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Homburg, Ch./ Kiedaisch, I./ Cannon, J. P.

Governance Mechanisms in Transnational Business Relationships

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Professor Dr. Christian Homburg
ist Inhaber des Lehrstuhls für Allgemeine Betriebswirtschaftslehre und Marketing I, Universität Mannheim, L 5, 1, 68131 Mannheim. Außerdem ist er Wissenschaftlicher Direktor des Instituts für Marktorientierte Unternehmensführung (IMU) an der Universität Mannheim und Vorsitzender des Wissenschaftlichen Beirates der Prof. Homburg & Partner GmbH.

Dr. Ingo Kiedaisch
ist früherer Wissenschaftlicher Mitarbeiter am Lehrstuhl von Prof. Homburg. Inzwischen ist er als Berater bei der S & K und Partner Unternehmensberatung, tätig.

Prof. Dr. Joseph P. Cannon
ist Professor für Marketing an der Colorado State University (College of Business) in Fort Collins, USA.

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ABSTRACT

Empirical research on buyer-supplier relationships has almost exclusively examined domestic (both firms from the same country) exchange. The growing importance of international marketing and global sourcing suggest a need to understand relationships across national boundaries -- transnational business relationships. Drawing on theories of governance, the authors hypothesize differences in governance between domestic and transnational business relationships. They examine the use of three specific governance mechanisms (market governance, trust, and formal contracts) commonly employed in buyer-supplier relationships. Hypotheses are tested with data from 511 purchasing professionals in the United States and Germany (201 reporting on transnational relationships). Results indicate that market governance and trust are used less in transnational than in domestic relationships. No differences are found in the use of contracts. Implications for theory and practice are discussed.

As firms expand their global sourcing and international marketing efforts, buyer-supplier relationships across borders -- *transnational* business relationships -- are becoming increasingly important. Although there is a rich body of literature on buyer-supplier relationships (Dwyer, Schurr, and Oh 1987; Gummesson 1987; Heide and John 1990, 1992), little empirical research has explicitly examined those relationships in an international context (Johnston and Spekman 1995). In a meta-analysis of the advances in international marketing, Douglas and Craig (1992, p. 297) comment on the status quo of current research on transnational buyer-supplier relationships:

> While management of buyer-seller relationships has become an increasingly important issue in many domestic markets, the complexity of buyer-seller relationships in an international context has been sadly neglected.

Cross-cultural research has provided many relevant insights, but it highlights cultural differences of business relationships by focusing on domestic relationships in different countries (e.g., Frazier, Gill, and Kale 1989; Kale 1986; Kumar, Scheer, and Steenkamp 1995a), rather than analyzing specific aspects of transnational relationships.

Only very few studies contribute to the emerging field of transnational business relationships between buyers and suppliers. Moreover, most of them are anecdotal (e. g., Reardon and Spekman 1994). Exceptions are studies by LaBahn and Harich (1995), Spencer, Wilkinson, and Young (1996), and the IMP Group (e. g., Hallén, Johanson, and Seyed-Mohamed 1987; Johanson and Hallén 1989). The work of the IMP Group is especially valuable because the researchers use domestic control groups to validate their insights on the differences and peculiarities of transnational buyer-supplier relationships.

The few studies analyzing business relationships in an international context reveal important effects of transnationality. They show that the level of adaptations is lower (Hallén, Johanson, and Seyed-Mohamed 1987, 1991; Johanson and Hallén 1989), the frequency and intensity of contacts are lower (Hallén, Johanson, and Seyed-Mohamed 1987; Johanson and

Wootz 1986), and the social distance between the exchange partners is greater in transnational than in domestic buyer-supplier relationships (Johanson and Wootz 1986).

To the best of our knowledge, the governance of buyer-supplier relationships has not been studied in the international context. Governance is a fundamental aspect of exchange relationships. It consists of the way exchange is coordinated and regulated and the processes and mechanisms used to organize and manage business relationships (Heide 1994; Mohr, Page, and Gundlach 1995). Three governance mechanisms receiving increased attention from both scholars and practitioners are market governance, trust, and formal contracts (Bradach and Eccles 1989; Mohr, Page, and Gundlach 1995; Morgan and Hunt 1994; Zenz 1994). Buying firms frequently rely on market governance by monitoring the products and prices of alternative sources of supply (Noordewier, John, and Nevin 1990). Trust develops if the partner is perceived as being honest and concerned for the customer and is an important governance mechanism of close, long-term relationships (Bradach and Eccles 1989; Ganesan 1994). Finally, business partners commonly draw up formal contracts that outline the obligations and responsibilities of each party in the relationship (Macaulay 1963; Stinchcombe 1985).

The purpose of this paper is to analyze the extent to which different governance mechanisms are used in transnational and domestic business relationships. Research of this type can contribute significantly to the emerging field of relationship marketing because it extends the scope of studies on buyer-supplier relationships to an international context. Although primarily descriptive rather than prescriptive in nature, our study is relevant to managers involved in international marketing or procurement because understanding transnational business relationships is crucial for the success of managers.

In the following section, we provide theoretical background for studying governance in transnational relationships. A key argument in the theoretical reasoning is that uncertainty plays an important role in the governance in transnational relationships. Subsequently, we propose hypotheses related to the three governance modes. We then describe an empirical study carried out in the United States and Germany, and report the results of the data analysis. Finally, we discuss implications and limitations of the study.

BACKGROUND

We selectively review theories of governance and discuss the role of uncertainty in business relationships. The two frameworks that provide guidance in the examination of governance in transnational buyer-supplier relationships are transaction cost theory and relational contracting theory. Then, we consider the unique nature of uncertainty in the context of transnational buyer-supplier relationships.

Theoretical Perspectives on Governance

Governance mechanisms or governance modes are "... those approaches employed by participants to structure and regulate their conduct in exchange" (Mohr, Page, and Gundlach 1995, p. 4). Governance is particularly important for managing complex exchanges characterized by a long time horizon and close cooperation (Bradach and Eccles 1989; Dwyer, Schurr, and Oh 1987; Heide and John 1992).

Transaction cost theory distinguishes governance by markets and hierarchies (Williamson 1979). One of the key drivers of the way exchanges are governed is the uncertainty surrounding an exchange situation (Williamson 1981, 1991). According to transaction cost theory, hierarchy is superior to market coordination under conditions of high uncertainty because market governance creates relatively higher transaction costs in such situations. A hierarchical mechanism commonly used in buyer-supplier relationships is the contract (Klein, Crawford, and Alchian 1978; Stinchcombe1985). Transactions characterized by low levels of uncertainty are governed most efficiently by markets. Hence, efficient governance requires the use of a mechanism suited to the level of uncertainty.

Although transaction cost theory provides valuable insights about governance, it does not consider social elements of business relationships. Several authors therefore have expanded the transaction cost framework with relational contracting theory and the idea of trust as a governance mechanism (e.g., Bradach and Eccles 1989; Heide and John 1992; Smith and Aldrich 1991). Relational contracting theory explicitly considers social elements -- norms -- as mechanisms governing long-term exchange (Macneil 1978, 1980). Relational norms regulate the behavior of the parties involved in commercial exchange and enhance the development of close and trusting business relationships (Kaufmann and Dant 1992; Kaufmann and Stern 1988, 1992). Trust is an important aspect of midrange forms of coordination such as business relationships: "... it should be clear that the social context as manifested in trust serves as a powerful control mechanism, just as price and authority do" (Bradach and Eccles 1989, p. 110).

Overall, the theoretical perspectives emphasize the role of costs and uncertainty in governance and the importance of three governance mechanisms: market governance, trust, and contracts. We next consider the specific problems that tend to raise uncertainty in transnational business relationships.

Uncertainty in Transnational Buyer-Supplier Relationships

In comparing international business with domestic economic activities, many authors have emphasized the manifold problems and risks that increase the uncertainty firms must face in the international arena (e. g., Cateora 1987; Klein, Frazier, and Roth 1990). As Mascarenhas (1982, p. 87) states: “If the domestic business environment can be labeled uncertain, the international business environment is doubly so.” Some sources of uncertainty affect both domestic and transnational business relationships (referred to as general sources of uncertainty), but the fact that several problems and risks are specific to transnational buyer-supplier relationships suggests that uncertainty is greater in such relationships.

One general source of uncertainty is the dynamism of the market. In the international context, a greater number of potential suppliers leads to intensified competition, which in turn leads to a higher frequency and magnitude of changes in the products, services, and technology available. For example, prices and costs change more often and more significantly in the international than in the domestic marketplace. Technologies and product quality change more rapidly because suppliers have to react immediately to competitive moves if they want to survive global competition. Additionally, the complexity of international business relationships is greater. The supply market consists of a highly diversified spectrum of suppliers that are very heterogeneous in capabilities.

For business relationships across borders one of the specific problems and risks (*international risk* in the terminology of Vernon 1983) is culture. Since Hofstede's (1980) seminal work on “culture's consequences,” problems in cross-cultural interaction have been studied extensively (e. g., Adler and Graham 1989; Anderson and Weitz 1989; Aviel 1990; Boyacigiller 1991; Ford 1984; Graham 1985; Hawrysh and Zaichkowsky 1989; Horng 1993; Kale and McIntyre 1991; Shane 1992; Törnroos and Möller 1993). Together, that body of research provides considerable evidence on the effects of culture on many facets of interaction.

Communication problems are another major concern in transnational buyer-supplier relationships. Apart from different languages, persons conducting transnational business must cope with unfamiliar verbal (Adler 1986) and nonverbal communication behavior (Bandyopadhyay and Robicheaux 1993). Further, fewer channels for formal and informal communication are present between countries than within countries (Håkansson and Johanson 1988).

Other problems specific to the transnational context are political risks (protectionism, expropriation) and economic risks, such as exchange rate fluctuations (Mascarenhas 1982). Such risks affect several marketing parameters, as shown by Rice (1984). Exchange rate fluctuations are particularly harmful for firms with a high volume of international trade activities. In addition, firms must cope with problems due to technological, social, time, and geographic distance (Ford 1984). Those aspects have been largely ignored in the literature, but are important in consideration of the specific problems that create uncertainty in the transnational context.

In summary, uncertainty apparently is higher in transnational than in domestic business relationships for two reasons. First, the general sources create a higher level of uncertainty in transnational relationships. Second, certain problems and risks are specific to the international context and need not be considered in domestic relationships. Implications for the use of the different governance mechanisms in the two contexts are discussed in greater detail in the next section.

HYPOTHESES

Drawing on theories examining governance in commercial exchange, uncertainty, and international business, we develop a set of hypotheses for each of the three governance mechanisms. We describe each mechanism, examine specific aspects of its use in the international context, and state a hypothesis about its relative use in transnational and domestic relationships.

Market Governance

In the industrial buyer-seller context of our research, market governance is reflected in the buyer's active monitoring of the supply market. Active market monitoring involves tracking the products and prices of alternative suppliers, relying on bidding processes for supplier selection, and using of multiple sources of supply. Market governance is an economic, market-related mechanism that plays an important role in many buyer-supplier relationships (e.g., John 1984; Noordewier, John, and Nevin 1990; Ouchi 1979). Interestingly, although market governance provides a foundation for transaction costs analysis, very little research has attempted to operationalize and explore it.

A buying firm faces several difficulties implementing market governance in the international context. First, international markets are less transparent than domestic markets and experience with foreign suppliers tends to be limited. Because generally less information is available about foreign suppliers and the sources of information are not well-known, active monitoring of alternative suppliers will be hampered by an information problem (Bello and Lohtia 1995). Further, the products and services of a foreign supplier may not be entirely comparable to those of domestic suppliers. In some cases only some features may differ, but in other cases a particular product may only be available from foreign suppliers. Finally, establishing an international source of supply requires the buyer to invest time and effort, which raise the switching costs and the ability to trigger the penalties inherent in the market mechanism.

Acquiring information about a foreign supplier and employing personnel acquainted with the other country both tend to be very costly. Hence, costs of market governance are higher in transnational than in domestic buyer-supplier relationships. We therefore would expect market governance to be employed to a lesser extent in a transnational context. That expectation is supported by the basic tenet of transaction cost theory which suggests market failure under conditions of high uncertainty are present transnational business relationships. Together, those arguments support the following hypothesis:

H1: The use of market governance is less common in transnational than in domestic buyer-supplier relationships.

Trust

We define trust as the buyer's perceptions of the credibility and benevolence of the supplier firm (Doney and Cannon 1997; Ganesan 1994; Kumar, Scheer, and Steenkamp 1995a). In accordance with research on interpersonal relationships (e. g., Blau 1964; Deutsch 1958; Larzelere and Huston 1980; Rotter 1967), trust has been emphasized as a vital concept in business relationships (Anderson and Narus 1986; Dwyer, Schurr, and Oh 1987; Mohr and Nevin 1990). Trust is an important social aspect of business relationships and is associated with less need for control activities (Smith and Aldrich 1991). Trust reflects an aspect of social control (Williamson and Ouchi 1981) inherent in clan-type institutions.

Although we predict that uncertainty in transnational business relationships leads to market failure, we expect the high costs of developing trust to limit the level of trust in transnational exchange. Particularly because of the cultural distance (Ford 1984) between buyers and suppliers with different cultural backgrounds, they need time to become acquainted with the differences and peculiarities that influence exchange behavior (Horng 1993). The parties are not familiar with each other's business customs and practices. Moreover, the low frequency of contact due to geographic distance (Johanson and Wootz 1986) has a negative effect on building trust (Doney and Cannon 1997). In domestic business relationships, meetings can be arranged easily and informal bonds can be built. Literature also suggests communication problems in transnational buyer-supplier relationships because of differences in both language and nonverbal communication (Bandyopadhyay and Robicheaux 1993).

Because of the importance of communication for building trust (e.g., Anderson and Narus 1990; Morgan and Hunt 1994), uncertainty in communication with a foreign exchange partner may lead to a low level of trust in transnational relationships.

H2: The customer’s trust in a supplier is lower in transnational than in domestic buyer-supplier relationships.

Formal Contracts

Formal contracts enable the exchange partners to set up and rely on formal agreements that outline their obligations and responsibilities (e.g., Gundlach and Achrol 1993; Stinchcombe 1985, 1990). Contracts are a classical mechanism for regulating exchange and “... may be used or may exist in greater or lesser degree, so that transactions can be described relatively as involving a more contractual or a less contractual manner of creating an exchange relationship ...” (Macaulay 1963, p. 56). Relational contracting theory argues that contracts prevail in discrete, short-term exchanges: “... for many modern exchanges involving longer terms and extended interaction, such as those found across many buyer-seller relationships..., such a discrete perspective is limited in its ability to provide guidance and regulate conduct of parties involved” (Gundlach and Achrol 1993, p. 141).

However, contracts provide a good basis for the settlement of disagreements that are anticipated to arise in the future. In contracts, uncertainty about the performance of a supplier can be reduced and unclear aspects made explicit. The written fixation and detailed description of obligations as well as penalties for nonperformance may help both parties overcome reservations. Our theoretical reasoning is supported by Håkansson and Johanson (1988, p. 377) who state that “... the tendency to use formal cooperation is stronger in international business as there are fewer developed channels for informal market communication between countries than in countries." Formalizing agreements with contracts helps to minimize misunderstandings that may arise with cross-cultural verbal communications.

The costs of setting up contracts are as low as the costs incurred to build trust or permanently monitor the market. Accordingly, Hawrysh and Zaichkowsky (1989, p. 32-33) claim that "... contractual language requiring specific performance and penalties in case of default is increasingly common in Japanese/American business agreements."

Formal contracts are also discussed as a substitute for integrating exchange as they establish a quasi-authority between exchange partners (Klein, Crawford, and Alchian 1978; Stinchcombe 1985; in relation to international relationships, see Haugland 1996). Contracts provide a governance mechanism that might act as hierarchy (Stinchcombe 1985). Hence, transaction cost theory would suggest greater use of contracts when the buying firm has little experience with the foreign supplier and uncertainty is high.

Overall, our arguments suggest a positive effect of transnationality on use of formal contracts.

H3: The degree of reliance on formal contracts is higher in transnational than in domestic business relationships.

RESEARCH METHOD

Data Collection and Sample

Data were collected in the United States and Germany by means of a questionnaire mailed to manufacturing firms in the chemical, mechanical, and electrical industries (U.S. SIC codes 28, 30, 32-38). Those industries were chosen because preliminary investigations indicated that they typically do a large share of business abroad. In the United States, the sample frame was drawn from members of the National Association of Purchasing Management (NAPM). The sample of German firms was provided by the German counterpart to NAPM, the BME (Bundesverband für Materialwirtschaft, Einkauf und Logistik) and the German Chamber of Commerce.

We focused on relationships in which the buying and selling organizations were both manufacturers and sales were made through direct channels of distribution. Consistent with the objectives of our study, the sampling design included both domestic and transnational supplier relationships. Transnational supplier relationships involve purchases from a supplier headquartered in another country. Therefore, the buying organizations were requested to report on either a domestic supplier or a transnational supplier in either Germany (for American buying firms) or the United States (for German buying organizations).

Pretests indicated that less than 20% of the firms conducted business with a supplier in the other country. Therefore, most of the data collection involved telephone prenotification, whereby potential respondents were screened and asked to participate in the study. Those indicating they had suppliers in the other country were asked to report on the transnational supplier with which they had most recently had contact. Buying firms that did not purchase internationally from the other country were asked to report on the domestic supplier with which they had most recently had contact. In the United States, qualified firms that agreed to participate were faxed a personalized letter and questionnaire; in Germany questionnaires were mailed. Firms not responding after three weeks were faxed or mailed a followup letter and another questionnaire.

In the United States, of the 566 firms contacted initially 370 were determined to be qualified, although 55 indicated they were either unwilling or unable to complete the questionnaire. Hence, 315 firms were faxed questionnaires, and responses were received from 227 or 61% of the able and qualified firms.

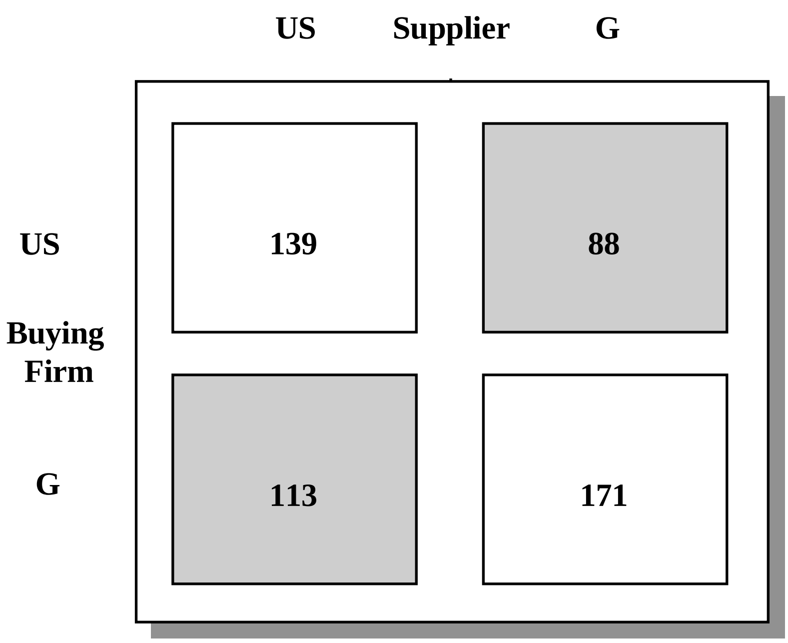
In Germany, 663 firms were mailed questionnaires without prenotification. To increase the number of transnational relationships, a second mailing list provided the names of German firms doing business with American suppliers. From that list, 521 firms were telephoned and 416 agreed to complete the questionnaire. We obtained 302 responses from the 1079 questionnaires mailed out, for an overall response rate of 28% in Germany

Altogether, 529 completed questionnaires were returned, with 227 American and 302 German manufacturing firms reporting on a supplier relationship. Twelve respondents reported a low level of confidence in their responses and were excluded from further analysis. An additional six responses were dropped because of excessive missing data. Our final usable sample consisted of reports on 511 buyer-supplier relationships.

Data collected respresented four categories of business relationships (see Figure 1): two types of domestic business relationships (American customers with American suppliers, German customers with German suppliers) and two types of transnational business relationships (American customers with German suppliers, German customers with American suppliers).

Figure 1

American and German Subsamples



Respondent competency was indicated in three ways. First, 78% of the respondents were either purchasing managers/directors or general managers/owners, whose titles indicated a high level of knowledge on the subject of the study. Second, two items at the end of the questionnaire assessed the respondents' confidence in their ability to respond to the questionnaire items and their level of involvement with the supplier. The mean ratings were uniformly high, 4.37 (confidence) and 4.32 (involvement) on a 5-point scale. Finally, almost 90% of the respondents had been involved in purchasing for more than five years. Together, the procedures and results suggested that the respondents were sufficiently qualified to act as key informants on their organization and its relationship with a supplier.

Nonresponse bias was tested in two ways. First, early and late responders were compared on several descriptive variables (e.g., experience in purchasing, number of employees at the respondent firm). Most of the late responders returned the questionnaire only after reminders. No differences were found between the two groups. Second, we compared the respondents with 85 nonrespondents (50 in Germany and 35 in the United States) who were contacted by telephone and agreed to answer four questions about themselves and their company (job title, purchasing experience, global sourcing experience, and number of employees in buying firm). We found no differences between the groups. Together the findings provide some evidence that nonresponse bias was not a problem with our data.

Measure Development and Assessment

Multi-item scales were generated on the basis of interviews with global sourcing experts and a review of the literature. The questionnaire was designed in English. To enhance translation equivalence (Douglas and Craig 1983), the questionnaire was translated into German by one person and backtranslated into English by a second person (each of whom were bilingual in English and German). The original English version and the translated/backtranslated English versions were checked for conceptual equivalence, and changes were made to the translated version where necessary. The resulting versions were then pretested and modified based on comments from purchasing managers in the United States and Germany. We either modified or directly adopted previously tested measures. In general, 5-point Likert scales with “strongly agree” and “strongly disagree” as anchors were employed.

We checked the psychometric quality of the measures by using procedures suggested in the measurement literature, assessing cross-language metric equivalence, item and scale reliability, unidimensionality, and convergent and discriminant validity (Anderson and Gerbing 1988; Bagozzi and Phillips 1982; Baumgartner and Homburg 1996; Douglas and Craig 1983; Fornell and Larcker 1981; Gerbing and Anderson 1988; Mullen 1995). The results of those analyses follow our description of the scales used to measure the theoretical variables.

Description of Measures. Market governance was operationalized as the extent to which a buying firm relies on the market mechanism to coordinate exchanges. It was assessed with five items asking the respondent to report on the use of bidding, multiple sources, and the control of prices and quality of other sources of supply. The operationalization was inspired by Noordewier, John, and Nevin (1990). Unlike other researchers, we used global items instead of items representing different monitoring procedures or items representing different aspects of supplier performance (e. g., Heide and John 1990).

For the operationalization of trust we drew primarily on the scales of Kumar, Scheer, and Steenkamp (1995a, b) and Ganesan (1994). The scale consists of six items measuring general trust, aspects of altruism, honesty, and the reliability of the supplier.

Finally, formal contracts captures the development of and referral to formalized contractual agreements in business relationships. Drawing on operationalizations by Dwyer and Oh (1987) and Cannon and Perreault (1994), we used four items to measure formal contracts. The items referred to the presence, content, and use of contracts to govern the relationship with the supplier.

Metric Equivalence. The first step in the analysis of the measures was structural equation modeling and confirmatory factor analysis to determine whether the factor loadings differred across the two different language samples. Equivalent factor loadings across the two different language versions of the questionnaire, would allow the samples to be combined for subsequent assessment procedures (Mullen 1995).

Multiple-group confirmatory factor analyses were run with LISREL 8 (Jöreskog and Sörbom 1993). The first constrained the factor loadings across the English and German language samples to be equivalent. The second allowed the factor loadings to be freed across the samples. A statistical test comparing the differences found no statistically significant differences in the factor loadings for the measures of the three governance mechanisms ($\chi^2_{diff(15)} = 21.25$; $p > .05$). The test provided strong evidence of metric equivalence across the two languages, and the two samples were combined for subsequent measure analysis.

Measure Reliability and Validity. Table 1 reports the items and summary measurement information related to the governance mechanisms. As suggested by the values, the items and scales have reasonable reliability and validity. Composite reliability of at least .6 and average variance extracted above .5 have been suggested by Bagozzi and Yi (1988). Only in the case of formal contracts is the average variance extracted slightly lower (.49) than the desirable value. The high t-values of the factor loadings indicate convergent validity (Bagozzi, Yi, and Phillips 1991). The overall fit indices show satisfactory results, with an AGFI (Jöreskog and Sörbom 1993) negligibly lower than the .9 value considered to be acceptable (Bagozzi and Yi 1988). The RMSEA meets the recommended value of .08 (Browne and Cudeck 1993). In summary, the statistics show satisfactory results.

Table 1

Measures[a] and Key Summary Statistics for Theoretical Constructs

Scale Name and Individual Items	*Composite Reliability*	*Average Variance Extracted*
Market Governance	.86	.55
We usually get more than one bid when we purchase this product.		
This supplier is our sole source for this product. (R)		
We do not even consider other suppliers for purchases of this product. (R)		
We try to use multiple sources for this particular supply.		
We often check the price and quality of other vendors of this product.		
Trust	.87	.54
This supplier is trustworthy.		
This supplier is genuinely concerned that our business succeeds.		
We trust this vendor keeps our best interests in mind.		
This supplier is not always honest with us. (R)		
We can not count on this supplier to keep its promises. (R)		
We completely trust this supplier.		
Formal Contracts	.79	.49
We have formal agreements that detail the obligations of both parties.		
We have contractual agreements that include specific penalties for non-performance.		
Our relationship with this supplier is governed by written contracts.		
We often refer to contracts to settle differences of opinion.		

Fit statistics: GFI = .91; AGFI = .87; CFI = .91; RMSEA = .08

[a] All scales are 5-point scales, with “strongly disagree” and “strongly agree” as the anchors.

(R) indicates reverse-coded items.

We tested discriminant validity by performing, one-at-a-time, chi-square difference tests between a model in which a factor correlation was fixed at 1.0 and the original (unrestricted) model. As every restricted model had significantly poorer fit than the unrestricted model, we concluded that the degree of discrimination between the two factors was sufficient. Discriminant validity was also supported by the criterion suggested by Fornell and Larcker (1981), which is based on a comparison of the squared pairwise correlations between factors with the average variance extracted for each of the factors.

To control for factors other than transnationality that might influence the governance of buyer-supplier relationships, we included sources of general uncertainty. The measures used to control for general sources of uncertainty were dynamism of product availability, dynamism of prices and cost, and product complexity. Besides uncertainty, availability of alternatives and product importance were included as control variables. Dynamism and availability of alternatives were measured with multi-item 5-point Likert scales; product complexity and product importance were measured with multi-item semantic differential scales. Home country of the buying firm, age of the supplier relationship, and customer firm size were included as additional controls. Although space limitations preclude reporting the full analysis, the measures of those constructs were evaluated by the same criteria described for the theoretical measures and exhibited good psychometric properties.

Transnationality and home country of the supplier were measured with binary variables. The dummy variables for transnationality took a value of one for a transnational relationship and a value of zero for a domestic relationship. The country dummy took a value of one for American and a value of zero for German respondents.

Data Analysis Procedure

To test the hypotheses, we used a multiple regression with two dummy variables (Hardy 1993), transnationality and home country of the buying firm. All of the independent variables were entered simultaneously as predictors of the use of market governance, the level of trust, and the degree of use of formal contracts in buyer-supplier relationships. Note that the regression coefficient of a dummy variable measures the difference in the predicted values of the dependent variable between the variable's two categories (Berry and Feldman 1985; Hardy 1993; Jain 1994) after accounting for the control variables.

RESULTS AND DISCUSSION

Hypothesis Tests

Table 2 reports the results of the multiple regression analysis testing the hypotheses. Two of three effects of transnationality are highly significant ($p < .01$). Drawing on transaction cost theory and the international marketing and sourcing literature, we hypothesized the level of market governance of buyer-supplier relationships to be lower in transnational than in domestic relationships because information about foreign suppliers is difficult to obtain, products may not be comparable, and costs associated with market governance are higher in transnational than in domestic buyer-supplier relationships. As predicted in H1, transnational business relationships were governed by the market to a lesser extent (ß = -.16, $p < .01$) than domestic ones.

Table 2

Results of Multiple Regression Analysis[a]

Independent Variables	Dependent Variables [a]		
	Market Governance	*Trust*	*Formal Contracts*
Transnationality	-.16***	-.19***	.04
Dynamism of Product Availability	-.06	-.14***	-.08
Dynamism of Prices and Cost	.23***	.02	.09*
Product Complexity	-.07	-.05	.22***
Buyer Firm Home Country	-.18***	.02	-.12***
Age of Supplier Relationship [b]	-.03	.06	-.07
Customer Firm Size (# of	.08*	.00	.16***
Availability of Alternatives	.37***	.14***	.05
Product Importance	.01	.13***	.01
F-Value/p	11.76***	6.51***	6.39***
R-Square	.27	.17	.16

[a] Standardized Regression Coefficients/significance

[b] Variable log-transformed to attenuate skewness

* p < .10

** p < .05

*** p < .01

Trust was posited to be lower in transnational than in domestic relationships. Developing trust in business relationships across borders involves higher costs because the activities involved are assumed to be more difficult and time consuming, and maintaining a good relationship requires more traveling. As hypothesized in H2, the level of trust was lower in transnational buyer-supplier relationships (ß = -.19, $p < .01$).

Contrary to H3, transnationality did not lead to greater use of hierarchy in the form of contracts between buyer and supplier in transnational relationships (ß = .04, p > .05). Perhaps certain factors reduce the usefulness of formal contracts in an international context. For example, the enforceability of contracts in an international environment may be limited. Our results suggest that the reliance on contracts is rather a function of the complexity of the product purchased, customer firm size, and buyer's home country. The higher the complexity of a product, the greater was the reliance on contracts (ß = .22, p < .01). Additionally, reliance on formal contracts was stronger in large customer firms (ß = .16, p < .01), but less pronounced in American buying firms (ß = -.12, p < .01).

Although we found several significant effects on governance mechanisms, the r-square values of the regression models are relatively low. The reason may be the lack of certain firm-specific variables in the models. For example, written purchasing policies (which are very common -- especially in German firms) would have strong effects on the governance mechanisms used in supplier relationships. Such firm-specific factors represent a different domain of variables and are outside the scope of our study. A major part of the questionnaire would have been needed to capture their content because of their complexity and heterogeneity. Against this background, the explanatory power of the regression models is considered satisfactory.

Theoretical Discussion

We address several aspects of transnational buyer-supplier relationships that have been neglected in prior studies. First, we argue that transnationality creates specific problems and risks aside from general sources of uncertainty. That differentiation is shown to be relevant as, apart from dynamism and complexity as general sources of uncertainty, transnationality has a separate and strong effect on the governance of buyer-supplier relationships.

Second, the implementation aspect of governance is emphasized. Transnationality not only creates a need for more governance, but also raises the costs of implementing the governance mechanisms in business relationships. This difficulty suggests a need for more research into other mechanisms which may be more useful in governing transnational exchange.

Our empirical study reveals a lower level of governance on an overall basis in transnational than in domestic buyer-supplier relationships. Both market governance and trust were employed less intensively in transnational relationships. However, the fact that we did not find a stronger reliance on formal contracts raises the question of whether other governance mechanisms besides the ones considered in our study are relevant for understanding transnational buyer-supplier relationships (e.g., reputation, commitment; see Anderson and Weitz 1989; Gundlach, Achrol, and Mentzer 1995; Hill 1990; Powell 1990).

Moreover, our results indicate that culture is important in studying relationships. German firms relied more than American firms on formal contracts and market governance, confirming the view that Germany has a more formal culture than the United States. Because contracts and market governance can be formalized to a high degree, which is not true for trust, trust was not affected by the cultural differences between these two countries.

The results also show that transnational buyer-supplier relationships are different from domestic buyer-supplier relationships. Hence, more international research on buyer-supplier relationships is needed. The effects of both transnationality and culture underscore the need for more empirical research in an international context. Previous empirical studies have been based almost exclusively on data related to domestic business relationships.

Managerial Implications

With the increasing importance of global marketing and global sourcing, a closer examination of transnational buyer-supplier relationships is imperative. We were able to show that transnational business relationships have different characteristics than domestic buyer-supplier relationships, even though the United States and Germany are relatively similar developed countries. Differences between transnational and domestic relationships might be greater for more dissimilar cultures and even more significant in relationships between buyers and suppliers in countries with different levels of economic development.

Practitioners must be sensitive to the unique characteristics of transnational buyer-supplier relationships. Rules and concepts applied in domestic business relationships may be misleading in a transnational context. Specifically, it is important to understand that the overall level of governance is lower in transnational relationships. Managers who are or will be responsible for building or managing transnational buyer-supplier relationships need appropriate preparation. Training activities beyond conventional language training should be the minimum preparation for interactions with foreign buyers or suppliers (Bush and Ingram 1996). Managers in charge of international marketing or global sourcing need a thorough understanding of the culture of business partners abroad.

Building and maintaining transnational business relationships as well as preparing for transnational interactions leads to idiosyncratic investments, which pay off only in the long run. Hence, management of transnational business relationships must be based on a long-term orientation. Short-term considerations do not justify the high costs and high efforts of the persons involved in international exchange processes. Building transnational business relationships is a strategic decision, and the long-term effectiveness of decisions to buy abroad to achieve short-term cost reduction, as have been made recently by many (especially German) firms, is questionable.

Limitations and Future Research

We analyzed the buyer-supplier relationships of two highly developed economies, the United States and Germany. As results by Frazier, Gill, and Kale (1989) indicate, business relationships in such countries have different features than those in less developed economies. Additionally, the cultures of the United States and Germany are only slightly different (Hofstede 1980; 1983a,b). Future research therefore should concentrate on less developed and culturally more dissimilar countries.

Another limitation of our study is that we have analyzed only market governance, trust, and formal contracts as governance mechanisms. Future studies should examine other governance mechanisms such as reputation, ownership, dependence, and commitment (Mohr, Page, and Gundlach 1995).

A third limitation is that we collected data from only one side of the dyad and from only one person, the purchasing manager (single-informant approach). Although Heide (1994) observed a significant correlation between the measures obtained from the two sides of the dyad, perceptions might nevertheless be different. Other functional managers might have a different perspective on transnational buyer-supplier relationships than purchasing managers. Future studies might analyze the extent to which perceptions of other managers confirm our results.

Finally, the time aspect of business relationships could be investigated in more detail (Dwyer, Schurr, and Oh 1987). Although we included the age of the relationship in our model, longitudinal data may be of greater value.

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