WARY MANAGERS/INVESTORS: VULNERABILITY, CONTROL, TRUST, AND DISTRUST IN FOREIGN ENTERPRISES IN CHINA

– ABBREVIATED VERSION –

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ABSTRACT

Based on a comparative, ethnographic study of foreign-controlled enterprises in two different regions in China, we generate a causal and process model with propositions to analyze the recursive relationship between vulnerability, control, and the development of trust and distrust. The model proposed is relevant to organization theory and international management.

INTRODUCTION

Foreign enterprises in transition economies like China represent a prime example of a setting in which problems of societal transformation and internationalization combine at the management level and make vulnerability particularly salient. Foreign managers and investors in the China context tend to be wary of corporate espionage, frauds, piracy, and imitation. An intriguing question is: How does this affect the development of their relationships with local members of the organizations they manage? To what extent is intra-organizational managerial action conditioned by the external conditions in which it is embedded? Is the embedded agency, in turn, capable of moderating the effect of those external conditions?

We conducted an ethnographic study of three foreign ventures in two different regions China in order to develop a contextually-grounded theoretical model with propositions to guide future studies. Our inductive field study yields a causal and sequential model with propositions to analyze the determinants of perceived vulnerability and the recursive relationship between vulnerability, control, and the development of trust and distrust.

VULNERABILITY, TRUSTWORTHINESS, TRUST, DISTRUST, AND CONTROL

The word vulnerability refers to the threat of suffering from externally caused damage. We examine the extent of vulnerability that is subjectively perceived by foreign managers and investors in relation to the local members who are in a position to do them harm in the light of external conditions that may promote the perception of vulnerability.

While vulnerability concerns the question to what extent an actor can be harmed by another actor, perceived trustworthiness captures the extent to which an actor believes that the other actor will not do harm, even though it would be possible. Perceptions of trustworthiness are dynamic in the sense that they change over time when the actors involved gain experience with each other (Mayer, Davis, & Schoorman, 1995). We will analyze the factors that cause foreign managers and investors to change their perceptions of the local members in this regard over time.

Vulnerability is the basic condition from which the problem of trust and distrust and the question of the others′ trustworthiness arise. However, previous empirical studies have framed vulnerability mainly as a consequence of trust (Mayer & Davis, 1999), an idea which is in line with rational choice conceptions of trust as a form of risk-taking (Coleman, 1990). This approach assumes that actors are in a kind of neutral position from which they can choose how much to increase or decrease vulnerability. In contrast, Möllering (2006) stresses that vulnerability comes before trust, as actors do not start from a neutral position. In our study, we examine the contending arguments concerning the relationship between trust and vulnerability.

The relationship between trust and distrust is equally complex. We have adopted and explored the conception of Lewicki, McAllister, and Bies (1998: 440) that trust and distrust are distinct dimensions and ″not opposite ends of a single continuum″ and that they can coexist.

Several authors recognize that trust is not merely a passive reaction to the trustworthiness of trustees, but also the result of an active trust investment (Child & Möllering, 2003; Williams, 2007). In our empirical analysis, we captured foreign managers′ and investors′ active trust investment activities that might have an impact on the perceived trustworthiness of the locals as well as on the levels of trust and distrust.

In addition to trust and distrust, the exercise of control is often seen as a managerial response that aims to reduce vulnerability. The broad distinction between formal control and social control (Cardinal, Sitkin, & Long, 2004; Inkpen & Currall, 2004) is applicable to our empirical analysis, and hence we relied on this distinction to fine-tune our interview questions on control issues.

Whereas the relationship between distrust and control is relatively clear, that between trust and control continues to be controversial (Das & Teng, 1998). Some authors argue that control which is based on asymmetric power may be a substitute for trust that stems from shared values and norms (Inkpen & Currall, 2004). Others contend that trust and control are complementary, and that the implementation of control may foster trust and vice versa (Sitkin, 1995) – with the resultant managerial challenge to achieve a balance (Long & Sitkin, 2006). We empirically examine the unresolved relationship between control and trust and extend the scope of our analysis by viewing trust and control together with distrust and vulnerability in a process perspective.

The above conceptualizations include two very important premises for our fieldwork. First, we have adopted a dynamic perspective, reflecting the co-evolution of vulnerability, trustworthiness, control, trust, and distrust over time. Secondly, we place such development in context and explicitly considered the role of the institutional context and other environmental conditions.

In examining the link between external, contextual conditions and internal organizational processes, we address a theoretical question that is analogous to the important conundrum of how embeddedness (Zukin & DiMaggio, 1990) and agency (Emirbayer & Mische, 1998) are related and reconciled in practice. Using the particularly vivid case of foreign managers in China, we analyze a form of embedded agency on the part of foreign managers and investors. We assume, on the one hand, that foreign managers and investors find themselves in Chinese operations that are clearly embedded structurally, culturally, cognitively and politically in various ways. On the other hand, the same managers and investors realize their agency – the potential to make a difference through their actions – at least within the organizations they manage.

RESEARCH QUESTIONS

In order to address the unsolved relationship between the concepts being reviewed, we explore two main research questions: (1) What are the conditions that shape the perceived vulnerability of foreign managers and investors? (2) How do trust, distrust, and control develop in relation to perceived vulnerability and perceived trustworthiness over time?

METHOD

We addressed highly delicate, elusive, and sensitive phenomena that an ethnographic study with intensive fieldwork is able to capture more effectively than a survey-based study. In particular, we chose a comparative, multiple-case approach as it permits the induction of richer and better-grounded propositions than a single-case study approach could (Eisenhardt, 1989).

We identified three cases that showed different levels of perceived vulnerability and were located in two different provinces. Our data collection (from early 2002 to mid-2006) involved in-depth interviews, obtaining factual information as well as open-ended narrative data. One of us guided three teams of research students with three members each to conduct the field studies in three waves over an average period of 20 months for each case. We observed procedures that enhance the validity and reliability of our research. Concerning data analysis, an interpretive analysis of content in the spirit of grounded theory (Glaser, 1998) led us to the construction of tentative propositions to show the causal relationship between constructs and patterns. The propositions were refined by frequently revisiting the data based on the replication logic

A BRIEF SUMMARY OF RESULTS

At the inception of Kunling, our first case, all the foreign managers interviewed felt highly vulnerable to an environment which lacked reliable institutions and a modern workforce, whose market they relied on, and in which they operated a plant with advanced proprietary knowledge and technology to protect. Hence, they had a low level of trust in and a high level of distrust of the locals and attempted to reduce their vulnerability by focusing on formal control and supplementing it with social control. In light of the locals′ compliance with control over time, the foreign investors and managers revised their initial perceptions and came to perceive the locals as trustworthy. They developed trust and lowered their distrust, and subsequently prompted the localization of managerial positions after five years in operation. However, they remained wary of leakages of proprietary knowledge and strengthened the associated control mechanisms once they suspected that leakages had occurred.

As for our second case, Elumin, the foreign managers and investors felt less vulnerable than their Kunling counterparts at the company′s inception. They did not have advanced proprietary knowledge to protect and relied on overseas markets. In addition, they felt that the locals were competent. Yet they were worried that the increasingly materialistic society might foster opportunistic behavior and were particularly wary of financial abuses. The foreign investors and managers focused on social control, which was supplemented by formal control. Similar to their counterparts at Kunling, they came to perceive the locals as trustworthy over time as they proved to be compliant with control. Eventually, they increasingly relied on local managers and adopted a responsibility-based system for the technical operation while maintaining formal control over financial matters.

As compared to his counterparts at Elumin and Kunling, the foreign investor of Hyform felt the least vulnerable. Hyform had neither advanced proprietary knowledge to protect nor a reliance on the local market. The foreign investor let his local partners run the operation with high autonomy and supplemented the active trust investment with formal control. In particular, he entered into a shareholder agreement with the local partners at the company′s inception.

PROPOSITIONS

Based on our cross-case analysis, we propose a theoretical framework that consists of two conceptual clusters. First, perceived vulnerability is shaped by technological, market, and institutional conditions. Second, perceived vulnerability has an effect on trust and distrust, which subsequently leads into a feedback cycle that also involves control, active trust investment, and perceived trustworthiness. The framework can be expressed in the following set of propositions, which we derived from our qualitative data and explain in detail in the full version of this paper:

Proposition 1a: The possession of advanced proprietary knowledge in a foreign-controlled enterprise increases the perceived vulnerability of its foreign managers and investors.

Proposition 1b: The more advanced the technology a foreign-controlled enterprise transfers to its local operation, the higher the perceived vulnerability of its foreign managers and investors.

Proposition 2a: The lower the entry barriers to the industry in which a foreign-controlled enterprise is operating, the higher the perceived vulnerability of its foreign managers and investors.

Proposition 2b: The higher the dependence of a foreign-controlled enterprise on the local market, the higher the perceived vulnerability of its foreign managers and investors.

Proposition 3a: Low confidence of foreign managers and investors in the legal enforcement system of a host country increases their perceived vulnerability.

Proposition 3b: Low confidence of foreign managers and investors in the social values held in the host country increases their perceived vulnerability.

Proposition 3c: The higher the confidence of foreign managers and investors in the work culture of a host region, the lower their perceived vulnerability.

Proposition 4: The higher the perceived vulnerability of foreign managers and investors, the lower their trust in and the higher their distrust of the local members in their enterprises.

Proposition 5a: When foreign managers and investors have high trust in and low distrust of local members, they are likely to focus on active trust investment.

Proposition 5b: When foreign managers and investors have low trust in and high distrust of local members, they are likely to focus on formal control.

Proposition 5c: When foreign managers and investors have moderate levels of trust in and distrust of local members, they are likely to focus on social control.

Proposition 6: If the local members respond positively to the use of control and active trust investment, their trustworthiness as perceived by the foreign managers and investors increases over time.

Proposition 7: Perceived trustworthiness of the local members moderates the effect of foreign managers′ and investors′ perceived vulnerability on their trust and distrust.

We emphasize that a learning process occurs in the sense that perceived trustworthiness, trust and distrust, and the use of control can be revised given new experiences and changing situations.

DISCUSSION AND CONCLUSION

In contrast to previous studies that framed vulnerability mainly as a consequence of trust (e.g. Mayer et al., 1995), our analysis highlights that perceived vulnerability is an antecedent of trust and distrust. We therefore maintain that vulnerability comes *before* trust (Möllering, 2006), without denying the possibility that trusting behaviors may increase vulnerability in return. Moreover, our field data reveals vulnerability as a mediator between external contextual factors and internal trust and distrust within organizations. We therefore argue that vulnerability should be treated as a central issue and a conceptual starting point in trust research.

We argue that the level of confidence in institutions shapes perceived vulnerability, which has a further effect on interpersonal trust and distrust. Previous empirical work by Child and Möllering (2003) showed a significant relationship between confidence in the institutional context and trust in local staff, but did not provide a precise explanation for this relationship. Our inductive results suggest that perceived vulnerability is the missing link. Moreover, we provide empirical support for the conceptualization of the coexistence of trust and distrust presented by Lewicki et al. (1998). We show the interplay between trust/distrust and control/active trust investment, and its subsequent impact on perceived trustworthiness and vulnerability.

Finally, our study contributes to the discussion around the notion of embedded agency (Emirbayer & Mische, 1998; Maguire, Hardy, & Lawrence, 2004). The managerial actions of the foreign managers and investors we observed were clearly conditioned by external factors, but they subsequently moderated the effects of external influences.

Since it is based on a small sample of firms, the generalizability of the theoretical model remains to be tested. However, we believe that our theoretical framework is applicable to foreign ventures operating in other transition or emerging economies, albeit to different extents. It would be an interesting research opportunity to conduct comparative studies of foreign ventures in different transition or emerging economies on the key issues of perceived vulnerability, control, and the development of trust and distrust.

The main finding of our study, however, is not simply that context matters. Rather, we find that while managerial perceptions of external conditions do make managers more or less wary – and accordingly, more or less prepared to trust organizational members internally – the influence of this externally induced perceived vulnerability can be moderated internally by a process of building up trustworthiness through control mechanisms and active trust investment.

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