

Informal Institutions, Personalism and Organisational Behaviour in the Arab World and China (Wasta and Guanxi)

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Abstract:

The aim of this investigation, as part of a doctoral dissertation, is an analysis and comparison of culture-specific and idiosyncratic governance mechanisms and social capital functions based informal and personalistic institutions in the Arab Middle-East and Chinese societies, called Wasta and Guanxi. The aim is to identify the impact of institutions shaped by high degrees of personalism on organisational behaviour, organisational learning and management as well as the compatibility of Arab and Chinese governance systems as a potential backbone for growing Chinese-Arab economic interaction.

This study is building on insights from both experimental research and institution economics which approach informal institutions based on a high degree of personalism as a crucial condition for cooperation and check on opportunism in collectivist societies replacing reliable third party enforcing mechanisms such as the rule of law.

Knowledge about the type and degree of personalism of institutions that link individuals and organisations is crucial for the development and implementation of management strategies since they impact organisational structure and learning behaviour. Through the analysis of qualitative interviews in Jordan this research aims to explore the collective action dimension of Wasta and analyse structural similarities and differences between Wasta and Guanxi. Considering the growing economic interaction between the Arab Middle East and East Asia, informal institutions and their potential compatibility could become an essential factor for future JV-strategies.

Whereas the downside of Wasta for economic development has been studied extensively, Wasta's role as a personal trust building mechanism in modern business-organisations has been mostly ignored and contradicting positions can be found in research-literature. In contrast Guanxi and its impact on Chinese businesses has experienced in-depth analysis and its trust building dimension, apart from the corruption aspect, has been acknowledged by business research literature.

This study aims to build a theoretical framework for approach informal institutions from a business-perspective in as a base for the design and implementation of management strategies. Given the growing internationalisation of some Arab economies and the ambitious targets build large-scale industrial organisations, particularly in the GCC, idiosyncratic institutions will impact the highly path-dependent process of economic development.

Key words:

Social Capital, Collective Action, Institutions, Organisational Behaviour, Trust, Management, Middle East, China

Introduction

Institutions on which social organisation in a society is based do not only vary according to their degree of formality but also reflect a society's structural development and are, especially in the case informal institutions, based on idiosyncratic processes that provide a governance mechanism. Informal institutions, which are usually operational in systems that are lacking a reliable third-party enforcing mechanism like the rule of law, are based on reputation mechanisms that punish opportunism and deviant behaviour with the loss of face and isolation within the group. Social isolation is a severe threat in the domains informal institutions where stigmatisation means the loss of all cooperation partners. Since the distribution of information about individual behaviour and trustworthiness is a cornerstone of informal institutions they require a dense and cohesive network based on face to face communication. Such networks that create the required personal trust are considered bonding social capital (Patulny and Svendsen, 2007) and consist of strong or embedded ties shaped by a high degree of personalism. Personal trust within the group is established through repeated interaction and structural embeddedness of ties which allow constant monitoring by the group. The strong degree of personalism and elaborate communication type of embedded ties are posing high marginal costs and limit the number of interaction partners. This particularistic character of informal institutions creates insecurity beyond the domain of bonding social-capital and requires building personal trust through bridging social-capital. The networking mechanisms to create such embeddedness and personal trust in bridging relations are a culture-specific process. Chinese societies are at all levels drawing on the binding power of reciprocity in Guanxi-relations. While the term Guanxi is referring to multidimensional construct that has many facets, it is a basic principle of economic cooperation in China. Despite a huge range of institutional and socioeconomic systems, which are varying from theocratic absolutist monarchies to moderately democratic republics and from economies almost exclusively based on raw-material extraction to globalised city-states with dominant service-sectors, Wasta is a feature common in all Arab societies. Initially a tribal mediation system that served as bridging social capital the role of Wasta to establish personal trust in modern business is ambivalent. Due to historical and institutional developments Wasta today in many Arab countries is used as synonym for corruption and nepotism. Within the discourse of the relevant literature contradicting views concerning the positive social-capital function of Wasta as a facilitator of collective action exist.

Depending on their degree of formality institutions are based ties with a varying degree of personalism. While purely formal and perfect institutions require no commitment relations between actors, informal institutions make the maintenance of embedded ties necessary. The degree of personalism is having a severe impact on organisational behaviour and organisational learning. Management strategies for environments of high informality and strong personalism need to take these environmental factors into account. Given the growing economic interaction between the Middle East and China and considering potential JV in the future institutions impact on organisational structure is required.

The aim of this study is to investigate into the bridging social-capital function of Wasta and to analyse structural similarities and differences between Guanxi and Wasta.

Institutions, formal vs. informal

Institutions that regulate social interaction are varying across societies according to their degree of formality. Norms, values and customs that impose constraints upon individual behaviour in social interaction are considered informal institutions. Contrary to formal institutions they are not codified neither is deviance punishable by a bureaucratic third party, be it the state or a company. Formal institutions are characterised by universality and predictability, meaning that formalised rules are available and applicable to every actor in the system, and the rules of the game are clearly defined a priori and therefore provide a reliable

Tab. 1: Formality scale of Institutions

Continuum of informal to formal social Interaction				
Degree of Formality	Institutions	Hegemonic Actors	Nature of Social Ties	Characteristics of Interaction
High: Predominantly formal interactions	Generally applicable and legally-binding laws, constitutions	State (+ supranational actors)	Law and authority	Written Communication, legally binding norms, rationality, impersonality, rigidity of rules, vertical relations
Medium-high: Mainly formal interactions	Specific articles in directives and contracts	State and corporate enterprise	Market and competition	Mainly written communication, codified norms, impersonality, vertical relations
Medium: Both formal and informal interactions	Modes of regulation of an arena	Leaders and middlemen	Negotiation and contestation	Verbal communication, socially defined codified norms, horizontal and vertical relations
Medium-low: Mainly informal interactions	Unexpressed social norms, taboos, values, customs	Community and peer-groups	Social control and identity	Practical knowledge, verbal communication, socially defined codified norms, horizontal relations
Low: Predominantly informal interactions	Personal agreements	Family and friends	Personal trust	Practical knowledge, face to face communication, codified norms, personalised trust, strong social ties, intuition

(Etzold et al. 2009)

base for interaction and ideally leave no space for opportunism. The universal character of formal institutions provide the framework for large-scale cooperation and modern bureaucracies since the high degree of codification enable the distribution of information at very low marginal costs and allow the extension of a system to almost infinite numbers of actors. (Fukuyama, 1996) Formal institutions that successfully manage to cover all aspects of social cooperation so that absolutely no information asymmetries can arise, which one actor could exploit, reduce the necessity for personalised trust and commitment relations and by that abolish transactions costs as well as opportunity costs. The assumptions of such perfect formal institutions enable perfect markets and perfect resource allocation in the neoclassical sense. (North, 2007; Aoki, 2001)

Informal institutions in contrast are shaped by a high degree of personalism and face to face interaction. The cornerstone of informal institutions as normative forces in social life is personal communication within a group and the threat of losing face and reputation as a credible cooperation partner within the collective.(Etzold, Bohle and Keck, 2009) Since informal institutions are operational in environments in which cooperation requires the establishment of personal trust and where interaction is limited to small groups of actors which maintain commitment relations due to the lack of universal rules which allow cooperation with strangers, the loss of reputation means the loss of all trading partners within the group. A condition for informal institutions to successfully pose a check on opportunism is cohesiveness. Only in well-connected, dense and cohesive groups can information about individual behaviour be transmitted efficiently, so that no free-riding can arise in a sphere of anonymity. (Blau, 2008) This requirement for personal monitoring is time-consuming and

poses high marginal costs for adding new actors to the group and by that limits the size of the group and the number of interaction partners. It is crucial for the survival of such personal monitoring systems to strictly limit the access to ingroup-status since overexpansion results in the collapse of the governance-mechanism. Consequently informal institutions reduce transaction costs within the group but impose high opportunity costs on participants. (Aoki, 2001; Granovetter, 1992; Boisot and Child, 1999)

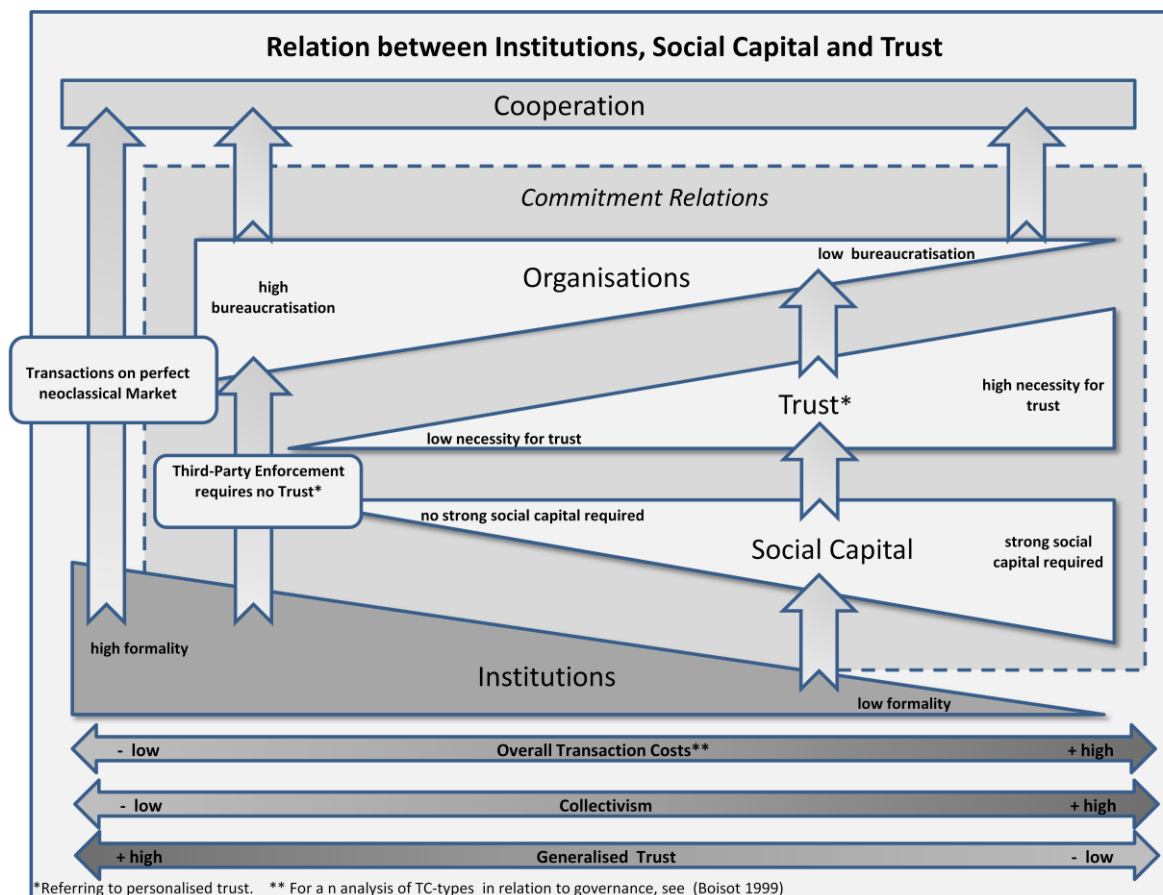


Figure 2: Institutions, Social-Capital and Trust

This particularistic character of informal institutions supplies a secure sphere for cooperation for a limited number of actors but leaves interaction between clusters of dense groups unmonitored where actors have to fear exploitation of information asymmetries. In order to overcome limited interaction partners and resulting opportunity costs, societies relying on informal institutions characterised by a high degree of personalism need to develop idiosyncratic governance-systems for cooperation beyond the secure sphere of personally monitored commitment relations or bonding social capital. Such relations, spanning across structural holes in networks, are considered bridging social capital. The function of bridging social-capital is to create personal trust and embeddedness which is neither protected through a formal nor an informal institution. Creating embeddedness and building bridging social capital is a culture-specific process and requires explicit knowledge of institutional structures. (Boisot and Child, 1999; Putnam, 2000; Granovetter, 2005; Noteboom, 2006)

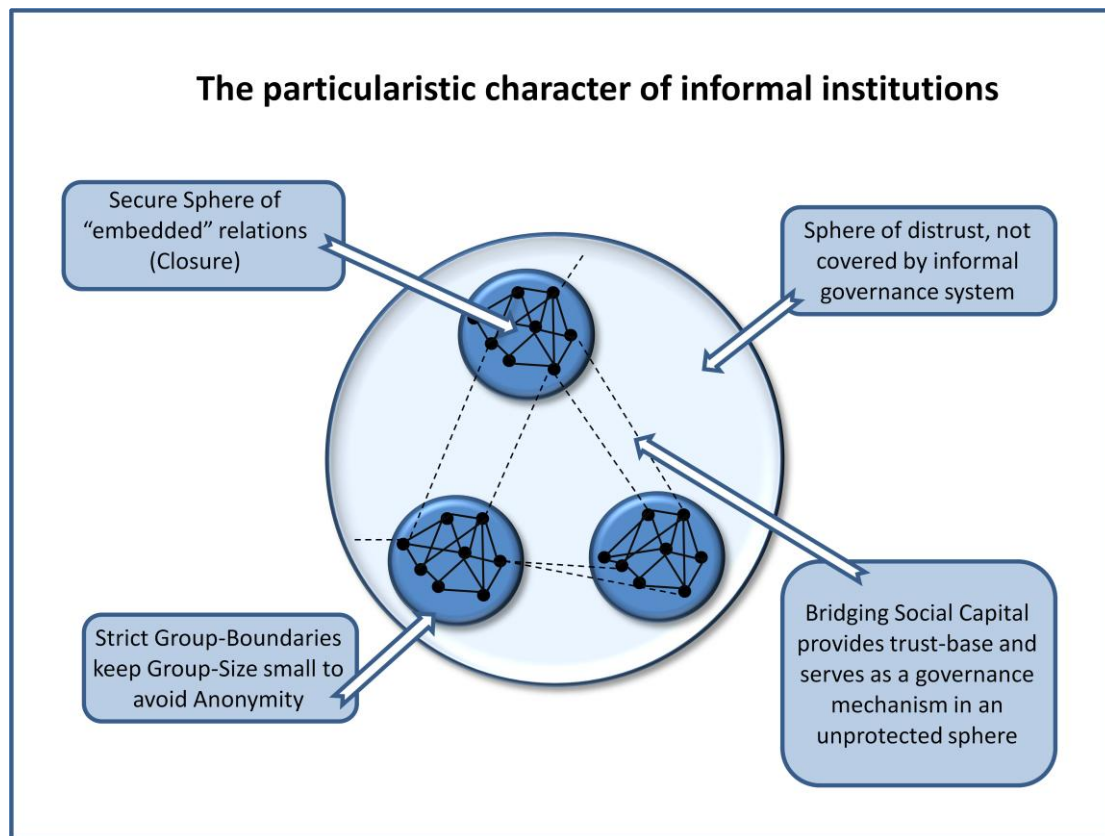


Figure 3: Informal Institutions and Particularism

Guanxi in Chinese and to a certain degree Wasta in Arab societies fulfil the role of creating embeddedness and bridging social capital. While the role of Guanxi has been studied extensively and the social capital function has been analysed, Wasta's function as bridging social-capital remains unclear. (Hutchings Kate and Weir, 2006)

Wasta

Wasta is a driving force in the Arab Middle East which impacts social and economic development in many dimensions. Despite its undisputed and omnipresent role surprisingly little research particularly from the business perspective has been carried out concerned with this issue. (Hutchings Kate and Weir, 2006; Cunningham and Sarayrah, 1993; Al-Rahami, 2008) Most studies of Wasta have approached it from a political science perspective and consequently placed it in the nepotism, cronyism and corruption domain. (Loewe, 2007) Although Wasta has traditionally served as an intertribal conflict settling mechanism and a cornerstone of Arab societies, the role of Wasta as a system to create social and structural embeddedness in the modern economies of present day Arabian countries has been underresearched. (Hutchings Kate and Weir, 2006)

The term Wasta is referring to an intercessory mechanism where one party is intervening on the behalf of a third party. In the past Wasta played an important role in settling disputes between tribes with the purpose to avoid violence in conflicts. In such a situation an honourable member of a tribe or a sheikh would negotiate on behalf of that family to find a peaceful solution in a conflict. Apart from this initial function, Wasta has developed further and the role it is playing today is somewhat diffuse and research is drawing an ambiguous picture. While most publications emphasise the corruption and rent-seeking dimension and stigmatise Wasta as a harmful practice which undermines economic development, some

authors focus on the social capital function of Wasta as an informal institution. (El-Said and Harrigan, 2009)

Although a practice called Wasta is still very common in most Arab countries the structure of this process is differing from its initial function. The conception of Wasta in most studies dealing with this issue is that of using the help of third parties to gain access to resources otherwise unattainable. Such a third party called a waseet is supporting the resource-seeker typically in situations such as dealing with authorities, getting admirable jobs or entering a prestigious university. In such cases the waseets are using their gatekeeper position and provide the desired good. Particularly in constellations where a waseet is required as a door opener dealing with authorities the role of a waseet has developed into a profession where the service of assisting to provide access is offered for payment. This abuse of power in a principle-agent setting is outright bribery and part of the harmful rent-seeking dimension of Wasta. Considering this side of Wasta it is having a very bad connotation and is considered unethical. This type of Wasta can be considered private social capital which exclusively benefits the owner instead of contributing to the public good. In this context Wasta is an institution that is utilized for rent-seeking behaviour instead of fostering cooperation and though creating wealth. As discussed above, the development of the structure of institutions is path-dependent. Although the Arab world is highly diverse in political and economic structures that have emerged, varying from orthodox Islamic monarchies with an economy based on the extraction of commodities or formerly socialist republics with a mainly agrarian economy to super-globalised city-states creating unprecedented wealth as international service hubs, patterns of a rentier-state are found in any of these systems. (El-Said and Harrigan, 2009; Weir and Hutchings Kate, 2005; Cunningham and Sarayrah, 1993; Loewe, 2007)

The rent-seeking dimension of Wasta can be traced back to several historical factors of institutional development. Since this analysis is focusing on Wasta in Jordan, only Jordanian institutional history can be discussed in detail, although most countries on the Arabian Peninsula have experienced a similar development at least until the mid 20th century when the discovery of oil began to fundamentally change the socioeconomic structures of the Gulf monarchies. The combination of societies based on tribal structures and colonial forces of various kinds from the Ottoman Empire to European colonisation anticipating and integrating the power of tribal leaders, laid the cornerstone for the development of Wasta towards its present rent-seeking function. The attempt to colonise the region has never penetrated the entire society but remained limited to urban areas and to fertile regions of agriculture with a settled population. In contrast the mostly nomadic population of arid regions basically maintained their independent regimes. Colonial powers basically limited their interaction with tribal society to negotiations with tribal leaders and delegation of power to them. This created a very powerful structural position for those members of the tribes administering the access to state-resources for their people. The government could establish their rule over the country by just securing the loyalty of a few notable tribal leaders. The assistance of sheikhs has been secured through financial subsidies, in the case of Jordan mainly funded by the British government. At a later stage this structure has reached legal recognition by inviting sheikhs to officially become members of the government to secure their privileges and by accepting the tribe as a legal administrative unit in the state. The institutionalisation of tribal customs and indigenous conflict resolution systems and securing loyalty of tribes through granting privileges access to public resources and power promoted Wasta to become a major organisational principle in Jordan. (Alon, 2007; Al-Rahami, 2008; Barakat, 1993)

Despite this development of Wasta towards cronyism and nepotism it initially grew out of custom which served to create embeddedness in a system of personal trust, social segmentation along tribal lines and informal institutions. As Sarayrah and Cunningham pointed out, the best way to tame Wasta is to limit its use to the traditional purpose it used to serve namely a conflict resolution and intertribal coordination mechanism. (Cunningham and Sarayrah, 1993) Nevertheless the function of Wasta of creating personal trust and embeddedness and by that serving as a governance mechanism for transactions beyond the

secure domain of bonding social capital within tribes is unclear. Few authors have so far approached Wasta as bridging social capital in Jordanian society and the role it plays as indigenous informal economic institutions apart from rent-seeking, corruption and nepotism has remained largely underresearched. Considering the impact of the structure of institutions on economic transactions, learning behaviour, economic development and organisational structure this issue is central to management research dealing with economies in the Arab Middle East. (Weir and Hutchings, 2005)

Personalism and Governance

Experimental research has demonstrated an impact of the availability of personal monitoring systems on cooperation rates depending on collectivist conditioning of players. (Yamagishi, 2008) Participants from collectivist societies showed high contribution rates in public good games if personal monitoring was available and free riding could be punished with a loss of reputation. Participants from societies classified as individualist, where individual reputation within the collective plays a lesser role, were not influenced by threat of stigmatisation within the group. In the absence of personal monitoring-mechanisms cooperation rates of collectivists almost collapsed. (Cook, Yamagishi and Coye, 2005) Similarly deviant behaviour and compliance to socially desired actions proofed to be significantly more depending on group-pressure in collectivist than in individualist societies. The normative function of personalistic monitoring is a cornerstone for economic cooperation particularly in developing countries where informal institutions in the past have been considered archaic and an obstacle to economic development. Recent research has in many cases identified local and idiosyncratic informal institutions based on personal monitoring as surprisingly stable, reliable and efficient systems to manage public goods. (Ostrom, 2005) Creating embeddedness and establishing in-group status in order to generate group-loyalty is crucial for successful cooperation in collectivist societies. In Chinese societies Guanxi is mechanism to create such embeddedness and to become a trusted in-group member. Successfully establishing bonds through Guanxi is required for outsiders to build the necessary personal trust. (So and Walker, 2006) To which degree social embeddedness and personal trust are required in Arab cultures and which role Wasta plays in that process remains diffuse.

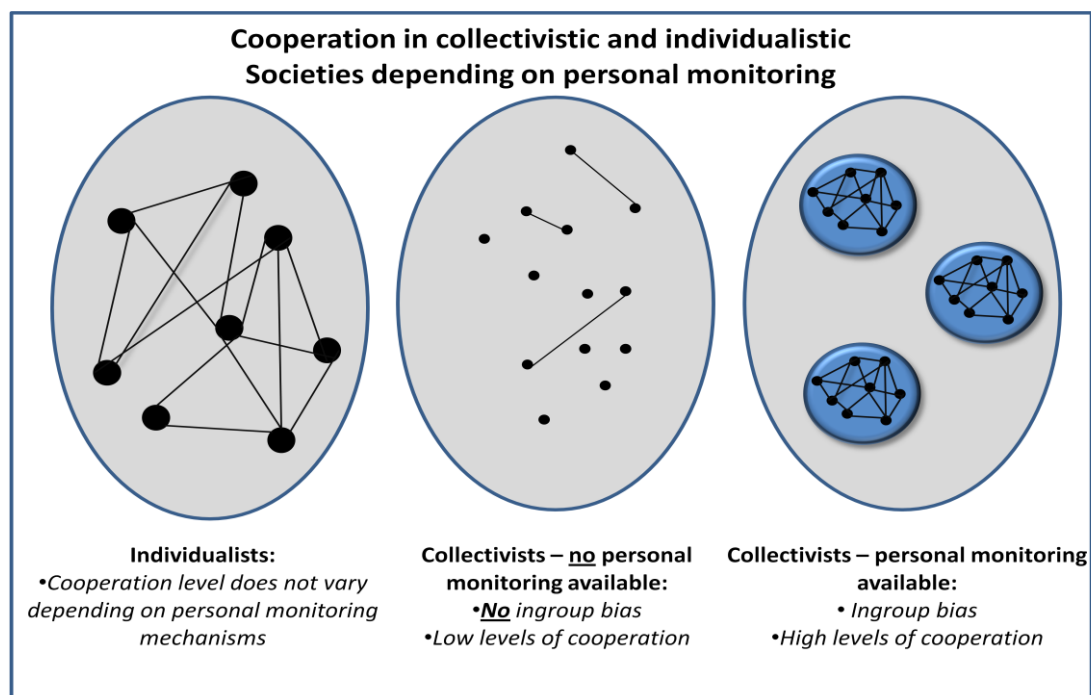


Figure 4: Cooperation: Collectivism and Monitoring

Personalism and organisational Behaviour

The degree to which companies rely on relational contracting and the degree of personalism also impacts the type of cooperation that emerges as well as organisational learning behaviour, since the type of ties that connect individuals and organisations determines the type of information that flows along them. (Granovetter, 1973; Hall and Soskice, 2004; Uzzi and Lancaster Ryon, 2003)

Arm's lengths ties, ties which are characterized by high degrees of formality and low emotional involvement favour the flow of public knowledge. Public knowledge is referring to the type of information with a high degree of abstraction meaning that it is codified and widely distributable among a large number of actors without high costs. Private knowledge in contrast is more concrete contains more information difficult to codify and is costly to transmit. (Uzzi and Lancaster Ryon, 2003; Boisot and Child, 1999) The distribution of this category of information requires embedded ties between actors. The dimension of public knowledge which cannot be abstracted and requires elaborate interaction is lost in communication based on arm's length ties. Despite the rational organisation and high degree of codification and abstraction of information in modern economies, public knowledge alone is insufficient in providing actors all the required information on the market. Uzzi and Lancaster (Uzzi and Lancaster Ryon, 2003) have demonstrated in a study of loan-markets, that private knowledge which is generated through embedded ties is a crucial factor in doing business. The dimensions of information which are not captured by formalised public knowledge can be a competitive advantage to actors on the market. Organisations maintaining embedded relations with certain actors can prove to be more flexible since the degree of abstraction of information companies are dealing with is not necessarily static. Particularly in domains of technological innovation and the process of globalisation, which is characterised by the absence of universal standards, firms might be confronted with information with low a low degree of abstraction which is difficult to process with arm's length ties. The embeddedness created through mechanisms such as Guanxi, provide organisations the base for the acquisition of private knowledge and can become pillars of corporate strategy in certain environments. (Weir and Hutchings Kate, 2005)

The requirement for network-closure (Coleman, 1988) and the limitation of network size in order to avoid anonymity in a governance system based on face to face monitoring can be a vital threat to an organisation in the sense that it is cut off from the sources of novel and diverse information. (Granovetter, 1973) While it is vital for the organisation that information within the network, about defection of individual actors, is quickly transmitted the opportunity cost for the efficiency of such a system is that new information might be prevented from entering the organisation. As briefly mentioned above, network cohesion is generally based on strong ties and the information flowing along these ties is generally old and recycled whereas the ties which provide new information from outside the group are weak ties. This referred to as "the strength of weak ties". (Granovetter, 1973) The establishment of such connections to outsiders of the tight group-structure is vital to the successful development of organisations and is an aspect of bridging social capital. The bonds established through networking systems as Guanxi do not only provide secure cooperation bases but also vehicles for individual and organisational learning in environments in which information is characterised by low degrees of abstraction. (Boisot and Child, 1999) Tapping into diverse sources of knowledge and combining the acquired information is a vital aspect of the innovation process.

Guanxi and Wasta; Similarities and Differences

While both systems look strikingly similar on the first glance they are differing fundamentally in their structure and their purposes. The most fundamental difference between Guanxi and Wasta is that Guanxi-relationships are dyadic while creating Wasta means a triadic relationship. Power-structures and social dynamics are vastly different in dyadic and triadic relationships. The structural power of the gatekeeper position makes Wasta much more prone to slide into cronyism and corruption than is the case with Guanxi. While the basic principle in establishing and maintaining Guanxi is reciprocity, this aspect seems to play a minor role in a Wasta-relationship. In Wasta no strict balance needs to be kept in order to keep it alive. The process of exchanging gifts and favours which is vital creating Guanxi is not a condition in Wasta. Traditionally creating Wasta by building trust and mediating between two parties has been considered an honour for the third party, which usually has been associated with costs for which the mediator could not expect compensation other than an honourable reputation. While gaining trust building Guanxi is required the less the two parties have in common, this causality seems not to work for Wasta. Building personal trust and maintaining Guanxi is particularly important to foreigners who are confronted with suspicion; this seems not to be the case with Wasta. Whereas personal trust needs to be established with other Arab business-partners (Western) foreigners are expected to be acting according to rational economic rules which are best dealt with written contracts and formal institutions. It is not clear if Wasta requires what in Guanxi is considered a Guanxi-base such as common ancestral background or common dialect. The role of tribal-identity in the process of building Wasta also remains unclear and needs to be investigated. (So and Walker, 2006; Cunningham and Sarayrah, 1993; Al-Rahami, 2008; Chua and Morris Michael W., 2006; Chenting and Littlefield, 2001; Kiong and Kee, 1998; Lovett, Simmons and Kali, 1999; Wellman, Chen Wenhong and Weizhen Dong, 2001; Xin and Pearce, 1996; Alston, 1989)

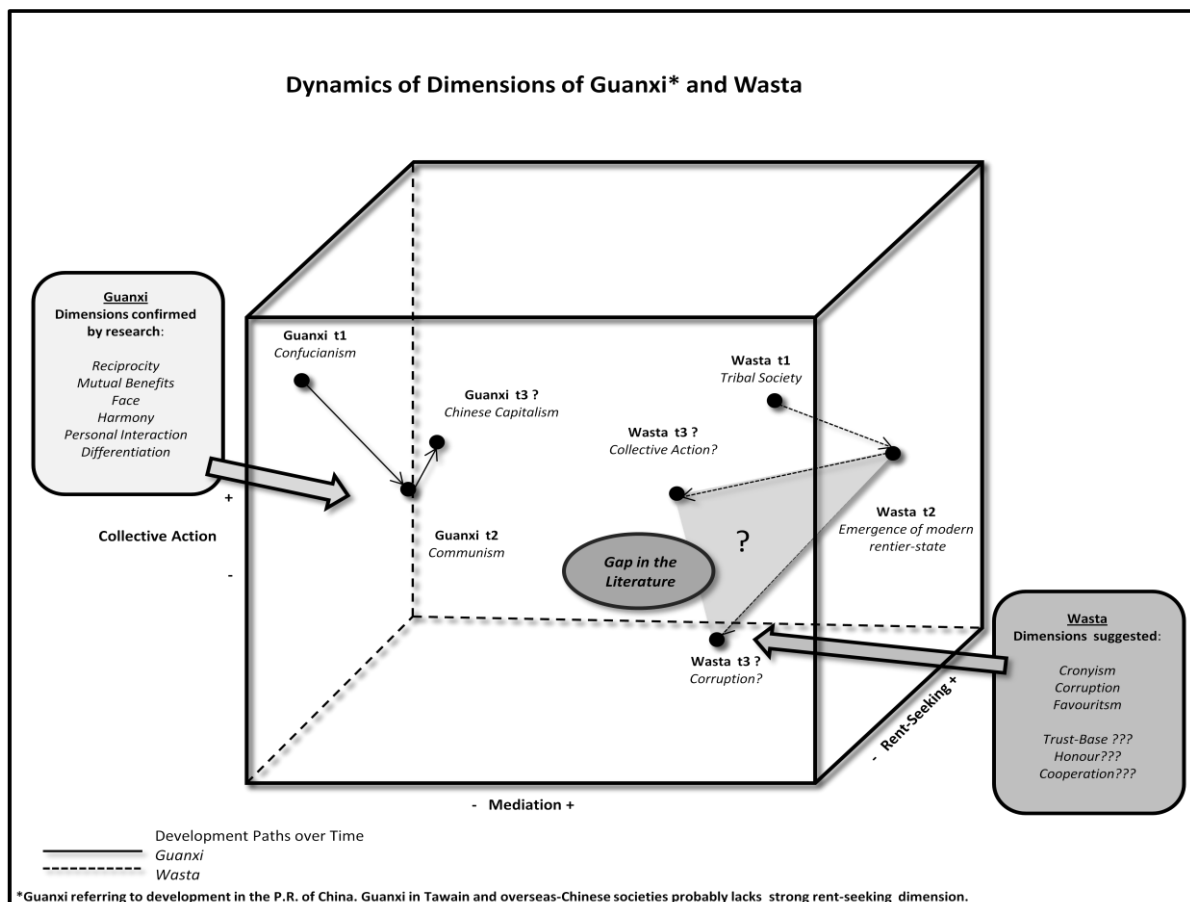


Figure 5: Dimensions of Guanxi and Wasta

Methodology

Collection of first data will be based on semi-structured qualitative interviews carried out in Jordan in September 2010. Open questions will be designed on the basis of an in-depth analysis of literature dealing with Guanxi. Previous Guanxi-literature is analysed to identify the trust-building and bridging social-capital function of Guanxi as a basis for a comparison of these two networking and governance systems. Interviews in Jordan will be carried out with local business-people and are aimed at shedding some light on the structure of a Wasta-process and its function building personal trust. The analysis of the qualitative interviews is supposed to deliver insights into the dimensionality and categories of Wasta based on which hypothesis for quantitative analysis can be formulated. Considering the little knowledge about Wasta in modern business-context, an initial qualitative study is required prior to designing a quantitative approach for a comparison of Guanxi and Wasta.

Conclusions

The presented theoretical framework is supposed to provide a basis for approaching Wasta and Guanxi as wealth-creating institutions and to further develop a theoretical model for a systematic comparison of these two mechanisms. This paper argues that Wasta should be analysed as a beneficial informal institution rather than merely stigmatise it as a local form of corruption. It furthermore proposes to develop a model for the comparison of Guanxi and Wasta. It is argued that the type and degree of personalism of the dominant institutional system impacts organisational behaviour and needs to be anticipated by management strategies. Idiosyncratic Arab management strategies and strategies for cooperation between non-Western economies will have to be designed in the future based on existing economic institutions.

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