the thirty entrepreneurs are shown as Table 8.1.

Table 8.1 The main sources of customers

Known	Introduced	Ordinary customer
8	14	8

According to the strength of the relationship between the entrepreneurs and their main customers, there are three main sources: known people as customers; customers introduced by someone else; and the ordinary customers attracted by either advertisement or shop. People known for a certain period of time are strong ties, while people introduced by a third party are weak ties (Granovetter, 1973) at the very beginning. Ordinary customers can be termed strangers; their relationship to the entrepreneurs are instrumental ties; while the other two categories, both strong and weak ties, are *guanxi* (Hwang, 1987).

Among the thirty cases, eight entrepreneurs mainly relied on people they had already known as their main customers at start-up. In this case, entrepreneurs have known their customers before they start their own business. This is in line with Arias' (1998) finding that *guanxi* is prior to and a prerequisite to the business relationship.

In two out of these eight cases mentioned above, the entrepreneurs did not have a stock of computers in advance when they set up computer trading companies. When the *guanxi* customers confirmed their purchases, the entrepreneurs simply resorted to a supplier for computers and handed them over to the customers. The gap between the price provided by the supplier and the price they sold was their profit. One entrepreneur joked at himself by saying, "My business sounds a carrying business, in a short distance. Sometimes, we took PCs from the next door to my company (who had the stock) to my

office. My customers came over to my office to collect the goods.” This is the paradigm for a computer trading company, in particular in the beginning of the booming of a computer product market, when people did not know much about computers and information about computers was not widespread in the early 1990s. Kornai (1992) argues that a legacy of the planned economy is its vertical channels for information flows on supply and demand between the centre and locales within the state structure. For the entrepreneurs, the asymmetric information in the market provided them with opportunity to seek profit. Social networks are a conduit or pipe for information and resources in the market (Podolny, 2001). Information about the known people’s need for computers and the trust from known people are two forms of social capital (Coleman, 1988). The social capital of the entrepreneurs helps the transactions to proceed.

Twelve out of the thirty entrepreneurs had most customers introduced by *guanxi*. In this circumstance, the entrepreneurs do not know their customers in advance. In order to sell their products, they ask existing *guanxi*, including relatives, former colleagues, friends, and fellow townsmen, etc. to help them find customers. *Guanxi* can extend beyond the relationship between two parties (Arias, 1998), the customers and the intermediary. The existing *guanxi* are likely to have close ties with the customers, while the relationship between the entrepreneurs and the customers are weak ties (Granovetter, 1973). As has been shown in Chapter 6, weak ties can also help roll the snowball. Similarly, weak ties, which are embedded in networks that do not overlap with those of the entrepreneurs, are more likely to have different information and have the strength of providing the entrepreneurs with new information and opportunities.

More importantly, weak and strong ties are not absolute and static. Weak ties can be developed into strong ties. In fact, several entrepreneurs admitted that some of their known customers were stranger customers at the first stance and they became good friends in the following business transactions, who in turn help introduce new customers to the entrepreneurs. Such a transformation will be examined in the coming sections.

In the remaining ten cases, most of the customers were “stranger” ordinary customers, that is, the entrepreneurs did not know these customers at all. They were either attracted by the advertisements of the products or by the shops the entrepreneurs ran. The relationship between the entrepreneurs and the customers is not *guanxi* at the first stance of business transaction. These instrumental ties are based on achieving specific goals, existing between people who interact with each other on a short-term basis, such as a salesperson and a customer (Hwang, 1987).

In fact, two firms in this group can also be counted in the category of relying on introduced customers. The two firms produced and sold education software to higher schools at start-up. They placed advertisement on some popular education magazines to publicise their products. Afterwards, they started to ask their *guanxi* network to introduce them to school teachers. If they could not find anyone to bridge them over to a school, they went for door-to-door sales. Some schools contacted them directly to enquiry about or buy their products. However, in order to guarantee a transaction, they often tried their best to find out some *guanxi*, who could bridge them over to the targeted customers, usually school principals, who make decisions.

As Chapter 7 suggested, five cases out of the thirty are in E-businesses. Four of them

relied heavily on *guanxi* for getting customers at start-up. The entrepreneurs in these four cases stated that the Internet only provides them with a platform to operate business, which is like a stage for performance. The practices behind the stage are much more crucial to the success of a performance. The other Internet housing company is having trouble attracting customers, perhaps partially due to not cultivating a well-prepared *guanxi* base. The interviewed entrepreneurs call this ‘*guanxi* resources integration’. Thus, Han (2000) comments that even to the surprise of many business-to-business dot-com start-ups, touting disintermediation as their main value proposition, existing channels dominated by *guanxi* vendors have not been wiped out as expected. You may do business online now, but you end up using the same old middlemen. Perhaps, this is most ironic to E-commerce.

To summarise, it is found that fewer than one third of the cases had known customers (eight out of thirty cases). This reflects the weakness of strong ties (Granovetter, 19973), i.e., the number of known people as customers is limited. The entrepreneurs were more likely to rely on customers introduced, the weak ties (Granovetter, 1973). However, the intermediary who introduced the customers to the entrepreneurs are existing *guanxi*! Hence, at least two third of the cases (twenty two out of the thirty cases) mainly relied on direct *guanxi* (known people) and indirect *guanxi* (introduced by known people) to get their customers at start-up. This once again justifies the importance of *guanxi* in business start-up. Informant 31 argued that a business could survive without *guanxi*, provided high quality of product and competitive price, but the business came at the cost of very low margin. Further he revealed:

If you treat the head of your danwei customer in a sauna house, the atmosphere is changed. Everything can be discussed (You can talk very frankly, and the head does not need to hide his intention). He may say, “Well, the price of RMB 1,800 is too low, I can offer you a price of RMB 2,600”. Then the gap of RMB 800 is kickbacks.

Actually RMB 1,800 is a good price for my business.

8.3 Mass product versus project and their customers

An interesting finding is that when the entrepreneurs produce or provide a mass product, they are less likely to rely on *guanxi*. As chapter 7 describes, there are 10 firms in PC trading business that produce and sell PCs and PC peripheries, which are mass products to individuals. In five out of the ten cases, the entrepreneurs' most customers were ordinary strangers, instrumental ties (Hwang, 1987). Contrasting sharply, only three out of the other twenty cases, whose products were more likely for customers other than individuals, i.e., a *danwei* (work unit), mainly a public buyer, relied on ordinary stranger customers. A *danwei* is usually a big buyer. Though the number of such buyers is small, the sales volume can be big. In other words, if the customer is a big buyer, *guanxi* is extremely important. This tendency can be seen in the comparison shown in Table 8.2.

Table 8.2 Different *guanxi* with main customers at start-up

	Known	Introduced	Ordinary customer	Total
PC firms	2	3	5	10
Other firms	6	11	3	20
Total	8	14	8	30

Most of the entrepreneurs define *guanxi* as a reciprocal relationship with officials in charge of projects³⁸. Unsurprisingly, the entrepreneurs, who sell products to *danwei*,

³⁸ A *danwei*, for example, may have a so-called office automation project, which needs both PCs and software. Though data on *danwei* buying power is not available, the estimated government procurement gives a clue. According to *China Business Times* (August 15, 2000), in general, government procurement amounts to about 10 per cent of a country's GDP. In 1999, the Chinese government

regard *guanxi* with them extremely important. The *danwei* officials make decision on what product they will buy. In the office, publicly, these officials appear to be “*gongshi gongban*”, doing official business according to official principles, and they seem not to let personal consideration interfere with their execution of public duty. But after the businessmen get familiar with them, everything can be under consideration. The head officials are crucial, since they are decision makers. However, this does not mean that the other related officials are not important³⁹. The entrepreneurs or their agents (such as sales representatives) must keep good relations with all of them, though costs of keeping different relations vary and they must cater to the differentiated interests of the officials.

In a similar vein, Staniszkis (1991) terms the advantage the cadre entrepreneurs take as political capitalism. In the companies run by the cadre entrepreneurs in East Europe, the main customer is not the consumer market but state industry. Profits are derived from the exclusive access to attractive markets, information and supply made possible by the dual status of the nomenklatura owners. Unlike Staniszkis’ (1991) finding, the Chinese officials in power realise their personal profit by turning power over goods into kickbacks without operating their own firms. In a sense, the entrepreneurs and the officials become agents to each other and they have a division of labour.

For case 21, *guanxi* relations for their business are comparatively stable at the moment, since the officials will stay in their posts for about three years. Thus informant 21 joked

purchasing was about RMB 1000 billion. The Chinese government mainly purchases goods, projects and services.

³⁹ A very interesting relevant case was published in *Business Week* (September 30, 1996). A leading salesman of Boeing Company, Lee Hsiung-Fei, knew everyone on the Chinese side, from line mechanics to pilots prior to the delivery of the first 767 airplane. When pilots, engineers and managers flew to Seattle to take delivery, he took them sightseeing, shopping, and hosted them in his home. According to his experience, he said, “It is important to get to know the airline at every level, down to the foot soldiers”.

that the time for them to be in positions was almost the same as the life cycle of the company's product. These officials are in their 50s, nearly retired age. What will happen when they retire is unknown yet to the company. It is argued that in China, those officials and managers in their late 50s are more likely to be found guilty of corruption or bribery⁴⁰, hence the term as "59 phenomenon"⁴¹. These officials know their power will have expired when they retire and thus grab money before losing power. For the entrepreneurs, this type of *guanxi* is useless once they retire, since they cannot provide social capital any more.

8.4 Different ways of having *guanxi*

As found previously, known people as customers and the intermediary resorted to for customers are *guanxi*, and the majority of the firms, i.e., twenty-two out of the thirty cases, relied on *guanxi* to sell their products at start-up. Further, it is found there are different types of *guanxi* relied upon for the operations, which include classmates, fellow townsmen, relatives, colleagues, former customers, friends' friends, and so on and so forth. Accordingly, there are different ways of having such *guanxi*. Some of them are from endowment, with some from savings, some from investment, some from subcontracting, and the rest from newly building up.

⁴⁰ The Berlin-based anti-corruption non-profit organisation, Transparency International, has compiled a 10-point Perception of Corruption Index of capturing the perceived level of bribery in various countries. The index, released annually, pulls together existing polls of international businessmen and financial journalists on their assessment of corruption in different countries. In 2001, Finland was listed on the top as the least corrupt country at a score of 9.9 out of 10. Singapore, Hong Kong and Taiwan had a score of 9.2, 7.5 and 5.9 respectively. The Mainland China was put near the bottom of the list with a higher level of corruption at an average score of 3.5 with Indonesia at a score of 1.9 (*Transparency International Perception of Corruption Index, 2001*).

⁴¹ For example, a model entrepreneur of a state owned store in Zhuhai City near Hong Kong has been arrested after allegedly accepting RMB millions in bribes. The entrepreneur Zhang, aged 57, had been labelled Zhuhai's "iron-woman" by the media. The anti-corruption investigator said many senior cadres, such as Zhang, were threatened by the retirement plan and were tempted to solicit private gains in the years before their retirement (*South China Morning Post, November 21, 2000*).

8.4.1 Endowment of *guanxi*

Wank (1999) has explained that *guanxi* from endowment are the social relations by virtue of birth into a family of a particular social class. Family background endows some entrepreneurs with certain types of *guanxi* with strong obligation. Consanguineous ties and family friends are in this category. An obvious example of this route of *guanxi* is seen in the members of the so-called “princes” party, the offspring of elite central officials (Tao and Ho, 1997).

Chapter 7 has found that few entrepreneurs were born in Beijing and most of the entrepreneurs come from ordinary families far outside Beijing where their firms are located. The entrepreneurs born in Beijing sometimes could access their endowment *guanxi* for help. For example, they asked their relatives to help introduce customers. Those born beyond Beijing do not have much social capital from endowment. Instead, they mostly rely on *guanxi* from other channels.

8.4.2 Savings of *guanxi*

A second route of *guanxi* is savings, which are mainly acquired through life experiences. In other words, this type of *guanxi* is accumulated during the time of common experiences or common background. An example of this source of *guanxi* is classmates. As Chapter 7 suggests, almost all of the interviewed entrepreneurs have university education background. Also, almost all of them admitted that they received help from their classmates in business start-up and they most frequently contacted their classmates, including classmates at an early age.

After years of studying together, two individuals have known each other very well. They not only share the same background of education and study experience; they may also have common hobbies. Classmates become a sort of close *guanxi*. However, it must be noted that not all classmates can be regarded as *guanxi*. It is true that there exists relationship among all classmates, but surely not all of the classmates would treat each other as *guanxi*. For example, two classmates do not get along well during the years of study, and neither would define the counterpart as *guanxi*. As Burt (1997b) finds, difficult colleagues are rarely chosen for personal relations.

The existence of relationships linking individuals is objective. Further, *guanxi* is a subjective perception of the parties involved. It is based on mutual recognition of the relationship between the two parties. Bourdieu (1986) thus argues that social capital involves durable obligations subjectively felt.

This type of *guanxi* usually has existed before an entrepreneur's business start-up (Wank, 1999). The pre-business *guanxi*, based on common life experiences, is often affection-motivated and has hardly anything to do with economic considerations at the beginning. This is especially true before people have decided their careers. The younger the age when a type of *guanxi* is set up, the purer it is. In reality, it cannot be ruled out that people deliberately cultivate *guanxi* for a future business career. Pre-business *guanxi* does not necessarily exist for purposes of economic gain, but it can be utilised for economic gain. Since pre-business *guanxi* is more likely to be affection based, obligations are more likely to be concerned, and accordingly economic gains may not be the priority of the concern. When an entrepreneur was asked if he paid interest to his friend who lent him money for business, he laughed: "We have never thought of this, as

we are good friends.”

8.4.3 *Guanxi* from investment

To some extent distinct from *guanxi* based on savings, *guanxi* relationships from investment are more likely to come into being for the purpose of business. Also, they are more likely to be termed business *guanxi*, compared with *guanxi* from savings. The first step, or, the basis for this type of *guanxi*, is to establish *guanxi*. Then, investment is needed to develop and maintain *guanxi*.

8.4.3.1 Establishing *guanxi*

Guanxi is a relationship of mutual recognition, as pointed out earlier. *Guanxi* commonly refers to friends, schoolmates, colleagues, and other acquaintances, which come from long time of interaction. Interaction between two individuals can lead to the establishment of *guanxi*. But where is the starting point of *guanxi*? Something in common acts as an intermediary for further interaction. The intermediary can be common experience, common background, and so on so forth, in a word, something in common.

The two parties can find something in common to start up their *guanxi*. For instance, when two individuals meet in certain settings, they may talk about where they come from, particularly if they are familiar with each other's accent. If they share the same dialect, the distance between them suddenly is shortened. *Laoxiang*, fellow townsman, becomes an important intermediate linking two individuals together. *Laoxiang* is

actually a flexible term for people from the same area. Geographically, the area can be a village, a town, a county, and even a province, and sometimes, it can be larger. In general, the closer geographically the hometowns of the two individuals, the closer they feel, and the more potential they will establish *guanxi*.

Similarly, another common reason for establishing *guanxi* can be alumni associations. The two individuals have not necessarily known each other before, and actually they may not have studied together during the same period.

If the opportunity of face-to-face interaction is not provided, introduction of a third party can bridge the gap. The logic is often “ My friend’s friend is a friend of mine, too.”

These are the most common bases for the entrepreneurs to establish social *guanxi* with someone they did not know before. The three common bases act in essence as an instrument to verify the reliability of both parties. When trust is built, *guanxi* tends to be closer, and further interactions ensue.

If entrepreneurs possess no basis for *guanxi*, but anticipate the need to request a favour, they may attempt to develop personal relations based on some other common experiences, such as common tasks and/or mutual enjoyments. Alternatively, joining certain associations can lead to knowing people and building *guanxi* (Odgaard, 1992). Bourdieu (1986) has also pointed out that people will consciously join certain clubs that provide social capital. However, belonging to the same association does not produce social capital as some social scientists optimistically assume, instead, the formal

associations may only be a small factor in the production of social capital or trust (Lyon, 2000). Nevertheless, belonging to the same association builds the basis for further interaction, which may lead to *guanxi*. Indeed, it is possible to consider every basis of *guanxi* to be a form of common experience.

An obvious practical difficulty in the formation of the basis of common experience is that there is no well-defined extent and type of experience that constitutes an adequate basis. Since the existence of trust is the essential criterion, regardless of the nature of the common experiences, common experience is indeed an excuse for building up *guanxi*. Whether real *guanxi* can be established and counted on needs further test in future interactions, in business terms, business transactions. As Falk and Kilpatrick (2000) observe, a precondition to building social capital is the existence of sufficient numbers of interactions of a particular quality.

8.4.3.2 Developing and maintaining *guanxi*

The basis of common experience or background only provides potential for setting up *guanxi*. Mutual recognition of a basis for *guanxi* is a necessary but insufficient condition for the existence of a *guanxi* relation. Social *guanxi* is dynamic, whose strength depends more heavily on interaction, unlike family (blood) *guanxi*, which is given and exists for sure. Once a basis for *guanxi* has paved the way for an opportunity to build *guanxi*, it must be nurtured by interpersonal interactions so that *guanxi* relationships can be activated. Rusbult (1980, 1983, and 1987) finds that the stability of a relationship depends on costs and benefits at present, and also on investments made in

the past and the degree to which support was given and received over time (cited in Van Duijn *et al.*, 1999, p191).

Documented research has pointed out the importance of gift-giving in *guanxi* exchange and investment (e.g., Walder, 1986; Solinger, 1989; Yang, 1989 and 1994). Further, Yang (1989) argues that the gift economy is one of the three modes of exchange in China, along with the state distributive economy and commodity economy. Nevertheless, investment in *guanxi* does not simply mean gift-giving or money. Bourdieu (1986) notes that the investment implies expenditure of time and energy, which in turn means direct or indirect expenditure of economic capital. To develop and maintain *guanxi*, investment is more than gift-giving. Time and efforts are also needed. There are some basic rules for the interactions.

First of all, it does not have to be based on money. Money talks, but money does not work in every setting, and sometimes, money has counter-productive result. For example, if money is offered soon after help, *guanxi* tends to be understood as money *guanxi*, or, “fee-for-service” *guanxi* (Luo, 2000). The impression is that the *guanxi* is or a one-time deal, which is not different from the exchange between two strangers. *Guanxi* ties will not last long. Informant 21 warned, “Presenting money inappropriately can result in distancing your *guanxi* and you.”

In a similar vein, Davies *et al.* (1995) point out that exchanges between *guanxi* need to be handled sensitivity as Western businessmen are in danger of overemphasizing the gift-giving and wining-and-dining components of a *guanxi* relationship, thereby coming dangerously close to be perceived as meat and wine friends, which is a Chinese

metaphor for mistrust. In the case where manipulative intent becomes apparent to the gift or favour receiver, the present may be refused or devalued and the manipulation fails to achieve its instrumental intent (Smart, 1993). Also, gift-giving may be viewed as bribery⁴².

Informant 32 gave a vivid metaphor about the delicacy of such interactions, “Don’t let spring know of planting willows ”. The appropriate approach for interaction must be considered according to circumstances. For instance, treating someone with decency while others treat him/her unfairly could result in a good relationship.

Also, it starts with and builds on the trustworthiness of the individuals. If an entrepreneur promises something, he must do it to show his trustworthiness. Mutual trust promotes close interactions, and thus *guanxi* is strengthened. It is also the case for a company. If a company promises certain things and delivers as promised, the company is showing trustworthiness and the counterpart would be more inclined to deal with them in the future. Informant 22 Mr WXQ’s story, which is about why a university professor became his regular customer and introduces new customers, demonstrates this point.

Some years ago, he popped in my shop to enquire about buying a home used computer. I happened to be on duty in the counter that day. I answered every question he asked patiently and clearly, though he only said that he would like to know more about computer and showed no sign of buying a computer. Several days later, he came back again and bought one. He is satisfied with our computer quality and service. More importantly, he believes that we are trustworthy, as we promise something, for example, quick service, we definitely deliver it. Now,

⁴² For further discussion about the relationship between gift-giving and bribery, and thus Guanxi and corruption see Luo (2000) and Wang (2000).

the professor introduces not only his friends and colleagues but also some laboratories to buy PCs here.”

Indeed, the trustworthiness of a company is built on the conduct of the individuals. A company’s image can come from conduct of every individual of the company, good or bad. Bearing this in mind, the entrepreneurs pay attention to the trustworthiness and reliability of the employees when they recruit.

It is also important to remember that frequent contacts with each other foster understanding and emotional bonds. A critical social capital of trust, not just obligation, is created through the repeated exchange of gifts and favours. *Ganqing* (feeling) is an important element in *guanxi*. The closer in emotional bond, the more obligations are felt in *guanxi*, and the more help can be expected from such *guanxi*. In practice, such contacts involve expressions of concern for another’s welfare and well-being through shows of human sentiment (Wank, 1999). Informant 11 had a good comment on how to maintain *Guanxi*:

Firstly, do not forget to bother your *guanxi*. This is the best way to keep in touch with *guanxi*.

Secondly, do not forget to help him or her, that is, repay the favours you have received.

Finally, the norm of reciprocity must be obeyed. The principle of *renqing* that underlies most *guanxi* ties suggests that favourism is often followed by a strong expectation of reciprocity (Hwang, 1987). The return of favours is certainly needed for further *guanxi*, but it must be returned in the right time and the right form, say, “a friend in need is a

friend indeed". For gift-giving⁴³, a form of reciprocity, the common time for entrepreneurs to reciprocate their *guanxi* ties is some important holidays in China, such as Spring Festival, Mid-autumn Festival, when either cash or gifts can be offered to a *guanxi* tie. The gifts can be presented either to the *guanxi* tie himself/herself or to other members of the *guanxi* family. Social life is a constant give-and-take. The latent function or purpose of the gifts is to establish the obligation to engage in social interaction and to uphold those obligations entailed in such interaction (Mauss, 1969).

Subcontracting is another important way that the entrepreneurs in the case studies developed *guanxi*.

8.4.4 Subcontracting *guanxi*

According to Mieghem (1999), the word subcontracting has been used for nearly two hundred years. The term refers to the practice of one company (the subcontractor or supplier) providing a service or good for another (the contractor, buyer, or manufacturer). Typically, subcontracting is the situation where the contractor "procures an item or service that is normally capable of economic production in the contractor's own facilities and that requires the contractor to make specifications available to the subcontractor" (Day, 1956, cited in Mieghem, 1999, p954).

Such subcontracting exists in the business operations of the interviewed private entrepreneurs, too. Some small software companies do not have the ability or reputation to secure big system integration contracts. They keep a close relationship with certain

⁴³ Yan (1996) classifies gift givings in a Chinese village into three categories: expressive gift giving on ceremonial occasions, expressive gift giving in non-ritualised situations, and instrumental gift giving (cited in Wang, 2000, p550).

big companies, who have such projects and subcontract some products needed in the whole projects, such as software, to the small ones. The small companies have *guanxi* with the big ones. In fact, in several cases, the *guanxi* persons in the big companies are stakeholders in the small ones.

As well, some interviewed companies do not have the ability to produce everything for their customers; they subcontract what they cannot provide to some other companies. *Guanxi* is an important factor in the consideration of such subcontracting, that is, they tend to subcontract the service or product to *guanxi*, which benefits both sides.

The above-mentioned are similar to the standard practice of subcontracting, and accordingly they gain similar benefits, such as the value of flexibility (Friedman, 1977), enabling enterprises to cut costs and spread financial risks (Colling, 1995). Subcontracting or outsourcing creates great opportunities but also new types of risks, including loss of control over a subcontractor or supplier. With *guanxi*, such subcontracting has not the risks. This is because *guanxi* is based on a long-term relationship, of which, trust, in terms of the ability to rely on, is important. Thus the most successful outsourcers find it absolutely essential to have both close personal contact and rapport at the floor level and political clout and understanding with the supplier's top management (Quinn and Hilmer, 1994).

Unlike the above-mentioned two circumstances, where the existing *guanxi* is the precondition of subcontracting and the contents of subcontracting are products and services, to subcontract *guanxi* is to utilise the *guanxi* of another when the entrepreneurs themselves lack such *guanxi*. In this case, *Guanxi* is the subcontract content.

Subcontracting renders the subcontracted process “someone else’s problem” (Colling, 1994). I call this subcontracting *guanxi*.

This is because the entrepreneurs cannot always have *guanxi* covering many areas where they plan to do business. Even if they have *guanxi* in the target areas, the existing *guanxi* may not work all the time, as is pointed out in Chapter 6, *guanxi* is contingent upon situations. A possible solution is to build new *guanxi*. However, *guanxi* is in general a long-term oriented relationship, and building *guanxi* is a lengthy process. The entrepreneurs cannot wait till *guanxi* is set up. The strategy is to subcontract *guanxi*. This is in particular important for those firms that do trans-regional businesses, where the entrepreneurs themselves either have no *guanxi* or have no time to develop *guanxi*.

Agents are a common choice for subcontracting *guanxi*⁴⁴. The need for *guanxi* is subcontracted to agents who have strength in this respect. People of such strength head the branches or offices. Product sales are expanded to many places where branches or offices are located. From this aspect, a *guanxi* marketing approach is used. In essence, it is *guanxi* that counts. *Guanxi* is subcontracted and expanded; as a consequence, products are sold. Similarly, Luo (2000) argues that sales force marketing strategy has become increasingly popular and effective. The activity, which heavily depends on *guanxi*, has three forms: direct dispatching of marketing personnel, setting up regional sales office, and selecting sales representatives from outside of the firm on a commission basis.

⁴⁴ Increasingly, multinationals are recognising the advantages of *guanxi* available to Hong Kong entrepreneurs and are using them as middlemen, brokers, and subcontractors as a more efficient way of entering the Chinese market (Pomfret, 1991).

In the case of subcontracting *guanxi*, cost considerations are the entrepreneur's concern, but the absence of necessary input of *guanxi* for sales is the main reason. There are a variety of practices of subcontracting. The first is similar to internal subcontracting within the firm, where a person with such *guanxi* resources is employed as a member of the firm. The entrepreneur pays the person salary, plus a certain percentage of bonuses from sales. The more the sales, the more the bonus. In the second case, the subcontractor gives the contractor a price for its product, the contractor itself sets the sale price to customers, and the balance between the two prices is the contractor's *guanxi* reward. In this circumstance, the subcontractor does not invest in the contractor, and the contractor sometimes does not need an office. A third way is that both the subcontractor and the contractor invest certain amount of money according to contract to set up an office, and the two parties share the profits. In all the three circumstances, the subcontractor provides product and services after sales.

An ideal agent is an existing *guanxi* tie, or introduced by an existing tie of the entrepreneur. But this is not necessarily the case. Instead, it can be found through advertisement. Nonetheless, certain *guanxi* resources are required for an agent so that the entrepreneur's product can be sold on the basis of the resources. In the advertisement description, it is clearly stated, "the applicants must have broad *Shehui guanxi* (social relations)". The agent can use his or her direct or indirect social network to promote products. As a result, *guanxi*-based selling can produce impressive marketing performance even when the product itself is not competitive (Luo, 2000).

Because the relationship between the contractor and the subcontractor is not well built, rather, it is mainly interest based, the subcontractor is very cautious at the beginning.

The subcontractor will try to verify the trustworthiness of the contractor via many channels, and a formal contract will be signed. Meanwhile, the subcontractor tends to bind the contractor into the business by requiring certain investment from the contractor. As reliability can only be communicated through action (Sobel, 1985). When the performance of the contractor demonstrates its reliability in a certain period, the subcontractor will invest more and rely more on the contractor. Successful experiences identify good partners and permit increases in the scale of exchange (Sobel, 2002, p150). Performance strengthens *guanxi*, and further co-operation follows.

8.4.5 Symbolic *guanxi*: linking to the elite

Private entrepreneurs like to have *guanxi* with the elite, since the elite are in advantageous positions. However, the elite are in the higher positions of social hierarchy, and are thus not always easily accessible for the entrepreneurs. Building *guanxi* with the elite is difficult. As is found, *guanxi* is a relationship of mutual recognition by the both sides involved. Without subjective recognition from both sides, there exist no obligations. The party in the advantageous position has no duty to help the other. But this does not jeopardise the entrepreneurs to take advantage of linking to some elite, though there is no real *guanxi* between them. They can set up symbolic *guanxi* with the elite after a face-to-face meeting, provided with evidence of such a meeting between them.

One entrepreneur hangs a very big framed picture taken with the CEO of the chip giant Intel on his PC shop. This is a mute testimony to his credibility in business. The picture acts as a third authoritative party to issue him credentials, which gives consumers a

reliable signal. Similarly, Unicom-Sparkice, a joint venture in the IT sector in Beijing, prints company fliers displaying the signatures of Prime Minister Zhu Rongji and President Jiang Zemin alongside those of Bill and Hillary Clinton. In China, such signature collections function as endorsements of talismanic import (*CNN*, January 19, 1999).

It is common that companies post pictures of the elite, in particular government VIPs, who have visited them, or calligraphy by such VIPs, as credentials to prove what they claim, and an instrument to promote their products. The higher the rank of the VIP and the more famous the VIP, the better the result is. This is because of the long history of officialdom-dominated civilisation in China (Bruun, 1993). The government has to ban such publications again and again, considering the activities ruin the VIPs' and government's images.

In fact in such circumstances, the entrepreneurs do not have personal relationship with the elite. For example, though the entrepreneur I interviewed did meet the CEO of Intel once, the relationship between him and the CEO is not *guanxi* as we discuss it here. He knows the CEO, as many other people, but the CEO does not know him, and has no obligation at all to help the entrepreneur. Thus, I call this kind of relationship symbolic *guanxi*, linking the entrepreneurs to the elite, rather than connection or *guanxi* with the elite. Nevertheless, such *guanxi* promotes the entrepreneurs' product sales.

It is not the meeting with the elite or shaking hands with the elite that is the condition for building such symbolic *guanxi*; instead, it is the symbolic themselves, such as photos taken with the elite that demonstrate the relationship. The entrepreneur might

have not the chance to meet the elite, but they can link themselves to the elite. For example, business boards carrying the elite's calligraphy commonly seen in China, help link the entrepreneur with the elite. Entrepreneurs can get handwritings of elite via certain channels. In some cases, entrepreneurs have to pay for such handwritings either to the elite or the channels. The handwriting of a former vice governor of Jiangxi province was displayed by many businesspeople, and the governor received considerable money for such writing (*China Daily*, March 12, 2000).

8.5 Conclusion

Again, the field research in the private IT sector suggests that in another most important aspect of business start-up, finding customers, *guanxi* plays a pivotal role. This finding does not support the argument that with the progress of reform, the importance of *guanxi* is declining (e.g., Guthrie, 1998). As found in Chapter 6, *guanxi* is contextual. It can be true that *guanxi* is not important in certain contexts. For example, as found previously, when their products are mainly for the mass market. Also, *guanxi* is not essential any more in getting everyday living goods such as food (Yang, 1994). The general argument that the importance of *guanxi* is waning is not appropriate. *Guanxi* still plays a very important role as suggested above and in Chapter 7.

This chapter finds that there are many ways of having different types *guanxi*. As power conversion theory suggests, being born into a cadre family or being a cadre can provide entrepreneurs with social capital. But these, endowment of *guanxi* and savings of *guanxi*, are simply two of the channels that produce social capital. *Guanxi* from endowment is not elective, other types of *guanxi*, in particular from investment and

subcontracting, are consciously created and developed. The practice of *guanxi*, the art of *guanxi*, provides entrepreneurs with potentials when *guanxi* has a competitive advantage in business.

Part 4 Conclusion

Chapter 9 Conclusion

9.1 Themes of the thesis

This thesis contributes to an understanding of private enterprise start-ups in China. In addressing this central question, it critically examines and utilises social capital theory. As there is no available research focusing on business start-up in the Chinese private sector, this thesis starts with some broad relevant literature for guidance. In the theoretical part of the thesis, after clarifying the concept of cadre, the thesis tests the dominant power conversion theory by analysing a national survey data on Chinese private enterprises. Further, it explores the reasons why there is no statistical evidence to support the argument that cadre-related entrepreneurs have an advantage in business start-up. It goes on to examine the two key concepts of social capital and *guanxi* and points out some weaknesses in the current literature. The case study part of the thesis aims to fill in some of the main deficiencies in the existing literature on social capital and *guanxi*. It studies how *guanxi* helped the researchers conduct fieldwork and businesspeople in the private IT start up their businesses. It further examines how *guanxi* and social capital are produced.

This chapter concludes the thesis. It draws together the threads of the previous chapters. Then it suggests some areas for further research opened up by this study. Lastly, it speculates some further implications of this research.

9.1.1 Background

This thesis presented the background of this research in Chapter 2. As the private sector was under-researched, compared to state owned enterprises, township and village enterprises, and foreign direct investment. It looked at the policy changes, operation environment and the development of the sector. It suggested that the private sector has played a more and more important role in the Chinese economy and social life.

9.1.2 Testing power conversion theory and cadre

As there exists no systematic research focusing on business start-up in the Chinese private sector, this thesis started with an examination of the relevant literature on post-communist societies in Chapter 1. According to the dominant power conversion theory, during the transition from socialism to capitalism, power accumulated during state socialism is converted into assets of high value in a market economy. Cadres are at an advantage not only in starting up but also in operating companies, because they can transfer state assets into quasi or real ownership for business. Also, they can use their social relations (networks) to get access to credit and valuable information. Entrepreneurs born into cadre families can take similar advantages into business. As a consequence, entrepreneurs who have been a cadre or have cadre connections are more successful.

Following the logic of power conversion theory, this thesis proposes two hypotheses that should hold in empirical data. Entrepreneurs with cadre background or close cadre social relations should be more likely to have much higher start-up capital. They should also be more likely to finance their start-ups from public funding.

The test of the hypotheses is based on an analysis of the unpublished 1995 national survey data set on private enterprises in China. In Chapter 3, in line with the power conversion thesis, the social background and the social relations of an entrepreneur, including the entrepreneur's father, spouse, closest relatives and closest friends, are examined. These variables are coded as a dichotomy: cadre and non-cadre. For start-up financing, variables used are: 1) the registered capital at business start-up; 2) the real assets at start-up; and 3) the main sources of start-up registered capital. Cross-tabulation analysis and the Chi-square test are utilised to examine the association between the entrepreneurs' background variables, i.e., their social origins and social relations, and business advantage variables, i.e., the registered capital and real assets at start-up, and the main sources of finance.

A surprising finding from the analysis is that being a cadre or having close cadre connections does not seem to have significant advantages in private enterprise start-up financing. In other words, statistically, being a cadre and having close cadre social relations does not tend to be associated with higher registered capital and real assets at business start-up. Neither do they seem to be more likely to have finance from public sources, such as bank loans and money from public units.

It is noted in Chapter 3 that it is essential to give a clear definition for the key term of cadre in testing the power conversion theory, as it has several meanings in different contexts in China. The argument that cadre related entrepreneurs have an advantage in private business operation is not convincing without a well-defined cadre concept.

In one usage, cadre refers to the personnel in government, Party, business enterprises

and service establishments, including technicians and teaching personnel (Vogel, 1967). Thus cadre can be understood as a class in contrast to worker and peasant. In another usage, people refer to anyone in a position of power as a cadre (Manion, 1985). Technicians and teachers, who are also titled cadres, are unlikely to have redistributive power of resources. It is the cadres in government who are in charge of the allocation of the resources in short supply (Walder, 1986). Thus a good definition of cadre should reflect the positional power in the hierarchy or the power of allocating resources of a cadre.

A cadre, for the purpose of testing the power conversion theory, is defined as someone reaching a certain position of power. The cadre category includes not only someone at the very top of the communist hierarchy but also everyone who reached some position of power, ranging from chief prefecture and county level officials down to village heads, who have the power of allocation of resources. Based on the clearly defined cadre concept, the analysis of the 1995 national survey on China's private enterprises does not support the general power conversion theory. Nor is this theory supported even if cadre is defined in a more restrictive manner to refer to those high level positions. It thus suggests that further qualitative research investigating how private entrepreneurs start up their businesses is needed.

9.1.3 Social capital and *guanxi*

It is argued that the logic of the power conversion theory is in the frame of Bourdieu's (1986) social capital theory. As Bourdieu (1986) notes, dominant social classes can use their privileged access to the three forms of capital, namely, economic capital, cultural

capital and social capital, to make strategic conversion of one kind of capital to another in order to solidify their class position. According to Bourdieu (1986, p248), social capital refers to the actual and potential resources embedded within, available through, and derived from the network of relationships possessed or created by an individual. In ordinary language, social capital can be termed connections (Bourdieu, 1993, p160).

However, the power conversion theory is too simple (Szelenyi and Kostello, 1996, p1093). With the conceptual apparatus of Bourdieu, one may interpret the theory as meaning that there are few or no limits to the conversion of cadre status into economic gains (Szelenyi and Szelenyi, 1995, p616). It pays much attention to those entrepreneurs with a cadre background or close connections with cadres but neglects how the entrepreneurs without such a background or connections survive and develop their businesses. Such a theory ignores the creation of social capital and the constraints of social capital. Besides being a cadre and coming from a cadre family, people can have other ways to possess and produce social capital.

It is argued that *guanxi* is a Chinese version of social capital. *Guanxi* are personal relations that can be resorted to for certain ends based on the norm of reciprocity. Like social capital in the West, *guanxi* has an instrumental function, and can be used for personal ends.

Chapters 4 and 5 examine the two concepts of *guanxi* and social capital and the relationship between them. It is argued that the two concepts overlap with each other. There are three main versions of social capital theory, represented by Bourdieu, Coleman and Putnam respectively. *Guanxi* and the concept of social capital in the three

main streams have common ingredients. Nevertheless, there are some differences between the two terms. *Guanxi* is closest to Bourdieu's (1986, 1993) notion of social capital, which is mainly looked at from the relational dimension of social capital.

It is further argued that there are several main weaknesses in the available research on both *guanxi* and social capital. In researching China, researchers mostly look at *guanxi* with government and government officials. Although governments play a critical role in the transition, focusing almost solely on changes in the government organizational hierarchy and on the fate of the cadre elite, such research overlooks the pursuit of power and plenty through *guanxi* by other economic actors in societies. Research on transitional economies needs to move beyond the limits of state-cadre centred analysis (Nee, 1996, p947).

Secondly, the available research implies that *guanxi* and social capital always have positive outcomes and treats social capital and *guanxi* as simultaneously a cause and an effect. However, social capital is not always instrumental for individuals; it may become a constraint to individuals' actions and choices.

Thirdly, the existing research on social capital, like the power conversion theory, mainly analyses existing social capital and positive outcomes but ignores how social capital comes into being. As Bourdieu (1986) argues, social capital is not necessarily naturally given; instead, it can be the product of investment by individuals who consciously or unconsciously aim at establishing or reproducing such social relations. Nevertheless, Bourdieu has never applied his theory in empirical research. It is believed that research on *guanxi* can contribute to social capital theory in terms of how social capital is

brought into being.

9.1.4 The role of *guanxi* in private business start-ups in the IT sector

Aiming at finding out how the Chinese private entrepreneurs start up their businesses, this thesis shifts to the in-depth qualitative research in the form of case studies in three chapters, Chapter 6, Chapter 7 and Chapter 8. The case studies concentrate on what types of *guanxi* the entrepreneurs of the private IT companies in Beijing Hi-tech Park resort to and how they utilize different types of *guanxi* for their business start-ups. The most recent field study in the private IT sector presents much richer multi-dimensional concepts for both *guanxi* and social capital.

As an initial attempt to focus on business start up in the Chinese private sector, this research finds that *guanxi* plays an important role. The importance of *guanxi* is examined in terms of its role in the two most critical aspects of business start-ups: financing and getting customers. It is found that there are several channels of business start-up financing in the private IT companies: personal savings, borrowing from friends or relatives, and investment from others. Without formal channels of finance available to the private entrepreneurs, they have to resort to *guanxi* for start-up finance. *Guanxi* resorted to for their start-up include relatives, friends and those introduced by known people, etc.

In the other critical aspect of business start-up, finding customers, the majority of the firms, relied on *guanxi* to sell their products at start-up. They either relied on known people to become customers or resorted to intermediaries to access customers. Both

known people and the intermediaries are *guanxi*.

9.1.5 Production and creation of social capital

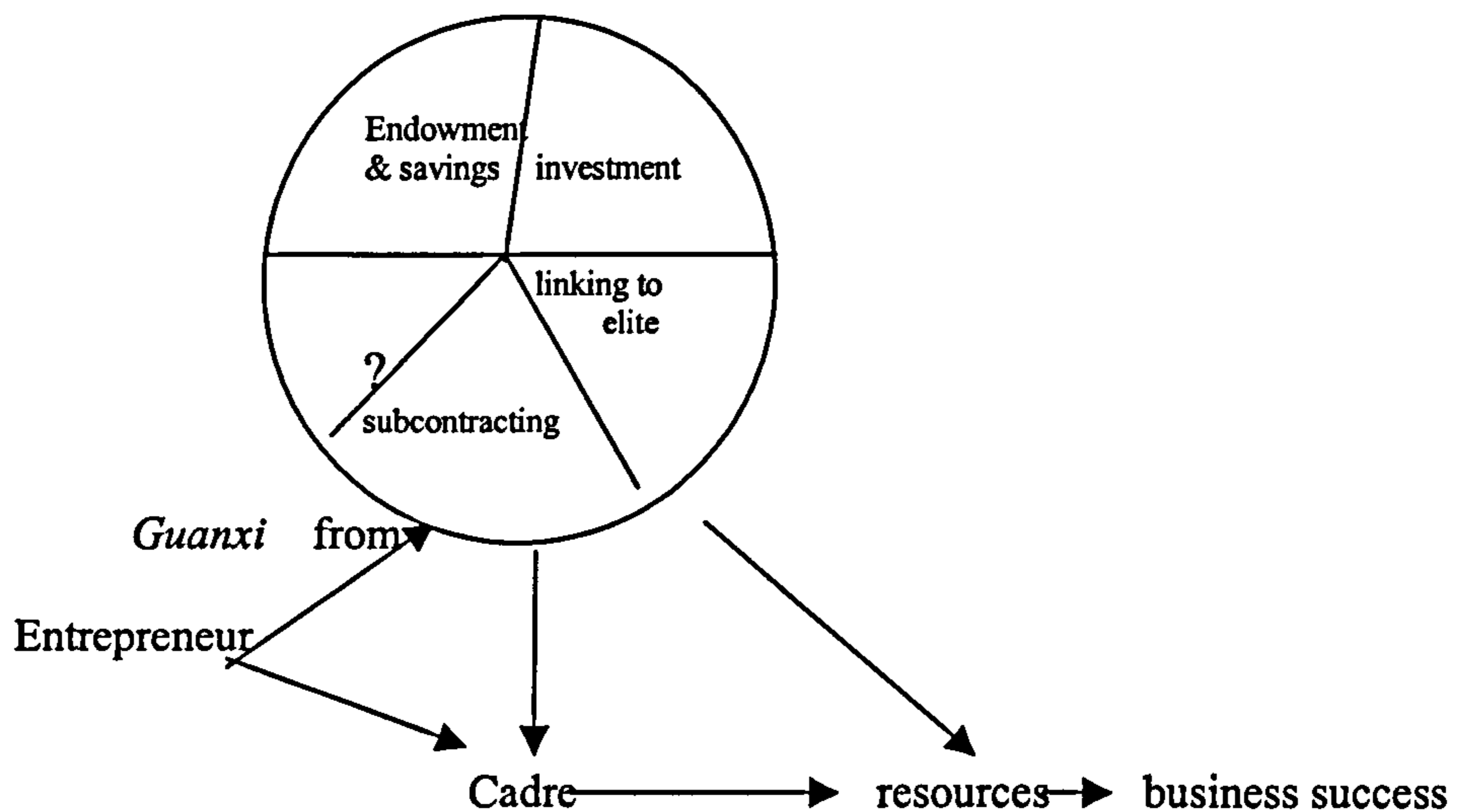
There are different types of *guanxi*, which include classmates, fellow townsmen, relatives, colleagues, former customers, friends' friends, and so on and so forth. There are several ways for different types of *guanxi* to come into being. Some types of *guanxi* come from endowment by virtue of birth into a family or a particular economic class or bureaucratic rank. Some types of *guanxi* are acquired through life experiences that predate the entrepreneurial career in childhood, education, work and political experiences. It is worth pointing out that political experience is simply one of the experiences that can lead to the acquirement of social capital. It is true, as Rona-Tas (1994) argues, cadres obtained a wide network of connections through party organisations. A cadre family background provides an entrepreneur with endowment connections. But this does not mean that being a cadre is the only chance for connection savings. Being a cadre and coming from a cadre family, which, the power conversion theory believes, provide entrepreneurs with social capital advantage are only two of the channels that produce social capital.

Chapter 6 and Chapter 8 have suggested that people have several other strategies to produce social capital when they themselves lack advantageous social relations. *Guanxi* can come from establishment and investment. Something in common between two individuals can be the basis for building up *guanxi*. The common bases for the establishment of *guanxi* include alumni, fellow townsmen, and the introduction of a common intermediary. Also, joining certain associations can lead to knowing people

and building *guanxi* (Odgaard, 1992). However, there is no well-defined extent and type of experience that constitutes an adequate basis. Common experience becomes a nominal category. Thus, Wank (1999, p174-175) argues that Chinese social networks have great institutional flexibility in extending claims based on family solidarity to persons outside the immediate family and authority because they are objects of veneration. Based on these preconditions, people interact with each other sufficiently in a particular quality (Falk and Kilpatrick, 2000) and invest in each other to building social capital in order to gain future access to different resources. Also, as was shown in Chapter 8, the tactic of subcontracting can solve the problem of one's own lack of *guanxi* by transforming it into 'someone else's problem' (Colling, 1995). In addition, entrepreneurs like to link themselves with the elite. Pictures taken with the elite and signature collections of the elite, in particular, of important government officials, establish symbolic *guanxi* with the elite, which function as endorsements of talismanic import.

Thus, the simple model of business success, according to the logic of power conversion theory (Figure 1.1), should be modified as in Figure 9.1. Entrepreneurs, in particular, those that have been cadres, can access resources via the cadre connections as Figure 1.1 suggested. Alternatively, they can resort to different types of *guanxi* for resources needed for business operation. The *guanxi* network of an entrepreneur can directly help access resources, which are not necessarily in the hands of cadres. The network may include cadres who have control over resources. Cadres who control these resources may not be members of the network itself, but the network can also bridge the entrepreneur over to them, if needed.

Figure 9.1 A more complex model for entrepreneurs to success



As the available research suggests, *guanxi* from endowment and savings can provide entrepreneurs with social capital and access to resources. However, *guanxi* can come from other strategies, such as investment, subcontracting, and linking to the elite. Moreover, there can be others (represented by the ? box in Figure 9.1), which have not been found in this limited research and thus are worth future research.

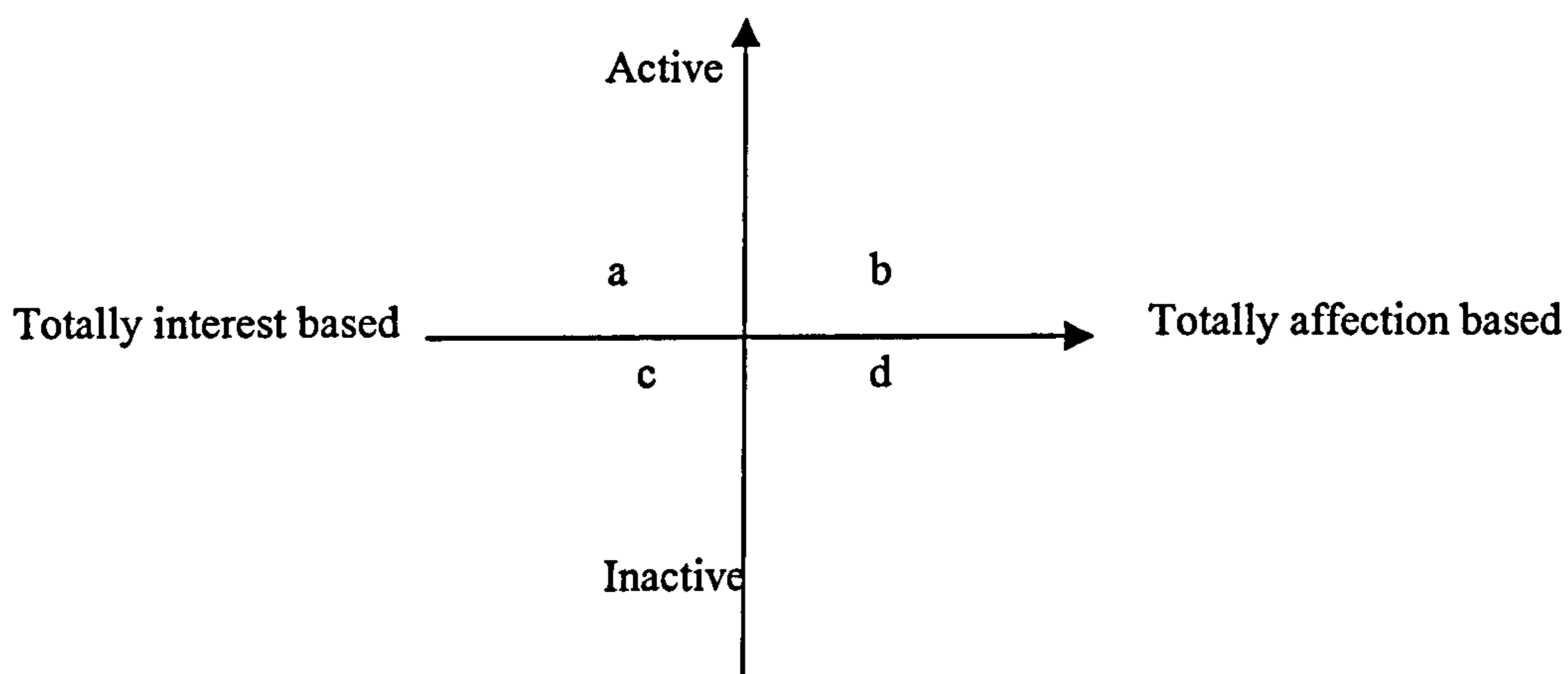
9.1.6 Two-dimensional *guanxi*

Granovetter (1973, 1974) and many other researchers have studied the “strength” of strong and weak ties. However, these two types cannot encompass the strengths of different types of *guanxi*. Some types of *guanxi* are neither weak nor strong ties.

It is not easy to measure the strength of *guanxi*. Burt (1997b) finds managers, like people in the general population, do not distinguish relations on a single dimension of strong versus weak. They distinguish on orthogonal dimensions of intimacy and

activity. There exist many types of ties, for example, emotional closeness, frequency, and time of knowing each other, support, discussion, and influence. The combination of the two dimensions, the strength, and the use of *guanxi* (activity), provides us with a good perspective to understand *guanxi* in business as shown in Figure 9.2.

Figure 9.2 The continuum of *guanxi* and the use of *guanxi*



In economic decisions, it is assumed that there are two extreme types of relationship between two individuals. One is totally interest based, while the other is totally affection based. The former is in line with rational choice in economics. The latter can be found typically in family relationship, where a father never considers the price of what he offers to his son. Totally interest based relationships, which are purely instrumental, and also usually short and unstable, are not *guanxi*. *Guanxi* mostly lies beyond the end of totally interest based relationship in the continuum of the two ends, with both interest and affective elements. Mixed ties are another term for most types of *guanxi*, which are likely relationships between people who know each other and expect to interact with each other on a long-term basis. Moreover, in such ties, people seek to influence others by *renqing* (Hwang, 1987).

Similarly, in the use of *guanxi* by an individual, there is a continuum between active and inactive. The interaction between the strength of *guanxi* and the activity of *guanxi* is demonstrated in Figure 9.2. Some types of *guanxi* are in box a. They may not be strong ties, but they are active in providing social capital. Some types of *guanxi* can be strong ties and also provide social capital actively, which are likely located in box b. Both box c and box d include *guanxi*, either weak ties or strong ties, which are not activated by an individual for personal ends. However, the individual may make such ties active when needed.

The strength of *guanxi* can be developed. Also, inactive *guanxi* can be made active. Furthermore, *guanxi* ties in the four boxes are not static. They can be developed into each other. For instance, a weak tie in box a can be developed into box b as a strong tie with the function of active investment as suggested in Chapter 8. Similarly, an active strong tie in box b may become an inactive strong tie in box d, because, for example, two good friends have lost contact for years. The convertibility of different types of *guanxi* depends on an individual's subjective dynamics. The convertibility of different types of *guanxi* and the effort of an individual are the dynamics of social capital.

9.1.7 *Guanxi xue*

An individual's access to social resources is instrumentally important (Lin et al., 1981; Lin, 1982). But if we conclude that *guanxi* is nothing but manipulative tactics used to gain profits and other desired goals, we fail to understand *guanxi*. Immediate instrumental purpose is subordinated to the greater aim of developing relationships that may serve as resources for future use over long periods of time (Smart, 1993). This is

the art of *guanxi*, or *guanxi xue*.

The Chinese use *guanxi xue* to express their concern with the tactics of *guanxi* construction and cultivation, which best ensure personal relationship building, utilization and development (Yang, 1994). *Guanxi xue* implies skill, subtlety, and cunning, as conveyed by the English word “artfulness”. It places an emphasis on the binding of power and emotional and ethical qualities of personal relationships (Luo, 2000). Nowadays, no one will say, “Mr X is my *guanxi*”. Instead, Mr X will be introduced to others as saying “Mr X is my friend”. This is perhaps partially because the government condemns *guanxi* practice and partially because *guanxi* has an instrumental denotation, while the term friend sounds to have an emotional element in the relationship.

Besides the emotional element, there are some basic rules in *guanxi xue*. Firstly, *guanxi* is mostly a long-term relationship. Secondly, frequent contacts with each other foster understanding and emotional bonds. Thirdly, it starts with and builds on the trustworthiness of the parties in *guanxi* ties. Fourthly but not lastly, the principle of *renqing* that underlies most *guanxi* ties suggests that favoritism is often followed by a strong expectation of reciprocity. Based on the norm of reciprocity, the repeated exchange of gifts and favours creates not only obligation but also a critical social capital of trust.

Moreover, it is argued that trust is an important element in *guanxi* relations. As a form of social capital, trust is not only the credibility and good intent of the parties involved but also is often considered as the ability to be relied on. Because *guanxi* is mostly

based on known people and networked people, their reliability, morals, and capability are known. Social networks function as a lens or prism through which the qualities of actors are inferred by potential exchange partners (Podolny, 2001).

9.1.8 Multi-dimensional *guanxi* and social capital

Guanxi is multi-dimensional, and so social capital. The richness of the concepts of *guanxi* and social capital were explored in the case study chapters, in particular Chapter 6, the self-reflective autobiographic account of field research methodology. The chapter described how the researcher utilised a *guanxi* approach to “roll the snowball” in conducting field research. It also analysed the relationship between the researcher and those who were supposed to help and those who helped roll the snowball.

This first hand experience suggests that social capital is not always instrumental for individuals; rather, it may become a constraint to individuals’ actions and choices (Portes and Sensenbrenner, 1993). For example, the embedded *guanxi* network of the researcher had in fact confined his vision in designing possible paths to access interviewees and indeed hindered the progress of field research at the beginning. Thus, it is not true that people seem to act with benefits from *guanxi* and social capital but without any constraints, as most available research on *guanxi* and social capital would lead us to believe. Social capital can also have negative outcomes. Realising this aspect of *guanxi*, Mr Mark Fagan, the CFO, investor liaison and chief media trouble-shooter of Sina.com, the largest Chinese portal, was quoted as saying, “It is far more risky today in allying yourself politically with someone in the government, than just pursuing the private-enterprise profit motive” (CNN, January 19, 1999). Negative consequences of

social capital in the same process also deserve attention for a balanced picture of the forces at play (Portes, 1998).

Furthermore, it is suggested that *guanxi* is contextual and contingent. For example, the change of the researcher's social status has impact on the social capital of his *guanxi* network. Thus, understanding the significance of social capital requires attention to networks in specific situations. Burt (1997) points out that in some settings, the social capital value of a network is a function of both form and content. Similarly, Rose (1998) argues that social capital is contingent and situational. For example, networks used to maintain health produce different outputs than networks that produce food or house repairs (Rose, 1998:19).

9.1.9 Power conversion theory in retrospect

When we look at the power conversion theory in retrospect, we are clear that cadre background and close connections with cadres are in fact only two of the channels that produce social capital. Besides the social capital from endowment from a cadre family and from savings during one's political experience, there are other alternatives, such as investment and subcontracting, which provide people with social capital and access to resources. There is evidence that the entrepreneurs with government experience have greater access to public financial source, which partially supports the power conversion theory. However, this is not the simple conversion of public assets as some research suggests. The clearly defined ownership of investment might have, to some extent, prevented the private entrepreneurs who received public finance from converting the money into personal property.

Although the entrepreneurs without government experience seem to have disadvantages in this aspect, they receive finance from private channels, as an alternative. The different channels may partially be due to the different embedded structures (Granovetter, 1985) of the entrepreneurs, where the entrepreneurs with government experience are more likely to have contacts with state owned firms, and thus their seeking of financial capital is confined in the state sector, while the entrepreneurs without government experience tend to sort their problem out outside government in their private domain. All Chinese live in a web of social relations. Families, kinship networks, neighbours, alumni, colleagues, and friendship circles are the communities in which they grow and on which they depend. Therefore, there is a need to look at connections more broadly, other than being confined to the examination of the closest connections with cadres.

Entrepreneurs born in cadre families and having been cadres may have an advantage in business, but transferring social capital into economic capital is a complex process. Social capital does not equate to an intended outcome. Thus Wank (1999, p87) notes that having bureaucratic connections does not in itself guarantee profitability. Entrepreneurs without such social capital can overcome this problem by creating social capital. Meanwhile, social capital of both cadre entrepreneurs and non-cadre entrepreneurs is contingent upon contexts and contents. For example, the researcher's own experience has showed that his social capital with government officials did not help much in his fieldwork. Instead, it constrained his action at the very beginning. In this sense, there is not an absolute advantage that cadre entrepreneurs can take. On the other hand, entrepreneurs without cadre experience are not necessarily in a disadvantageous position. Social capital, which bridges the two competing theories of

the circulation of elites and power conversion, is the area and process that both of them must consider.

9.2 Areas for further research

The findings of this thesis have also opened up some areas for further investigation, which are beyond this limited thesis. These include firstly, areas around the question if cadre related entrepreneurs have an advantage and secondly, further research on social capital. The first one contains some interrelated questions. Why cadre related entrepreneurs have not been found to have an advantage in business start-up? What is a best indicator for the measurement of such an advantage? Will cadre related entrepreneurs have an advantage after the implementation of China's privatisation policy? The second one includes other possibilities of producing social capital and comparative research on social capital in other cultures.

9.2.1 From cadre related entrepreneurs advantages to cadre advantages

The 1995 survey on private enterprises analysed in this thesis could not include private firms run by cadre related entrepreneurs but under the guise of state owned or collectively owned firms. The data was collected before the Chinese Communist Party introduced a top-down privatisation policy in 1997 (*Financial Times*, December 8, 1997). These limitations of the data may have restricted the ability to find the advantages that cadre related entrepreneurs can take.

Some research has suggested that entrepreneurs who have close connections with

government have benefited from this later top-down privatization. For example, Li (2000) finds that being a standing member of People's Congress in Hanchuan City provided the private entrepreneur Mr. Liu Xingkun with benefits in business. Being in the prominent political position, he bought a bankrupt state owned plastic factory at half of its real value of about RMB 10 million. This cheap take-over facilitated quick expansion of his businesses, and enhanced his business reputation. Li (2000) thus assumes that private entrepreneurs can expand their resource mobilizing ability if they take part in political activities, such as being a head of a village, a member of People's Congress or Political Consultative Committee. It is worth pointing out that this entrepreneur was a peasant and his success in business led him to be selected as a member of the county's People's Congress, which provides him with social capital. This is not a simple one-way of transferring social capital into economic capital; rather, economic capital and social capital are mutually convertible. The president of Feilong Group, one of the most influential pharmaceutical companies, remarked on the relationship between private enterprises and the government, "Every enterprise hopes to build up a connection with the government" (cited in Wong and Sun, 2000:123). This indicates another aspect of the complexity of social capital.

Also, the finding that there is no significant advantage for cadre related entrepreneurs is limited to business start-up. Many ways are open for entrepreneurs to achieve primary accumulations of capital during the transition, as suggested in Chapter 2. These include those who had their primary capital accumulations from illegal activities. For example, Lai Changxing, the mastermind of the biggest smuggling scandal in China, made a fortune from smuggling (*Xinhua News Agency*, September 5, 2001). Later, entrepreneurs started to invest their money in legal activities. During the process, the

illegal history of primary accumulations was covered up. A fashionable slogan in the private sector is: Do not ask the origin of the hero(ic) entrepreneur (Zhu *et al.*, 1999). This can contribute to the similar possibilities for both cadre related entrepreneurs and non-cadre related entrepreneurs to have the highest start-up capital found in Chapter 2.

There are several ways for cadres to gain during the transition. One is to go for private businesses, but this involves risk. Others can outperform them in business operation (Nee, 1989, 1991). Two other channels have no risk, at least, not business risk. Cadres' ability to gain control over lucrative assets could vary by the characteristics of assets and enterprises. It is possible that they can convert public assets into private, or get more out of their effort because of their power and connections (Walder, 1996, p1063). A second choice is to remain in the office and support family members to operate business, as Staniszkis (1991) writes that the power in industry and the state administration is linked with activities on one's own account in a private company. This is also the choice for the "princelings" – relatives of high-ranking officials or party members in China (Tao and Ho, 1997; Wank, 1999). A third alternative is concealed: power for money, such as kickbacks and bribery. They can even have shares in a private company, which are so-called "power shares" (Wank, 1999, p101). Cadres can get rich together with private entrepreneurs, shoulder to shoulder, without giving up their government positions.

Yu (1998) argues that an upstart rich group is emerging in China's transition. Unlike the ordinary rich people, such as honest private entrepreneurs, who get rich by their hard work leading to capital accumulation, the upstarts reap staggering profits from scratch.

Their wealth comes from illegal activities, such as smuggling. Corrupt government officials hide themselves in this group. Their activities are concealed and thus it is very difficult to investigate the number and wealth of this group. A reporter from the state-run Central Television said he shelved a documentary project about the rich in China because few wanted to be interviewed and most of them made their first million by breaking the law (*Washington Post*, March 17, 2002). To investigate such a population and their activities is most challenging to social scientists. Though difficult, such research is desirable.

9.2.2 Creation of social capital from other perspectives

This thesis is simply a starting point for understanding the role of social capital in business and the dynamics of social capital. As argued previously, there are other possibilities that produce social capital, which are beyond this research. For instance, Tsui and Farh (1997, p58-59) find that an individual may be favourably inclined toward people who are demographically similar, even though these people are otherwise strangers at an interpersonal level. Demographic similarities or differences affect interpersonal relationships and individual reactions through the process of categorisation and identification. Relational demography provides people with a basis and potential to create social capital. There may be other social, cultural, economic and psychological factors that may influence over social capital. Further conceptual and empirical research is desired.

9.2.3 Research on *guanxi* and social capital can contribute more

No one could dispute that social capital is multifaceted (Sobel, 2002, p144), as this research has demonstrated. However, a single research cannot capture the many faces of social capital. Comparative research can contribute greatly to social capital and its role in business.

Similar phenomena to *guanxi* in business exist in many developing countries. They have local names such as *pratik* in Haiti, *suki* in the Philippines, *onibara* in Nigeria, *casera* in Peru, *sedaqa* in Morocco, and *blat* in Russia (Granovetter, 1993; Rose, 1997 and 1998; Lyon, 2000). In the West, people say that it is not what you know but whom you know that counts. In the labour market, personal ties play an important role in finding desired jobs (e.g., Lin et al., 1981; Sander and Nee, 1996). In the United States, almost every university careers services gives advice on how to use personal networks to find a job. Universities in the UK have started to follow suit. Even in Silicon Valley, the start-up financing of many IT giants was based on informal social networks (Cringley, 1996). In recent years, growing interest has been developed in the concept of relationship marketing among both academic and practitioners, where the notion of relationship is similar to *guanxi* (Riley and Chernatony, 2000; So, 2000).

According to North (1981), institutions are a set of rules, compliance procedures, and moral and ethical behavioural norms designed to constrain the behaviour of individuals in the interests of maximizing wealth. There are two sorts of institutions: (1) formal institutions based on universalistic rules and procedures; and (2) informal rules and particularistic social relationships based on shared identity such as family, kinship, and social network. Informal institutions such as norms of social relations help to create and maintain a stable situation where trust can be built and transaction costs reduced.

Informal institutional arrangements can supplement or substitute for legal structures in ways that reduce uncertainties and costs in economic transactions (Kollock, 1994), as many transactions are so complex that law cannot possibly cover all contingent circumstances (Moore, 1994). Thus even in well-institutionalised countries, informal arrangement based on social relations can play a role.

Granovetter (1992:273) argues that economic institutions do not emerge automatically in response to economic needs. Rather, they are constructed by individuals whose action is both facilitated and constrained by the structure and resources available in social networks in which they are embedded. The social relations, which affect economic action, are always present (Granovetter, 1985). Thus, some modern economists attempt to take account of social influences in economic action and decision (e.g., Richardson, 1972; Williamson, 1985).

What are the similarities and differences in the phenomena across countries? Dodd and Patra (2002) have taken an early effort. Their comparison between Greek entrepreneurs and that of other countries, Canada, Japan, Italy, Northern Ireland, Sweden, the UK and the USA, suggests that not all national entrepreneurs network in the same way and that generic behaviour across borders cannot be assumed. What are the factors contributing to the differences? What are the similarities and differences between the developed and the developing? Research on these questions can not only contribute to the richness of social capital but also to business operation in practice and to theories of institutional economics.

9.3 Implications of this research

This thesis has at least two implications for research. Firstly, *guanxi* is still important in many aspects of business. Accordingly and secondly, the Chinese system of business seems to be developing toward network capitalism.

9.3.1 *Guanxi* in the era of “new economy”

According to some researchers (e.g., Walder, 1986; Solinger, 1989), in the Chinese planned economy era, the centralised distribution gave officials a monopoly on the allocation of goods and services. Citizens had to cultivate *guanxi* with officials to obtain these scarce resources. In the state owned enterprise sector, the use of *guanxi* by the managers could help get supplies in shortage and keep production continuous (Child, 1996); The removal of government bureaucratic regulations on access to raw materials left state owned enterprises solely reliant on *guanxi* networks to ensure that supplies of raw materials arrived in a dependable manner (Whitcomb and Li, 1996). However, some researchers maintain that the development of market activities has led to the declining utility of *guanxi* in Chinese business. They insist that markets give citizens access to resources that lie outside the purview of officialdom, that exchange relations in the market economy increasingly depend on the quality of goods and services rather than *guanxi*, and thus the market economy institutionalises new norms of legality that replace particularistic and reciprocal *guanxi* (e.g., Guthrie, 1998).

Being the symbol of Chinese high technology, Zhongguancun High-tech Park undertakes the task to absorb and deliver global advanced technology, to foster emerging industries, and to play a demonstration role to other domestic Science Parks (Wang, 2000). As suggested in Chapter 6, IT industry is dominant in Zhongguancun

Park. To a large extent, the IT sector in Zhongguancun represents the development of “new economy” in China with several characteristics. Firstly, the IT is a newly developing sector, as found in Chapter 6, most companies were set up in the 1990s and 2000s. Secondly, the sector is most market oriented. They are developed under the law of market with little government interference. Thirdly, the government does not provide them with any financial support (e.g., The Great Wall Institute of Enterprise Strategy, 1996). The facts from this most advanced segment still suggest the importance of *guanxi* networks, for example, in financing business start-up and finding customers.

New economy is not only a term of fashion but also a myth to many. The crux of the new economy is the idea that the development of information technology creates high productivity growth without unemployment and inflation. Krugman (1998) comments that new economy is nothing new, but simply technological changes in the United States.

The first hand field research has also indicated that the so-called new economy is not new at all in term of ways to finance start up and find customers. Even more ironically, Internet companies, E-businesses, have to rely on *guanxi* to find customers. Taking the important role of *guanxi* in the start-ups of the Chinese private IT companies into consideration, the IT sector, whose technology is the basis of the new economy, is also built on conventional paths. The networks that are crucial to the start-ups are not the networks of information technology but of *guanxi*. Similarly, Hong Kong based portal tom.com, listing to thunderous applause and a quadrupling of its share price on its first day of trading in March 2000, lay claim not to content but to its connection with Hong Kong’s premiere tycoon, Li Ka-shing (Kalathil, 2000). The Internet, the virtual world, is

embedded in social and institutional forces that exist in the “real world” (Drake *et al.*, 2000).

9.3.2 The Chinese tradition of networking

The roots of networking as an institutionalized practice are ancient and extensively developed in China (Boisot and Child, 1996). Hwang (1987) believes that the instrumental use of *guanxi* persisted in Chinese society because of cultural and structural factors. It is true. Particularly, the connection between bureaucracy and business has long existed in Chinese history. This is probably because of the superior status of bureaucracy in the Chinese society, where bureaucracy has dominated and is deemed as formal hierarchy (Brunn, 1993). Understandably, at the turn of the 21st century, a majority of the successful overseas Chinese entrepreneurs attempted to disguise bourgeois wealth with the prestige of purchased degrees, titles and brevet posts (Godley, 1981). Brunn (1993) comments that modernization and development in China seem to have taken place alongside a strong continuity in fundamental ideologies, values and orientations among the social groups within the locality, all of whom seek to establish and utilize connections to the bureaucracy. Wank (1999) looks at the patron-client ties between private entrepreneurs and officialdom as “commodifying communism”. But indeed, the connection between bureaucracy and business is not the legacy of communism alone (Huang, 2001). Godley (1981) points out further that, generally, Chinese business tended to be carried out under the protective cover of lineage government or religious community, and was connected to patronage networks provided by government officials. Redding (1990) and Zheng (1997) also find that overseas Chinese in Southeast Asia have carefully built networks into the government

and military power bases for their business.

9.3.3 *Guanxi* as a competitive advantage for overseas Chinese

According to Boisot and Child (1996), research on Sino-foreign joint ventures suggests that overseas Chinese investors are more likely to establish business relationships through friendship ties or other informal contacts than are Western investors. Increasingly, multinationals are recognising the advantages of *guanxi* available to Hong Kong entrepreneurs and are using them as middlemen, brokers, and subcontractors as a more efficient way of entering the Chinese market (Pomfret, 1991).

Nearly 85 per cent of cumulative foreign direct investment in China from 1979 to 1993 has come from sources in Hong Kong, Taiwan, Macao, Singapore and Thailand, with the proportions attributable to this group, essentially made up of the ethnic Chinese diaspora, rising over the period (Christerson and Lever-Tracy, 1997). *Guanxi* networks have played a major role in facilitating FDI flows to China (Wang, 2000). Lee Kuan Yew, Singapore's elder statesman, identified *guanxi* as an important advantage that overseas Chinese can make use of as they compete against western rivals for business operation in China and claimed that *guanxi* capability would be of value for a least the next twenty years (*Far Eastern Economic Review*, December 2, 1993).

9.3.4 Functions of *guanxi*

Because of high institutional uncertainties in China, *guanxi* has economic legitimacy, which constitutes a substitute for institutional support for business. It reduces

operational uncertainties, including political uncertainty, and enhances economic returns (Luo, 2000; Tao and Ho, 1997). Similarly, Faure (1994) points out that *guanxi* networks build up trust. These networks of trust serve to reduce uncertainty and transaction cost.

With the progress of reform, a rational-legal system is being constructed (Guthrie, 1998). However, the role of *guanxi* will not disappear, as many transactions are so complex that law cannot possibly cover all contingent circumstances (Moore, 1994). Informal institutional arrangements cannot only substitute for but also supplement legal structures in ways that reduce uncertainties and costs in economic transactions (Kollock, 1994). For example, a survey in Shanghai finds that though individual economy operators (*getihu*) accepted formal law requirements about formation and enforcement, the effects of traditional norms of informality also remained in evidence. In response to questions about the formation of loan obligations, 50 per cent of *getihu* indicated that they would respond to the debtor's refusal to pay by seeking a mutual friend to remind the debtor to perform. While the vast majority, 71 per cent of *getihu* respondents, said they would repay a debt in order to protect their reputation, and only 14 per cent indicated that legal duty would be the reason for repayment. The elements of social capital that involve *guanxi* operate as a complement to formal law (Potter, 2000).

Also, *guanxi* establishes a link for the flow of information on resource supply and demand, reducing information cost, promoting business effectiveness; *Guanxi* can spur the development of new market channels and render protection against contextual hazards (Luo, 2000; Tao and Ho, 1997). Similarly, Granovetter (1974) emphasizes the importance of weak, bridging ties. Burt (1992, 1999) terms weak ties structural holes.

In conclusion, it is critical to make clear what role *guanxi* plays when we discuss its importance or unimportance. *Guanxi* is not needed any more to obtain daily needs as Walder (1986) finds. Neither is it important in the procurement of most raw materials. On the contrary, the instrument used to acquire goods in the shortages of the past is now utilized to sell goods in the competitive market. Also, *guanxi* becomes the path and instrument to re-organise resources, as suggested by the interviewed entrepreneurs. Furthermore, *guanxi* can supplement or substitute legal structures in ways that reduce uncertainties and costs in economic transactions. In similar vein, Podolny (2001) points out that beyond the benefit of conveying market stuff between two market actors, social networks also work as an information cue on which others rely to make inferences about the underlying quality of one or both of the market actors. Hence, it may be more appropriate to say *guanxi* plays a less important role in certain aspects with the process of marketisation and the development of the Chinese economy, but it is still active in other ways.

The Beijing enterprise managers believed that the quality of *guanxi* was more important than the price charged or any contractual conditions (Child, 1996). In Tianjin, according to a report (*Tianjin Daily*, June 2, 1999), managers spend 60 to 70 per cent of their time and energy on *guanxi* cultivation. In the similar vein, a survey on private entrepreneurs (Zhao, 1998) in Beijing, Shanghai and Guanzhou reveals that they list *guanxi* with customers as of the first importance in business. *Guanxi* with suppliers comes second, followed by *guanxi* with employees and shareholders. *Guanxi* with government is regarded as fifth important. These results represent the continuity and change of *guanxi*.

9.3.5 *Guanxi* and WTO

China is now a member of the WTO, which is mainly a legal mechanism to ensure a free and transparent market, and solve trade and investment disputes between members (*China Daily*, October 23, 2001). The impact of the entry on domestic industries will further drive China towards a market economy. More structural readjustments are needed if China is to adapt to the requirements of the WTO. Legal transparency, equal treatment and trade liberalization are all needed (*China Daily*, December 11, 2001).

Undoubtedly, China will have to speed up reforms in all economic fields and adapt itself to the world trade system. On the other hand, all the countries with an interest in the huge market will have to understand the Chinese business system, of which *guanxi* is an important element. China's economy is big in every way (*EIU*, April 24, 2002). The size of the Chinese economy is likely to climb, in world rankings, from its current position as the sixth largest to the second largest by 2030. Such an economy stands to offer exciting business and capital market opportunities to foreigners over the next 10 years or so, said economists with global investment bank Lehman Brothers (*China Daily*, February 5, 2002). The Chinese government can adjust its policies and liberalise the Chinese market, such as lowering the tariff level, canceling import quotas and non-tariff barriers, and allowing foreign companies into the state monopoly sectors, e.g., telecommunications, banking, insurance, securities and tourism. However, neither the WTO nor the Chinese government can totally change the business practices embedded in the informal institution. As *guanxi* is a culturally embedded feature of economic and political life in China (Child, 1996) and economic action is characterised by four kinds of "embeddedness"----cognitive, cultural, social, and political (Zukin and DiMaggio, 1990, p5). It is impossible for the WTO or the Chinese government to change all the four aspects of embeddedness in a short term.

9.3.6 A path-dependent transition

At first it appeared as if the fall of Communism brought with it the end of history and that all societies were converging around models of liberal capitalism (e.g., Fukuyama, 1992). Burawoy (1992) has pointed out that there is no guarantee that Eastern Europe or the post communist states are sailing smoothly toward modern capitalism. Stark (1992) criticizes the assumption that post-socialist societies are progressing towards a well-defined end, some clear, or ideal, type of market capitalism teleological. Some transition theory measures the degree of success of transition by contrasting concrete East European or Chinese economies with pure models of market capitalism, as if it were possible to build capitalism by design. In fact, socioeconomic change under post-socialism should be understood as a path-dependent transformation, which is a process of readjusting existing institutions to the changing socioeconomic environment.

The role of *guanxi* in business is likely to have strong path-dependent effects in the process (Stark, 1992). For example, *guanxi* networks have become an important channel for firms in China to enter the international markets. Based on the data of several sources, Christerson and Lever-Tracy (1997) find that China's manufacturing firms are typically linked to global markets through Hong Kong and Taiwanese trading companies and buying agents. These firms take orders from multinationals and then coordinate production to a group of contractors in China. This arrangement is often based on *guanxi*, such as ethnic and kinship ties.

Furthermore, in the globalisation of economic activities, the ethnic Chinese firms in Southeast Asia gain competitive advantage from the formation of this

culturally-embedded *guanxi* networks (Yeung, 1999). These personal and business networks add scope and depth to the family firms. By being part of such *guanxi* networks, family firms are tied to other family firms. Therefore, by combining, they reach beyond the limitation imposed by their size, both geographically and economically (Hamilton, 1996).

9.3.7 A network capitalism

Boisot and Child (1996) argue that a new capitalist system with Chinese characteristics—network capitalism is emerging. Within a frame of information codification and diffusion, Boisot and Child (1996) identify the nature of the system of industrial governance and transaction in China's economic development. They argue that the emergent features of China's economic order, namely, the business system, the nature of market arrangements, the form of capitalism, and the role of government in the system, suggest that China's institutional form is network capitalism.

Modern capitalist economies should not be reduced to only one of their constitutive parts: markets are but one of a multiplicity of coexisting coordinating mechanisms in modern capitalism (Stark, 1992). Market orientation should be distinguished from market coordination. A broad variety of institutions of non-market coordination are compatible with high performance market orientation (Stark, 1996). Various researches indicate that there are sectors where the most competitive forms of economic coordination are neither market nor statist but new forms that are labeled as networks, alliance and interfirm agreements. We have only begun to understand and identify them (Stark, 1992). The evidence presented in this thesis points to the new form of economic

systems.

For decades, capitalism was defined vis-à-vis socialism and vice versa. Capitalisms must be defined and compared vis-à-vis each other (Stark, 1996). The spirit of Chinese capitalism rests with the ability of Chinese to network together to form a relatively coherent socio-economic group to survive discrimination in the host Southeast Asian countries (Redding, 1990). Ross (1999) suggests that the market model for China is communitarian capitalism. The Chinese government claims that it is building a socialist market economy. Despite this dispute, a network business system is evident in China, which may remain as an important mechanism for the economy and society in the foreseeable future. Furthermore, best-selling prognosticator Naisbitt (1997) predicts that a collaborative network of Chinese entrepreneurs, from China and overseas will increasingly gain economic power and outperform the West and even Japan. Time, and future research will tell whether this observation still holds true in the coming years.

Appendix A: Statistical Analysis

Table A1.1 start-up registered capital * respond power Crosstabulation

			respond power		Total
			non-cadre	cadre	
start-up registered capital	<=150000	Count	860	480	1340
		% within respond power	58.2%	47.4%	52.7%
	150001-500000	Count	402	288	690
		% within respond power	26.3%	28.4%	27.1%
	500001-1180000	Count	142	120	262
		% within respond power	9.3%	11.8%	10.3%
	>1180000	Count	127	125	252
		% within respond power	8.3%	12.3%	9.9%
Total		Count	1531	1013	2544
		% within respond power	100.0%	100.0%	100.0%

Table A1.2 registered capital * respond power
Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	23.980 ^a	3	.000
Likelihood Ratio	23.826	3	.000
Linear-by-Linear Association	23.639	1	.000
N of Valid Cases	2544		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 100.34.

Table A1.3 Directional Measures for start-up registered capital * respond power

			Value	Asymp. Std. Error ^a	Approx. T	Approx. Sig.
Nominal by Nominal	Lambda	Symmetric	.000	.000	. ^b	. ^b
		start-up registered capital Dependent	.000	.000	. ^b	. ^b
		respond power Dependent	.000	.000	. ^b	. ^b
	Goodman and Kruskal tau	start-up registered capital Dependent	.004	.002		.000 ^c
		respond power Dependent	.009	.004		.000 ^c

a. Not assuming the null hypothesis.

b. Cannot be computed because the asymptotic standard error equals zero.

c. Based on chi-square approximation

Table A1.4 Symmetric Measures for registered capital * respond power

		Value	Approx. Sig.
Nominal by Nominal	Phi	.097	.000
	Cramer's V	.097	.000
	Contingency Coefficient	.097	.000
N of Valid Cases		2544	

a. Not assuming the null hypothesis.

b. Using the asymptotic standard error assuming the null hypothesis.

Table A2.1 start-up real assets * respond power Crosstabulation

			respond power		Total
			non-cadre	cadre	
start-up real assets	<=200000	Count	805	461	1266
		% within respond power	55.9%	48.8%	53.1%
	200001-600000	Count	322	236	558
		% within respond power	22.4%	25.0%	23.4%
	600001-2000000	Count	211	147	358
		% within respond power	14.7%	15.6%	15.0%
	>2000000	Count	102	100	202
		% within respond power	7.1%	10.6%	8.5%
Total		Count	1440	944	2384
		% within respond power	100.0%	100.0%	100.0%

Table A2.2 start-up real assets * respond power
Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	15.672 ^a	3	.001
Likelihood Ratio	15.536	3	.001
Linear-by-Linear Association	13.159	1	.000
N of Valid Cases	2384		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 79.99.

Table A2.3 Directional Measures for start-up real assets * respond power

		Value	Asymp. Std. Error ^a	Approx T	Approx Sig
Nominal by Nominal	Symmetric	.000	.000	.	.
	start-up real asse Dependent	.000	.000	.	.
	respond power Dependent	.000	.000	.	.
Goodman and Kruskal's tau	start-up real asse Dependent	.003	.001		.000 ^c
	respond power Dependent	.007	.003		.001 ^c

a. Not assuming the null hypothesis.

b. Cannot be computed because the asymptotic standard error equals zero.

c. Based on chi-square approximation

Table A2.4 Symmetric Measures for start-up real assets *
respond power

		Value	Approx. Sig
Nominal by Nominal	Phi	.081	.001
	Cramer's V	.081	.001
	Contingency Coefficient	.081	.001
N of Valid Cases		2384	

a. Not assuming the null hypothesis.

b. Using the asymptotic standard error assuming the null hypothesis.

Table A3.1 start-up registered capital * father power Crosstabulation

			father power		Total
			non-cadre	cadre	
start-up registered capital	<=150000	Count	878	349	1227
		% within father power	55.2%	46.3%	52.4%
	150001-500000	Count	401	235	636
		% within father power	25.2%	31.2%	27.1%
	500001-1180000	Count	160	79	239
		% within father power	10.1%	10.5%	10.2%
	>1180000	Count	151	90	241
		% within father power	9.5%	12.0%	10.3%
Total	Count	1590	753	2343	
	% within father power	100.0%	100.0%	100.0%	

Table A3.2 Chi-Square Tests for start-up registered capital * father power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	17.519 ^a	3	.001
Likelihood Ratio	17.451	3	.001
Linear-by-Linear Association	10.415	1	.001
N of Valid Cases	2343		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 76.81.

Table A3.3 Directional Measures for start-up registered capital * father power

			Value	Asymp. Std. Error ^a	Approx. T	Approx. Sig.
Nominal by Nominal	Lambda	Symmetric	.000	.000	.	.
		start-up registered capital Dependent	.000	.000	.	.
		father power Dependent	.000	.000	.	.
Goodman and Kruskal's	k	start-up registered capital Dependent	.004	.002		.000 ^c
		father power Dependent	.007	.004		.001 ^c

a. Not assuming the null hypothesis.

b. Cannot be computed because the asymptotic standard error equals zero.

c. Based on chi-square approximation

Table A3.4 Symmetric Measures for start-up registered capital * father power

			Value	Approx. Sig.
Nominal by Nominal	Phi		.086	.001
		Cramer's V	.086	.001
		Contingency Coefficient	.086	.001
N of Valid Cases			2343	

a. Not assuming the null hypothesis.

b. Using the asymptotic standard error assuming the null hypothesis.

Table A4.1 start-up real assets * father power Crosstabulation

			father power		Total
			non-cadre	cadre	
start-up real assets	<=200000	Count	830	334	1164
		% within father power	55.4%	47.9%	53.0%
	200001-600000	Count	329	180	509
		% within father power	22.0%	25.8%	23.2%
	600001-2000000	Count	215	117	332
		% within father power	14.4%	16.8%	15.1%
	>2000000	Count	124	66	190
		% within father power	8.3%	9.5%	8.7%
Total	Count	1498	697	2195	
	% within father power	100.0%	100.0%	100.0%	

Table A4.2 Chi-Square Tests for start-up real assets * father power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	10.732 ^a	3	.013
Likelihood Ratio	10.721	3	.013
Linear-by-Linear Association	7.305	1	.007
N of Valid Cases	2195		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 60.33.

Table A4.3 Directional Measures for start-up real assets * father power

		Value	Asymp. Std. Error ^a	Approx. T	Approx. Sig.
Nominal by Nominal	Symmetric	.000	.000	.	.
	start-up real assets Dependent	.000	.000	.	.
	father power Dependent	.000	.000	.	.
Goodman and Kruskal t	start-up real assets Dependent	.003	.002		.001 ^c
	father power Dependent	.005	.003		.013 ^c

a. Not assuming the null hypothesis.

b. Cannot be computed because the asymptotic standard error equals zero.

c. Based on chi-square approximation

Table A4.4 Symmetric Measures for start-up real assets * father power

		Value	Approx. Sig.
Nominal by Nominal	Phi	.070	.013
	Cramer's V	.070	.013
	Contingency Coefficient	.070	.013
N of Valid Cases		2195	

a. Not assuming the null hypothesis.

b. Using the asymptotic standard error assuming the null hypothesis.

Table A5.1 start-up registered capital * spouse power Crosstabulation

			spouse power		Total
			non-cadre	cadre	
start-up registered capital	<=150000	Count	911	370	1281
		% within spouse power	53.6%	52.6%	53.3%
	150001-500000	Count	470	177	647
		% within spouse power	27.7%	25.1%	26.9%
	500001-1180000	Count	166	79	245
		% within spouse power	9.8%	11.2%	10.2%
	>1180000	Count	152	78	230
		% within spouse power	8.9%	11.1%	9.6%
Total	Count	1699	704	2403	
	% within spouse power	100.0%	100.0%	100.0%	

Table A5.2 Chi-Square Tests for start-up registered capital * spouse power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	4.675 ^a	3	.197
Likelihood Ratio	4.606	3	.203
Linear-by-Linear Association	2.382	1	.123
N of Valid Cases	2403		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 67.38.

Table A6.1 start-up real assets * spouse power Crosstabulation

			spouse power		Total
			non-cadre	cadre	
start-up real assets	<=200000	Count	871	335	1206
		% within spouse power	54.2%	51.3%	53.4%
	200001-600000	Count	379	151	530
		% within spouse power	23.6%	23.1%	23.5%
	600001-2000000	Count	230	104	334
		% within spouse power	14.3%	15.9%	14.8%
	>2000000	Count	127	63	190
		% within spouse power	7.9%	9.6%	8.4%
Total	Count	1607	653	2260	
	% within spouse power	100.0%	100.0%	100.0%	

Table A6.2 Chi-Square Tests for start-up real assets * spouse power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3.273 ^a	3	.351
Likelihood Ratio	3.222	3	.359
Linear-by-Linear Association	3.063	1	.080
N of Valid Cases	2260		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 54.90.

Table A7.1 start-up registered capital * cloest relative power Crosstabulation

			cloest relative power		Total
			non-cadre	cadre	
start-up registered capital	<=150000	Count	562	648	1210
		% within cloest relative power	54.2%	52.7%	53.4%
	150001-500000	Count	276	346	622
		% within cloest relative power	26.6%	28.2%	27.5%
500001-1180000	Count	93	132	225	
	% within cloest relative power	9.0%	10.7%	9.9%	
>1180000	Count	105	103	208	
	% within cloest relative power	10.1%	8.4%	9.2%	
Total	Count	1036	1229	2265	
	% within cloest relative power	100.0%	100.0%	100.0%	

Table A7.2 Chi-Square Tests for start-up registered capital * cloest relative power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	4.356 ^a	3	.226
Likelihood Ratio	4.360	3	.225
Linear-by-Linear Association	.003	1	.956
N of Valid Cases	2265		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 95.14.

Table A8.1 start-up real assets * cloest relative power Crosstabulation

			cloest relative power		Total
			non-cadre	cadre	
start-up real assets	<=200000	Count	538	617	1155
		% within cloest relative power	54.8%	53.5%	54.1%
	200001-600000	Count	228	262	490
		% within cloest relative power	23.2%	22.7%	23.0%
600001-2000000	Count	132	188	320	
	% within cloest relative power	13.5%	16.3%	15.0%	
>2000000	Count	83	86	169	
	% within cloest relative power	8.5%	7.5%	7.9%	
Total	Count	981	1153	2134	
	% within cloest relative power	100.0%	100.0%	100.0%	

Table A8.2 Chi-Square Tests for start-up real assets * cloest relative power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3.777 ^a	3	.287
Likelihood Ratio	3.794	3	.285
Linear-by-Linear Association	.263	1	.608
N of Valid Cases	2134		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 77.69.

Table A9.1 start-up registered capital * closest friend power Crosstabulation

			closest friend power		Total
			non-cadre	cadre	
start-up registered capital	<=150000	Count	420	814	1234
		% within closest friend power	57.0%	51.1%	53.0%
	150001-500000	Count	203	434	637
		% within closest friend power	27.5%	27.3%	27.4%
500001-1180000	Count	57	182	239	
	% within closest friend power	7.7%	11.4%	10.3%	
>1180000	Count	57	162	219	
	% within closest friend power	7.7%	10.2%	9.4%	
Total	Count	737	1592	2329	
	% within closest friend power	100.0%	100.0%	100.0%	

Table A9.2 Chi-Square Tests for start-up registered capital * closest friend power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	13.185 ^a	3	.004
Likelihood Ratio	13.613	3	.003
Linear-by-Linear Association	11.035	1	.001
N of Valid Cases	2329		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 69.30.

Table A9.3 Directional Measures for start-up registered capital * closest friend power

		Value	Asymp. Std. Error ^b	Approx T	Approx Sig.
Nominal by Nominal	Lambda Symmetric	.000	.000	.	.
	start-up registered capital Dependent	.000	.000	.	.
	closest friend power Dependent	.000	.000	.	.
Goodman and Kruskal's	start-up registered capital Dependent	.002	.001		.005 ^c
	closest friend power Dependent	.006	.003		.004 ^c

- a. Not assuming the null hypothesis.
- b. Cannot be computed because the asymptotic standard error equals zero.
- c. Based on chi-square approximation

Table A9.4 Symmetric Measures for start-up registered capital * closest friend power

		Value	Approx Sig.
Nominal by Nominal	Phi	.075	.004
	Cramer's V	.075	.004
	Contingency Coefficient	.075	.004
N of Valid Cases		2329	

- a. Not assuming the null hypothesis.
- b. Using the asymptotic standard error assuming the null hypothesis.

Table A10.1 start-up real assets * closest friend power Crosstabulation

		closest friend power		Total	
		non-cadre	cadre		
start-up real assets	<=200000	Count	411	761	1172
		% within closest friend power	58.8%	50.8%	53.4%
	200001-600000	Count	149	367	516
		% within closest friend power	21.3%	24.5%	23.5%
	600001-2000000	Count	104	230	334
		% within closest friend power	14.9%	15.4%	15.2%
	>2000000	Count	35	139	174
		% within closest friend power	5.0%	9.3%	7.9%
Total		Count	699	1497	2196
		% within closest friend power	100.0%	100.0%	100.0%

Table A10.2 Chi-Square Tests for start-up real assets * closest friend power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	18.818 ^a	3	.000
Likelihood Ratio	19.715	3	.000
Linear-by-Linear Association	14.453	1	.000
N of Valid Cases	2196		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 55.39.

Table A10.3 Directional Measures for start-up real assets * closest friend power

		Value	Asymp. Std Error ^b	Approx T	Approx Sig ^c
Nominal by Nominal	Lambda Symmetric	.000	.000	.	.
	start-up real assets Dependent	.000	.000	.	.
	closest friend power Dependent	.000	.000	.	.
Goodman and Kruskal ta	start-up real assets Dependent	.003	.002		.000 ^a
	closest friend power Dependent	.009	.004		.000 ^a

a. Not assuming the null hypothesis.

b. Cannot be computed because the asymptotic standard error equals zero.

c. Based on chi-square approximation

Table A10.4 Symmetric Measures for start-up real assets * closest friend power

		Value	Approx. Sig.
Nominal by Nominal	Phi	.093	.000
	Cramer's V	.093	.000
	Contingency Coefficient	.092	.000
N of Valid Cases		2196	

a. Not assuming the null hypothesis.

b. Using the asymptotic standard error assuming the null hypothesis.

Table A11.1 main sources of start-up capital * respond power Crosstabulation

			respond power		Total
			non-cadre	cadre	
main sources of start-up capital	family & friend	Count	431	286	717
		% within respond power	27.8%	27.8%	27.8%
	personal savings	Count	892	570	1462
		% within respond power	57.5%	55.3%	56.7%
	public finance	Count	198	145	343
		% within respond power	12.8%	14.1%	13.3%
	others	Count	29	29	58
		% within respond power	1.9%	2.8%	2.2%
Total		Count	1550	1030	2580
		% within respond power	100.0%	100.0%	100.0%

Table A11.2 Chi-Square Tests for main sources of start-up capital * respond power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3.780 ^a	3	.286
Likelihood Ratio	3.726	3	.293
Linear-by-Linear Association	1.317	1	.251
N of Valid Cases	2580		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 23.16.

Table A12.1 main sources of start-up capital * father power Crosstabulation

			father power		Total
			non-cadre	cadre	
main sources of start-up capital	family & friend	Count	440	236	676
		% within father power	27.2%	31.1%	28.4%
	personal savings	Count	936	401	1337
		% within father power	57.8%	52.8%	56.2%
	public finance	Count	214	98	312
		% within father power	13.2%	12.9%	13.1%
	others	Count	30	25	55
		% within father power	1.9%	3.3%	2.3%
Total		Count	1620	760	2380
		% within father power	100.0%	100.0%	100.0%

Table A12.2 Chi-Square Tests for main sources of start-up capital * father power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	9.740 ^a	3	.021
Likelihood Ratio	9.464	3	.024
Linear-by-Linear Association	.185	1	.667
N of Valid Cases	2380		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 17.56.

Table A13.1 main sources of start-up capital * spouse power Crosstabulation

			spouse power		Total
			non-cadre	cadre	
main sources of start-up capital	family & friend	Count	474	192	666
		% within spouse power	27.5%	26.7%	27.3%
	personal savings	Count	985	409	1394
		% within spouse power	57.2%	56.9%	57.1%
	public finance	Count	231	93	324
		% within spouse power	13.4%	12.9%	13.3%
	others	Count	31	25	56
		% within spouse power	1.8%	3.5%	2.3%
Total	Count	1721	719	2440	
	% within spouse power	100.0%	100.0%	100.0%	

Table A13.2 Chi-Square Tests for main sources of start-up capital * spouse power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	6.437 ^a	3	.092
Likelihood Ratio	5.983	3	.112
Linear-by-Linear Association	1.422	1	.233
N of Valid Cases	2440		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 16.50.

Table A14.1 main sources of start-up capital * closest relative power Crosstabulation

			closest relative power		Total
			non-cadre	cadre	
main sources of start-up capital	family & friend	Count	284	361	645
		% within closest relative power	27.0%	28.8%	28.0%
	personal savings	Count	602	707	1309
		% within closest relative power	57.3%	56.5%	56.9%
	public finance	Count	145	155	300
		% within closest relative power	13.8%	12.4%	13.0%
	others	Count	19	29	48
		% within closest relative power	1.8%	2.3%	2.1%
Total	Count	1050	1252	2302	
	% within closest relative power	100.0%	100.0%	100.0%	

Table A14.2 Chi-Square Tests for main sources of start-up capital * closest relative power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	2.324 ^a	3	.508
Likelihood Ratio	2.330	3	.507
Linear-by-Linear Association	.574	1	.449
N of Valid Cases	2302		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 21.89.

Table A15.1 main sources of start-up capital * closest friend power
Crosstabulation

			closest friend power		Total
			non-cadre	cadre	
main sources of start-up capital	family & friend	Count	219	447	666
		% within closest friend power	29.4%	27.5%	28.1%
	personal savings	Count	419	926	1345
		% within closest friend power	56.2%	57.0%	56.8%
public finance	Count	97	213	310	
	% within closest friend power	13.0%	13.1%	13.1%	
others	Count	10	39	49	
	% within closest friend power	1.3%	2.4%	2.1%	
Total	Count	745	1625	2370	
	% within closest friend power	100.0%	100.0%	100.0%	

Table A15.2 Chi-Square Tests for main sources of start-up capital * closest friend power

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3.465 ^a	3	.325
Likelihood Ratio	3.688	3	.297
Linear-by-Linear Association	1.771	1	.183
N of Valid Cases	2370		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 15.40.

Table A16.1 start-up registered capital *all/non-cadre Crosstabulation

			respond power		Total
			non-cadre	cadre	
start-up registered capital	<=150000	Count	135	45	180
		% within respond power	57.0%	49.5%	54.9%
	150001-500000	Count	61	19	80
		% within respond power	25.7%	20.9%	24.4%
500001-1180000	Count	20	11	31	
	% within respond power	8.4%	12.1%	9.5%	
>1180000	Count	21	16	37	
	% within respond power	8.9%	17.6%	11.3%	
Total	Count	237	91	328	
	% within respond power	100.0%	100.0%	100.0%	

Table A16.2 Chi-Square Tests for start-up registered capital *all/non-cadre

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	6.673 ^a	3	.083
Likelihood Ratio	6.291	3	.098
Linear-by-Linear Association	5.146	1	.023
N of Valid Cases	328		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 8.60.

Table A 16.3 start-up real assets * all/non-cadre Crosstabulation

			respond power		Total
			non-cadre	cadre	
start-up real assets	<=200000	Count	128	35	163
		% within respond power	55.9%	41.7%	52.1%
	200001-600000	Count	51	24	75
		% within respond power	22.3%	28.6%	24.0%
	600001-2000000	Count	35	16	51
		% within respond power	15.3%	19.0%	16.3%
	>2000000	Count	15	9	24
		% within respond power	6.6%	10.7%	7.7%
Total		Count	229	84	313
		% within respond power	100.0%	100.0%	100.0%

Table A 16.4 Chi-Square Tests for start-up real assets * all/non-cadre

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	5.331 ^a	3	.149
Likelihood Ratio	5.298	3	.151
Linear-by-Linear Association	4.474	1	.034
N of Valid Cases	313		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 6.44.

Table A17.1 main sources of start-up capital * all/non-cadre Crosstabulation

			respond power		Total
			non-cadre	cadre	
main sources of start-up capital	family & friend	Count	73	32	105
		% within respond power	30.4%	33.7%	31.3%
	personal savings	Count	139	45	184
		% within respond power	57.9%	47.4%	54.9%
	public finance	Count	27	14	41
		% within respond power	11.3%	14.7%	12.2%
	others	Count	1	4	5
		% within respond power	.4%	4.2%	1.5%
Total		Count	240	95	335
		% within respond power	100.0%	100.0%	100.0%

Table A17.2 Chi-Square Tests for main sources of start-up capital * all/non-cadre

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	8.850 ^a	3	.031
Likelihood Ratio	8.046	3	.045
Linear-by-Linear Association	.881	1	.348
N of Valid Cases	335		

a. 2 cells (25.0%) have expected count less than 5. The minimum expected count is 1.42.

Table A18.1 start-up registered capital * all/non-cadre in commerce Crosstabulation *

			respond power		Total
			non-cadre	cadre	
start-up registered capital	<=150000	Count	40	13	53
		% within respond power	66.7%	50.0%	61.6%
	150001-500000	Count	12	5	17
		% within respond power	20.0%	19.2%	19.8%
	500001-1180000	Count	5	4	9
		% within respond power	8.3%	15.4%	10.5%
	>1180000	Count	3	4	7
		% within respond power	5.0%	15.4%	8.1%
Total	Count	60	26	86	
	% within respond power	100.0%	100.0%	100.0%	

a. D27A18 = 1.00

Table A18.2 Chi-Square Tests for start-up registered capital * all/non-cadre in commerce

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	4.088 ^a	3	.252
Likelihood Ratio	3.830	3	.280
Linear-by-Linear Association	3.837	1	.050
N of Valid Cases	86		

a. 3 cells (37.5%) have expected count less than 5. The minimum expected count is 2.12.

b. D27A18 = 1.00

Table A18.3 start-up real assets * all/non-cadre in commerce Crosstabulation *

			respond power		Total
			non-cadre	cadre	
start-up real assets	<=200000	Count	39	11	50
		% within respond power	65.0%	45.8%	59.5%
	200001-600000	Count	12	6	18
		% within respond power	20.0%	25.0%	21.4%
	600001-2000000	Count	7	6	13
		% within respond power	11.7%	25.0%	15.5%
	>2000000	Count	2	1	3
		% within respond power	3.3%	4.2%	3.6%
Total	Count	60	24	84	
	% within respond power	100.0%	100.0%	100.0%	

a. D27A18 = 1.00

Table A18.4 Chi-Square Tests for start-up real assets * all/non-cadre in commerce

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3.261 ^a	3	.353
Likelihood Ratio	3.140	3	.371
Linear-by-Linear Association	2.613	1	.106
N of Valid Cases	84		

a. 3 cells (37.5%) have expected count less than 5. The minimum expected count is .86.

b. D27A18 = 1.00

Table A18.5 main sources of start-up capital * all/non-cadre in commerce Crosstabulation

			respond power		Total
			non-cadre	cadre	
main sources of start-up capital	family & friend	Count	27	13	40
		% within respond power	43.5%	50.0%	45.5%
	personal savings	Count	32	9	41
		% within respond power	51.6%	34.6%	46.6%
	public finance	Count	3	3	6
		% within respond power	4.8%	11.5%	6.8%
	others	Count		1	1
		% within respond power		3.8%	1.1%
Total	Count	62	26	88	
	% within respond power	100.0%	100.0%	100.0%	

a. D27A18 = 1.00

Table A18.6 Chi-Square Tests for main sources of start-up capital * all/non-cadre in commerce

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	4.894 ^a	3	.180
Likelihood Ratio	4.906	3	.179
Linear-by-Linear Association	.262	1	.609
N of Valid Cases	88		

a. 4 cells (50.0%) have expected count less than 5. The minimum expected count is .30.

b. D27A18 = 1.00

Table A19.1 start-up registered capital * all/non-cadre manufacturing Crosstabulation

			respond power		Total
			non-cadre	cadre	
start-up registered capital	<=150000	Count	42	18	60
		% within respond power	48.8%	54.5%	50.4%
	150001-500000	Count	27	8	35
		% within respond power	31.4%	24.2%	29.4%
	500001-1180000	Count	7	3	10
		% within respond power	8.1%	9.1%	8.4%
	>1180000	Count	10	4	14
		% within respond power	11.6%	12.1%	11.8%
Total	Count	86	33	119	
	% within respond power	100.0%	100.0%	100.0%	

a. D27A13 = 1.00

Table A19.2 Chi-Square Tests for start-up registered capital * all/non-cadre manufacturing

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	.600 ^a	3	.897
Likelihood Ratio	.613	3	.893
Linear-by-Linear Association	.033	1	.856
N of Valid Cases	119		

a. 2 cells (25.0%) have expected count less than 5. The minimum expected count is 2.77.

b. D27A13 = 1.00

Table A19.3 start-up real assets * all/non-cadre in manufacture Crosstabulation *

			respond power		Total
			non-cadre	cadre	
start-up real assets	<=200000	Count	42	12	54
		% within respond power	51.2%	40.0%	48.2%
	200001-600000	Count	19	11	30
		% within respond power	23.2%	36.7%	26.6%
	600001-2000000	Count	15	5	20
		% within respond power	18.3%	16.7%	17.9%
	>2000000	Count	6	2	8
		% within respond power	7.3%	6.7%	7.1%
Total	Count	82	30	112	
	% within respond power	100.0%	100.0%	100.0%	

a. D27A13 = 1.00

Table A19.4 Chi-Square Tests for start-up real assets * all/non-cadre in manufacture

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	2.113 ^a	3	.549
Likelihood Ratio	2.041	3	.564
Linear-by-Linear Association	.163	1	.687
N of Valid Cases	112		

a. 1 cells (12.5%) have expected count less than 5. The minimum expected count is 2.14.

b. D27A13 = 1.00

Table A19.5 main sources of start-up capital * all/non-cadre in manufacture Crosstabulation

			respond power		Total
			non-cadre	cadre	
main sources of start-up capital	family & friend	Count	23	9	32
		% within respond power	26.4%	26.5%	26.4%
	personal savings	Count	55	20	75
		% within respond power	63.2%	58.8%	62.0%
	public finance	Count	9	5	14
		% within respond power	10.3%	14.7%	11.6%
Total	Count	87	34	121	
	% within respond power	100.0%	100.0%	100.0%	

a. D27A13 = 1.00

Table A19.6 Chi-Square Tests for main sources of start-up capital * all/non-cadre in manufacture

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	.478 ^a	2	.787
Likelihood Ratio	.460	2	.795
Linear-by-Linear Association	.127	1	.722
N of Valid Cases	121		

a. 1 cells (16.7%) have expected count less than 5. The minimum expected count is 3.93.

b. D27A13 = 1.00

Table A20.1 start-up registered capital * high rank respondent Crosstabulation

			high rank respondent		Total
			non cadre	>=county	
start-up registered capital	<=150000	Count	1324	16	1340
		% within high rank respondent	53.0%	36.4%	52.7%
	150001-500000	Count	674	16	690
		% within high rank respondent	27.0%	36.4%	27.1%
500001-1180000	Count	258	4	262	
	% within high rank respondent	10.3%	9.1%	10.3%	
>1180000	Count	244	8	252	
	% within high rank respondent	9.8%	18.2%	9.9%	
Total		Count	2500	44	2544
		% within high rank respondent	100.0%	100.0%	100.0%

Table A20.2 Chi-Square Tests for start-up registered capital * high rank respondent

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	6.830 ^a	3	.078
Likelihood Ratio	6.363	3	.095
Linear-by-Linear Association	4.599	1	.032
N of Valid Cases	2544		

a. 2 cells (25.0%) have expected count less than 5. The minimum expected count is 4.36.

Table A20.3 start-up real assets * high rank respondent Crosstabulation

			high rank respondent		Total
			non cadre	>=county	
start-up real assets	<=200000	Count	1249	17	1266
		% within high rank respondent	53.2%	44.7%	53.1%
	200001-600000	Count	548	10	558
		% within high rank respondent	23.4%	26.3%	23.4%
600001-2000000	Count	352	6	358	
	% within high rank respondent	15.0%	15.8%	15.0%	
>2000000	Count	197	5	202	
	% within high rank respondent	8.4%	13.2%	8.5%	
Total		Count	2346	38	2384
		% within high rank respondent	100.0%	100.0%	100.0%

Table A20.4 Chi-Square Tests for start-up real assets * high rank respondent

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	1.664 ^a	3	.645
Likelihood Ratio	1.544	3	.672
Linear-by-Linear Association	1.358	1	.244
N of Valid Cases	2384		

a. 1 cells (12.5%) have expected count less than 5. The minimum expected count is 3.22.

Table A21.1 start-up registered capital * high rank father Crosstabulation

			high rank father		Total
			non-cadre	>=county	
start-up registered capital	<=150000	Count	1178	49	1227
		% within high rank father	53.1%	38.9%	52.4%
	150001-500000	Count	588	50	638
		% within high rank father	26.4%	39.7%	27.1%
	500001-1180000	Count	226	13	239
		% within high rank father	10.2%	10.3%	10.2%
	>1180000	Count	227	14	241
		% within high rank father	10.2%	11.1%	10.3%
Total	Count	2217	126	2343	
	% within high rank father	100.0%	100.0%	100.0%	

Table A21.2 Chi-Square Tests for start-up registered capital * high rank father

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	12.422 ^a	3	.008
Likelihood Ratio	11.935	3	.008
Linear-by-Linear Association	3.124	1	.077
N of Valid Cases	2343		

- a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 12.85.

Table A21.3 Symmetric Measures for start-up registered capital * high rank father

			Value	Approx. Sig.
Nominal by Nominal	Phi		.073	.008
	Cramer's V		.073	.008
	Contingency Coefficient		.073	.008
N of Valid Cases			2343	

- a. Not assuming the null hypothesis.
 b. Using the asymptotic standard error assuming the null hypothesis.

Table A21.4 start-up real assets * high rank father Crosstabulation

			high rank father		Total
			non-cadre	>=county	
start-up real assets	<=200000	Count	1108	56	1164
		% within high rank father	53.3%	48.3%	53.0%
	200001-600000	Count	474	35	509
		% within high rank father	22.8%	30.2%	23.2%
	600001-2000000	Count	316	16	332
		% within high rank father	15.2%	13.8%	15.1%
	>2000000	Count	181	9	190
		% within high rank father	8.7%	7.8%	8.7%
Total	Count	2079	116	2195	
	% within high rank father	100.0%	100.0%	100.0%	

**Table A21.5 Chi-Square Tests for start-up real assets *
high rank father**

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3.355*	3	.340
Likelihood Ratio	3.166	3	.367
Linear-by-Linear Association	.033	1	.856
N of Valid Cases	2195		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 10.04.

Table A22.1 start-up registered capital * high cadre spouse Crosstabulation

			high cadre spouse		Total
			non	>=county chief	
start-up registered capital	<=150000	Count	1263	18	1281
		% within high cadre spouse	53.5%	41.9%	53.3%
	150001-500000	Count	632	15	647
		% within high cadre spouse	26.8%	34.9%	26.9%
	500001-1180000	Count	241	4	245
		% within high cadre spouse	10.2%	9.3%	10.2%
	>1180000	Count	224	6	230
		% within high cadre spouse	9.5%	14.0%	9.6%
Total		Count	2360	43	2403
		% within high cadre spouse	100.0%	100.0%	100.0%

**Table A22.2 Chi-Square Tests for start-up registered
capital * high cadre spouse**

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3.019*	3	.389
Likelihood Ratio	2.910	3	.406
Linear-by-Linear Association	1.701	1	.192
N of Valid Cases	2403		

a. 2 cells (25.0%) have expected count less than 5. The minimum expected count is 4.12.

Table A22.3 start-up real assets * high cadre spouse Crosstabulation

			high cadre spouse		Total
			non	>=county chief	
start-up real assets	<=200000	Count	1185	21	1206
		% within high cadre spouse	53.3%	55.3%	53.4%
	200001-600000	Count	519	11	530
		% within high cadre spouse	23.4%	26.9%	23.5%
	600001-2000000	Count	329	5	334
		% within high cadre spouse	14.8%	13.2%	14.8%
	>2000000	Count	189	1	190
		% within high cadre spouse	8.5%	2.6%	8.4%
Total		Count	2222	38	2260
		% within high cadre spouse	100.0%	100.0%	100.0%

Table A22.4 Chi-Square Tests for start-up real assets * high cadre spouse

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	2.126 ^a	3	.547
Likelihood Ratio	2.653	3	.448
Linear-by-Linear Association	.904	1	.342
N of Valid Cases	2260		

a. 1 cells (12.5%) have expected count less than 5. The minimum expected count is 3.19.

Table A23.1 start-up registered capital * High cadre relative Crosstabulation

		High cadre relative		Total
		non	>=county chief	
start-up registered capital	<=150000	Count 1046 52.9%	164 57.1%	1210 53.4%
	150001-500000	Count 550 27.8%	72 25.1%	622 27.5%
	500001-1180000	Count 199 10.1%	26 9.1%	225 9.9%
	>1180000	Count 183 9.3%	25 8.7%	208 9.2%
Total	Count 1978 100.0%	287 100.0%	2265 100.0%	

Table A23.2 Chi-Square Tests for start-up registered capital * High cadre relative

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	1.859 ^a	3	.602
Likelihood Ratio	1.868	3	.600
Linear-by-Linear Association	1.075	1	.300
N of Valid Cases	2265		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 26.36.

Table A23.3 start-up real assets * High cadre relative Crosstabulation

		High cadre relative		Total
		non	>=county chief	
start-up real assets	<=200000	Count 1007 54.0%	148 55.2%	1155 54.1%
	200001-600000	Count 430 23.0%	60 22.4%	490 23.0%
	600001-2000000	Count 278 14.9%	42 15.7%	320 15.0%
	>2000000	Count 151 8.1%	18 6.7%	169 7.9%
Total	Count 1866 100.0%	268 100.0%	2134 100.0%	

**Table A23.4 Chi-Square Tests for start-up real assets *
High cadre relative**

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	.766 ^a	3	.858
Likelihood Ratio	.791	3	.852
Linear-by-Linear Association	.257	1	.612
N of Valid Cases	2134		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 21.22.

Table A24.1 start-up registered capital * high cadre friend Crosstabulation

			high cadre friend		Total
			non	>=county chief	
start-up registered capital	<=150000	Count	1068	166	1234
		% within high cadre friend	53.6%	49.6%	53.0%
	150001-500000	Count	547	90	637
		% within high cadre friend	27.4%	26.9%	27.4%
500001-1180000	Count	200	39	239	
	% within high cadre friend	10.0%	11.6%	10.3%	
>1180000	Count	179	40	219	
	% within high cadre friend	9.0%	11.9%	9.4%	
Total	Count	1994	335	2329	
	% within high cadre friend	100.0%	100.0%	100.0%	

**Table A24.2 Chi-Square Tests for start-up registered
capital * high cadre friend**

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	4.308 ^a	3	.230
Likelihood Ratio	4.123	3	.249
Linear-by-Linear Association	4.018	1	.045
N of Valid Cases	2329		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 31.50.

Table A24.3 start-up real assets * high cadre friend Crosstabulation

			high cadre friend		Total
			non	>=county chief	
start-up real assets	<=200000	Count	1008	164	1172
		% within high cadre friend	53.6%	51.7%	53.4%
	200001-600000	Count	438	78	516
		% within high cadre friend	23.3%	24.6%	23.5%
600001-2000000	Count	288	46	334	
	% within high cadre friend	15.3%	14.5%	15.2%	
>2000000	Count	145	29	174	
	% within high cadre friend	7.7%	9.1%	7.9%	
Total	Count	1879	317	2196	
	% within high cadre friend	100.0%	100.0%	100.0%	

Table A24.4 Chi-Square Tests for start-up real assets *
high cadre friend

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	1.199 ^a	3	.753
Likelihood Ratio	1.172	3	.760
Linear-by-Linear Association	.445	1	.504
N of Valid Cases	2196		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 25.12.

Table A25.1 main sources of start-up capital * high rank respondent
Crosstabulation

			high rank respondent		Total
			non cadre	>=county	
main sources of start-up capital	family & friend	Count	710	7	717
		% within high rank respondent	28.0%	16.7%	27.8%
	personal savings	Count	1433	29	1462
		% within high rank respondent	56.5%	69.0%	56.7%
	public finance	Count	338	5	343
		% within high rank respondent	13.3%	11.9%	13.3%
	others	Count	57	1	58
		% within high rank respondent	2.2%	2.4%	2.2%
Total		Count	2538	42	2580
		% within high rank respondent	100.0%	100.0%	100.0%

Table A25.2 Chi-Square Tests for main sources of
start-up capital * high rank respondent

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3.121 ^a	3	.373
Likelihood Ratio	3.365	3	.339
Linear-by-Linear Association	.870	1	.351
N of Valid Cases	2580		

a. 1 cells (12.5%) have expected count less than 5. The minimum expected count is .94.

Table A26.1 main sources of start-up capital * high rank father Crosstabulation

			high rank father		Total
			non-cadre	>=county	
main sources of start-up capital	family & friend	Count	630	46	676
		% within high rank father	28.0%	36.5%	28.4%
	personal savings	Count	1276	61	1337
		% within high rank father	56.6%	48.4%	56.2%
	public finance	Count	297	15	312
		% within high rank father	13.2%	11.9%	13.1%
	others	Count	51	4	55
		% within high rank father	2.3%	3.2%	2.3%
Total		Count	2254	126	2380
		% within high rank father	100.0%	100.0%	100.0%

Table A26.2 Chi-Square Tests for main sources of start-up capital * high rank father

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	5.081 ^a	3	.166
Likelihood Ratio	4.867	3	.182
Linear-by-Linear Association	1.541	1	.215
N of Valid Cases	2380		

a. 1 cells (12.5%) have expected count less than 5. The minimum expected count is 2.91.

Table A27.1 main sources of start-up capital * high cadre spouse Crosstabulation

			high cadre spouse		Total
			non	>=county chief	
main sources of start-up capital	family & friend	Count	652	14	666
		% within high cadre spouse	27.2%	30.4%	27.3%
	personal savings	Count	1368	26	1394
		% within high cadre spouse	57.1%	56.5%	57.1%
public finance	Count	319	5	324	
	% within high cadre spouse	13.3%	10.9%	13.3%	
others	Count	55	1	56	
	% within high cadre spouse	2.3%	2.2%	2.3%	
Total		Count	2394	46	2440
		% within high cadre spouse	100.0%	100.0%	100.0%

Table A27.2 Chi-Square Tests for main sources of start-up capital * high cadre spouse

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	.380 ^a	3	.944
Likelihood Ratio	.388	3	.943
Linear-by-Linear Association	.322	1	.571
N of Valid Cases	2440		

a. 1 cells (12.5%) have expected count less than 5. The minimum expected count is 1.06.

Table A28.1 main sources of start-up capital * High cadre relative Crosstabulation

			High cadre relative		Total
			non	>=county chief	
main sources of start-up capital	family & friend	Count % within High cadre relative	560 27.8%	85 29.2%	645 28.0%
	personal savings	Count % within High cadre relative	1145 56.9%	164 56.4%	1309 56.9%
	public finance	Count % within High cadre relative	263 13.1%	37 12.7%	300 13.0%
	others	Count % within High cadre relative	43 2.1%	5 1.7%	48 2.1%
Total		Count % within High cadre relative	2011 100.0%	291 100.0%	2302 100.0%

Table A28.2 Chi-Square Tests for main sources of start-up capital * High cadre relative

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	.424 ^a	3	.935
Likelihood Ratio	.434	3	.933
Linear-by-Linear Association	.347	1	.556
N of Valid Cases	2302		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 6.07.

Table A29.1 main sources of start-up capital * high cadre friend Crosstabulation

			high cadre friend		Total
			non	>=county chief	
main sources of start-up capital	family & friend	Count % within high cadre friend	572 28.2%	94 27.6%	666 28.1%
	personal savings	Count % within high cadre friend	1156 57.0%	189 55.4%	1345 56.8%
	public finance	Count % within high cadre friend	261 12.9%	49 14.4%	310 13.1%
	others	Count % within high cadre friend	40 2.0%	9 2.8%	49 2.1%
Total		Count % within high cadre friend	2029 100.0%	341 100.0%	2370 100.0%

Table A29.2 Chi-Square Tests for main sources of start-up capital * high cadre friend

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	1.300 ^a	3	.729
Likelihood Ratio	1.246	3	.742
Linear-by-Linear Association	.727	1	.394
N of Valid Cases	2370		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 7.05.

Appendix B: Questionnaire on Start-ups in the private IT firms

1. Your Sex: 1) Male; 2) Female
2. You were born in _____ (year)
3. Your education
4. Your enterprise was registered in _____ (year)
5. How many investors were there when you registered your business ____
What were they (job and position) then?
6. Your enterprise is registered as 1) sole proprietorship; 2) partnership; 3) corporate limited company
7. What business is your firm mainly in (in terms of revenue)?
8. The amount of registered capital of your enterprise at start-up:
9. The amount of real available capital when you started up

10. Performance of your enterprise

	1) output value	2) sale value	3) added value	4) other income	5) tax	6) other fees	7) profit
A. the first year							
B. 1999							

11. How did you get primitive capital when you started your enterprise (choose three according to the order of importance)

A. first important	B. second important	C. third important

- | | |
|----------------------------------|--------------------------------------|
| 1) family heritage; | 2) work savings; |
| 3) gains from stock or property; | 4) overseas investment; |
| 5) borrowing from relatives; | 6) bank loan; |
| 7) borrowing from work unit ; | 8) borrowing from other individuals; |
| 9) others (please specify) | |

If you choose 5) or 6) or 7) or 8), did you pay interest?

12. At the beginning of your business,
Who were your main customers?

How did you get to know them?

13. The market coverage of your business in terms of area:

1) Beijing; 2) beyond Beijing; 3) overseas; 4) others

14. Please fill in the proper number

	1) occupation	2) character of workunit	3) position
	1. technical profession; 2. governmental cadre; 3. enterprise cadre; 4. ordinary worker; 5. military service; 6. ordinary employee in commerce or service; 7. peasant; 8. professional or craftsman; 9. individual economy; 10. others; 11. no job	1. all people owned; 2. township collective; 3. town collective; 4. partnership (among state owned, collective, private and individual); 5. foreign invested; 6. private enterprise; 7. individual economy; 8. farmer household or village collective; 9. no job	1. section chief; 2. division chief; 3. department chief; 4. head of county or higher; 5. head of enterprise; 6. middle managerial cadre in enterprise; 7. enterprise staff on supplying and marketing; 8. ordinary cadre; 9. head of town (commune); 10. head or cadre of village; 11. leaser of state owned or collective unit; 12. military officer; 13. no job
A. Your father mainly is/was			
B. you were firstly in year			
C. Before this business, you were			
D. The closest relatives are			
E. The most frequently contacted friends are			
F. Your spouse currently is			

15. The places where you were born, live, and work

	1. big city	2. middle city	3. small city	4. town	5. village
A. Born place					
B. your family lives in					
C. your business location					

16. Who were the most important people in your business start-up? Please list their positions, and specify in what aspects they helped.

17. Consider all of the contacts or connections you have made in your business so far, who have been your most valued connection or contacts in the sense that they were the most important to your business success? Please give their positions.

- 1).
- 2).
- 3).

How did you know them respectively?

- 1)
- 2)
- 3)

18. What is the role of *guanxi* in business, do you think?

19. How do you reciprocate those who help you in your business?

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