

The Impact of Chinese Entrepreneur's Social Networks on the Development of Private Enterprises in China

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Abstract—The Entrepreneur's social network in China is the reflection of the deep-seated cultural and social background, which exerts both positive and negative effect on the development of the Chinese private enterprises. However, when the Chinese enterprises are further involved in the economic trend of the world, the negative effect will become the impediment of the development of the enterprises. As a result, establishing and improving a rational modern management regulation will play a critical role in promoting the growth of the enterprises.

Keywords—*Entrepreneur's Social Network; Private Enterprise; Entrepreneur; Relationship; Management System*

I. RESEARCH BACKGROUND

Since the 1990s, China has started its period of economic restructuring. The market environment became open and free. Numerous private enterprises sprung up in this period of time in China. At the same time, a number of outstanding private entrepreneurs appeared. However, due to political and other social issues, these new-started private enterprises had to compete with state-owned enterprises and foreign-funded enterprises for resources. This difficult situation blocked the development of private enterprises from the very beginning. Ultimately, the social network of entrepreneurs became an important way for them to access to resources. Private entrepreneurs gained development resources from their social network so as to create a better environment for their enterprises and to get a stronger position in the market. It was proved that the entrepreneur's social network is an effective way to allocate resources in the specific social structure and traditional culture in China during that period of time. Like the cases of Mr. Zhang Ruimin of Haier and Mr. Li Dongsheng of TCL, for a successful private entrepreneur, in addition to the outstanding business talent, a strong social network, which can help them to get more resources, is greatly needed. However, while the market is growing mature today, the market system is improving as well in China. Due to the characteristics of Chinese entrepreneurs' social network, it is becoming a negative impact on the development of enterprises now instead of a positive one in the past. The reliance on the entrepreneurs' social network becomes the shackle of the further development of private enterprises. Moreover, it greatly reduces the

competitive advantages of private enterprises in the international market, and hinders the process of internationalization of the private enterprises. Therefore, by analyzing the characteristics, background, and the role of both positive and negative aspects of Chinese entrepreneurs' social network, this study will propose a developmental trend for Chinese entrepreneurs' social network in the future.

II. THE CHARACTERISTICS OF CHINESE ENTREPRENEUR'S SOCIAL NETWORKS

The entrepreneur's social network is a unit of all the organizations and individuals which are directly related to the entrepreneur's activity during the whole business process. The American sociologist, Mark Granovetter from Stanford University, has created theories in modern sociology since the 1970s. According to his theory on social networks, social networks are divided into strong ties and weak ties. Strong ties refer to closely-knit groups of friends, weak ties on the other hand tie together people from different backgrounds and circles of friends. Weak ties link the network members to the broader society, while strong ties do not necessarily do so. Relationships between father and son, husband and wife, close friends, close partners are strong ties. And relationships between classmates, colleagues, or between enterprises and their agents, suppliers, financial intermediaries, government administrative departments are weak ties. In Chinese social and cultural context, entrepreneur's social networks show the following features:

A. *Relationship is Prior to the System*

In more developed market-oriented economy countries, entrepreneur's social network runs inside the legal system and market system. But in China, the social network of entrepreneurs is a separate set of social norms system, which is beyond the market system, but still attached to it. Thus, there is a double-layer relationship among the business activities of enterprises. One is the official relationship inside the legal and market system, and the other is the personal relationship outside the legal and market system. In the opinion of many entrepreneurs, it is much easier and more effective to deal with problems through the personal relationships than through the complicated official process, because personal relationship is

more direct and convenient, and costs lower. Therefore, when entrepreneurs encounter problems, most of them are likely to use their personal relationships from social networks to coordinate and solve the problems, rather than to rely on the formal legal and market system. Between entrepreneurs, there are also personal relationships. Maybe they know one another directly, or they can contact with each other through a common friend, so that they can create a cooperative relationship rather than a hostile one between each other. In this case, they can work together easily to solve the problem through negotiation, and this effective way always works for both sides.

B. Entrepreneur's Social Network is Based on The Renqing

Renqing is a special issue in China, and it is similar to a "favor" in the western world but much more complicated. Renqing is a kind of resource you can use during the social transaction, and it works as a virtual currency, such as materials, benefits, and emotions. Renqing is not only a special relationship in China, but also a special trust mechanism, and the entrepreneur's social network is based on Renqing. In fact, except the strong ties based on genetic or extremely close relationships, most of the social relationships are based on the exchange of Renqing. A relationship will be established after the Renqing exchange is confirmed. Most of the private entrepreneurs lack for inborn relationships, so the benefit from genetic relationship is rare for them. In this situation, they mainly depend on the relationship they acquired from the society by Renqing exchange. Therefore, entrepreneurs have to pay much attention to the establishment and development of relationships during their daily business activities, so that they can gain credibility and increase the emotional and material investment in dealings with dealers, customers, and government departments in order to establish social relationships beyond the pure economic relationships. This strategy can help them to build up paths to more resources.

III. THE BACKGROUND OF CHINESE ENTREPRENEUR'S SOCIAL NETWORKS

A. The Cultural Background

First of all, due to China's long-term feudal social system in the history, whose main features are centralization of state power and autocratic system, policies and regulations were developed by dominators and lacked the necessary supervision and constraints in the implementation process. In order to coordinate the relationships between various interest groups, those in power often had to lead a permissive, preferential and flexible environment for some certain groups of people. In this situation, Chinese people formed a natural sense, which made them believe that almost all systems and rules can be adjusted or betrayed because of relationships or interests. Due to the lack of credibility of official agencies, people generally agreed that the system was far less reliable than personal relationship, and credible relationships would be built based on mutual trust in familiar environment, or be built between individuals who confirmed the acceptance of Renqing.

Secondly, after two thousand years, Confucianism was deeply built into the heart of each family and individual by the imperial examination system, so it still has a huge impact on China's current culture, policy and economy. The core basis of

Chinese entrepreneur's social network is the thought and philosophy of the Confucianism, which is centered with the benevolence, said "the benevolent loves others". Seemingly, this is similar with Christian's concept, which has a significant impact on the mainstream of Western culture, but actually, there are many differences between them, and this is why the Chinese entrepreneur's social network is different from Western entrepreneur's. Although both Confucianism and Christianity advocate benevolence, the Christian assumption is the equality of all human beings; all people are the people of God, even father and son are also brothers in the eyes of God; while the Confucian assumption is the different levels of love to different levels of people. The sense of hierarchy is very strong in Chinese culture, so people here are used to divide people with ranks or grades. Although it is the love, it is different love between lieges, father and son, and even husband and wife, thus, the differential mode of association (Chaxugeju) is formed. For this reason, entrepreneurs can not make decisions rationally when facing to relevant individuals or organizations, and they naturally show favoritism based on relationships.

B. The Social Background

1)The Characteristics of Market Environment

At the beginning of the reform and opening up in China, China experienced a transition from a planned economy to a market economy, so the market system was not completely built up, the property rights system was not clear, and the laws and regulations could not be effectively implemented. In this market situation, resources were allocated unequally, and state-owned enterprises occupied a large amount of resources, while private enterprises had difficulties to access to resources, so private entrepreneurs could only get resources through the personal network of relationships. Meanwhile, the entire market lacked rational control, and the law system and political system were not good enough to prevent all illegal activities, so private entrepreneurs had the opportunities to maximize the benefit from social networks during their business activities, and created access to resources through abnormal channels in order to achieve their economic purpose. Moreover, the traditional Chinese sense of the importance of social networks matched the needs of the market environment of that period, so the private entrepreneurs quickly got the opportunity, occupied a good position in the competition, and finally made a further development.

2)The Characteristics of Enterprises

The important role of entrepreneur's social networks in the enterprise development is also determined by characteristics of the enterprises. Western scholar S. G. Redding did a deep research on the relationship between Chinese cultural characteristics and evolution of China's economic system in 1990. He summarized some of the characteristics of Chinese enterprises, including a clear decision-making power concentrated at the top, small-sized, low-level internal division of labor and specialization, existence of formal factors as well as low-level standardization (or normalization), and the strong trend of unity of ownership and decision-making power.

Due to the characteristics listed above, the information and resources needed by decision-making and implementation

process during the private enterprises' business activities depend heavily on the social networks of entrepreneurs, so it is important and urgent for private entrepreneurs to establish social networks. In addition, the Chinese private enterprises are in the infancy period of time, and most of them are medium-sized or small enterprises. Due to the lack of information, technology, capital and other resources, they can not compete with large enterprises or foreign-funded enterprises alone, so it is the only choice for them to get rid of the problems by obtaining resources, help and support through the entrepreneurs' social networks.

IV. THE POSITIVE ASPECT OF CHINESE ENTREPRENEUR'S SOCIAL NETWORKS

A. *Facilitate the Access to Resources*

Resources from official channels are extremely limited for private enterprises, so entrepreneurs' social networks provide an extra opportunity to access to resources. Entrepreneurs' social network itself is not a kind of economic resources, but a lot of social resources hide inside the network. Most of the business activities between enterprises, such as financial credit, delayed payment, and mutual aid contract orders, are based on Renqing behaviors, which rely on entrepreneurs' social networks.

B. *Reduce the Transaction Costs*

In a society whose market economy system and political system are not mature enough, the risks and uncertainties during transactions are quite large. The pattern of interpersonal interaction of Chinese people is established based on the social networks of relationships, and they build trust between each other by establishing the two-side special relationships. The more mature the relationship is, the more they trust each other, and the greater the possibility of a deal is. Such a transaction pattern can not only reduce transaction costs by saving the time for searching information, making contracts and performing the contracts, but can also control the risks and uncertainties.

C. *Provide a Shortcut for Entrepreneurs' Access to Valuable Information*

Social networks of entrepreneurs make it easier for entrepreneurs to get valuable information. Nodes in a network, which have a lot of contacts with each other, have a certain similarity and correlation with one another in business activities. Therefore, when searching among their own social networks, it is possible for entrepreneurs to find similar cases, so that they can solve the problems easier and faster. Entrepreneur's social network is also a network of information. Since everyone in this network understand each other well, it is easier to find useful information or the access channel. This process greatly saves the time of searching for information, and reduces the opportunity cost of useless information. Especially the strong ties, which include trust, cooperation and stability, create an environment with weak protection of business knowledge and technical information, in which information can be shared easily. This mechanism greatly reduces cost of the information flow, so it becomes the most accessible source of information for entrepreneurs.

V. THE NEGATIVE ASPECT OF CHINESE ENTREPRENEUR'S SOCIAL NETWORKS

A. *Reduce the Degree of Rational Decision-making*

Rational decision-making process is built on the basis of equal information resources and objective analysis. The relationship between entrepreneurs in the social networks is based on mutual trust, so entrepreneurs can not rationally identify the information obtained from the network due to the reason of feelings, emotions and other factors, or even omit the step of filtering information. When face to the strong ties, decision-making process is often easily disturbed, shaken, or influenced, so the decisions always benefit the strong ties, but not the enterprise's maximum interests. For example, when choosing suppliers or agents, the decision may be made based on the information from contacts in the social networks (including friends and relatives), but not based on rational analysis about the product quality, service or business reputation.

B. *Resulting in a Lack of Innovation*

Most people pay much attention to the strong ties, because the crowds belong to strong ties have closer relationship with them, and are more worthy of trust. However, Granovetter's research indicates that strong ties are not actually strong; on the contrary, a weak tie has the force to be seriously reconsidered. This is because that people with strong ties know each other well, and have a lot of similarities of knowledge structure, experience, background, and thinking mode, thus, they can not bring new resources or information. This kind of decision-making process based on redundant resources and information does not make much sense. However, if entrepreneurs put more effort on building up some sorts of bridges between weak ties, variable resources will be delivered and innovative decisions will be stimulated. Therefore, during decision-making process, the weak ties are actually the real "strong ties".

C. *Restrict the Process of Market-oriented Reform*

Social networks of entrepreneurs, after all, are a kind of group. Every group has the characteristic of exclusiveness. Members outside the networks and those inside the networks share unequal positions during transactions. In this case, resources can not achieve optimum allocation, which hinders the process of market-oriented reform. Additionally, there are many informal channels inside the networks, so many laws and regulations would not work as designed to maintain the market order. So it follows that powerful monopoly organizations may use its networks to monopolize the market and grab excess profits; cronyism may seriously constrains the enterprise's development and institutional innovation; collusion between business and government may hurt public welfare and economic efficiency.

VI. SUGGESTION OF THE FUTURE OF CHINESE ENTREPRENEUR'S SOCIAL NETWORKS

During the period of social transformation in China, entrepreneur's social networks played an important role on the allocation of resources and the development of private enterprises. But as the market increasingly regulated and

private enterprises gradually moving towards internationalization, the past positive aspects of the social networks of entrepreneurs become negative ones and start to restrict the further development of private enterprises.

In fact, the social network of entrepreneurs itself is not the problem. It is always a channel to access to economic resources, and can also help to reduce transaction costs and information costs. We are not suggesting to abandon the entrepreneurs' social networks in the future, but rather to retain the positive impact of social networks on the development of private enterprises. At the same time, we should pay more attention to the construction of the social and market system so as to improve entrepreneurs' social networks in a highly rational environment. In that case, the social networks with individual entrepreneurs as the nodes will develop into the ones with enterprises as the network nodes, and it will play a role in optimizing the allocation of resources in the market. Enterprises can also establish their competitive advantages through the new social networks. To achieve this aim, we should do as follows:

A. Establish a Scientific and Rational System

To solve the problems caused by entrepreneurs' social networks in China at this period, the key is to establish a scientific and rational system in private enterprises, and to implement it effectively. In the long run, enterprises can only remain competitive advantages when operating in a formal system, and the core of the system is a scientific decision-making process. By establishing a standardized and scientific decision-making process, all decisions will be made based on a series of scientific feasibility assessment, which can anticipate and help to avoid various risks, and all actions will be led by business interests. This scientific decision-making process can help to stop relying solely on entrepreneur's intuition, experience, or relationship, and to avoid the negative impact of emotions and relationships on the entrepreneur.

B. Entrepreneurs' Social Networks Should Be More Open

Derived from the traditional family networks of entrepreneurs, Chinese entrepreneurs' social networks are highly isolated. Although members inside the network are strongly related, the entire network is closed, so it is difficult to accept outsiders, to receive external information, or to share information with the outside. Rational decision-making process requires sufficient information, so that it will create greater value. Enterprise is difficult to grow bigger and stronger if it just depends on the traditional entrepreneur's social network. In the future, entrepreneur's social network should be more open, and entrance barriers should be lower, so that more resources from outside can be obtained, and furthermore, the entrepreneur's social network will develop into the credit system of the whole society.

C. Enterprises should develop core competitive advantage

At the beginning of a private enterprise's development, entrepreneurs always use their social networks to look for customers. And basically, the enterprise's development relies on the entrepreneur's personal capabilities and relationships. Business partners also commit only with the entrepreneur instead of the enterprise. However, entrepreneurs can not

always be along with the enterprises, so in order to keep on developing in a long period of time, it is necessary for enterprises to build up core competitive advantages, to enhance the positive image, to build up business reputation, and to transfer the customers' trust from the entrepreneur to the enterprises, so that the entrepreneur's social networks will become the enterprises' social networks.

D. Comply with the International Business Rules

For a long time, Chinese private enterprises are operated in a non-standard business environment, in which entrepreneurs are used to achieve economic goals through their social networks. However, during the process of internationalization, market competition will be no longer limited within a region or a country, but within a scope of global competition. In this market situation, it is unlikely to succeed if depending only on the entrepreneur's social networks. Moreover, in a more regulated market, business operations are also constrained by international rules, so private entrepreneurs have to adjust their thinking mode and business operation habits to understand how to use social networks effectively, otherwise, unnecessary losses will emerge inevitably due to the conflicts between international business rules and Chinese entrepreneurs' business operation habits.

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