



Dr. Oecon

Governing international customer relationships

**The influences of product differentiation,
customer market attractiveness, and
relational capability**

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PART I

1 INTRODUCTION

1.1 *Background*

There seems to be a general trend in today's business-to-business markets that firms sell to a fewer number of customers, and try to form closer relationships with those that remain. A number of rationales have been attributed to this trend, including intense pressures to improve the efficiency and effectiveness of sales and procurement efforts, more intense competition, and newer management strategies such as relationship marketing, just-in-time delivery, total quality management, and strategic partnering (Cannon et al. 2000).

Paralleling this trend, great attention from a wide range of disciplines in a large number of contexts has been devoted to the following question - what makes firms form close customer relationships? In order to answer this question, a wealth of theoretical perspectives has been used, and a range of different methods have been applied. It is not the intention of this dissertation to delve into all of these perspectives, neither to review all the methods applied. Rather, basis is taken in what seems to be largely accepted within the B2B marketing literature. In order to avoid arms-length trading relationships, there are generally two approaches to follow; first, by designing long-term, detailed contracts the parties are legally bounded to each other over a long term; and second, one may strengthen the relationship by stimulating relational bonding, so that mutually accepted norms of behavior are created and maintained. The organizing and regulation of inter-firm exchanges by taking such approaches are often labeled formal and relational contracting respectively.

The most popular approach to study relationship governance seems to be the deployment of some kind of synthesis of transaction cost economics (TCE) and relational exchange theory (RET). The principal focus of TCE is on how the presence of exchange hazards increases the risk of being exposed to opportunistic behavior. In this situation, the transaction should be moved towards the hierarchy, due to its superior safeguarding,

adaptation, and evaluation capabilities (Heide 1994). In the context of interfirm relationship governance, this means that the degree of formal contracts increases. The focus of RET is on how mutually accepted norms of behavior between the exchange partners are established over time. Such norms are assumed to largely constitute the ongoing governance of the relational exchange relationship, functioning as a governance mechanism in their own right (Macneil 1980; Noordewier et al. 1990). The role of such norms is manifested in *ex ante* prescription of permissible limits of behavior and *ex post* function of reference points in case of non-compliant behavior.

The principal idea of such a dual approach to relationship governance is that it incorporates both the selfish side and the social side of human nature. By excluding either one of the frameworks, one misses important aspects of relationship governance (Macneil 1986). On the one hand, due to its emphasis on the role of more 'soft values' (Robicheaux and Coleman (1994), relational exchange theory is powerful when focusing on governance on the basis of norms and personal relations. Such issues represent an area in which TCE's explanatory power is limited due to its assumption of opportunism. On the other hand, TCE is robust when concentrating on the role of the legal contract, which affords a rough indication around which inter-firm relations vary, and an occasional guide (Llewellyn 1931) or 'safety net' (Lambe et al. 2000) if relational governance temporarily or permanently breaks down.

By using this dual approach, one has been able to accumulate a considerable body of knowledge about the conditions under which either or both of these forms of governance are deployed. However, inspection of the current account of studies leaves important matters largely unexplored. Simple empirical observation suggests that firms in the same industry use very different approaches in bringing their products to market. Yet, following TCE, which seems to be the theoretical basis of the larger number of studies, firms in the same industry should choose identical approaches in bringing their product to market, because they all face the same exogenous attributes (Hunt and Morgan 1995). Ghosh and John (1999) posited that this theoretical matter could be solved by bringing into the TCE model elements related to the firm's heterogeneous resources and strategic positioning considerations. More specifically, they posited that differences related to positioning, customer brand equity, technology, and channel resources have impact on the extent to which the firm relies on formal and relational governance in its business relationships. Their arguments were of conceptual and anecdotal character. Needless to say, such kinds of arguments need to be backed up by systematic empirical work.

Abstract

This study investigates what makes firms involve in closer relationships with their international customers. In particular, the study pays attention to how a firm's market positioning strategy and relational capabilities influence the organizing of a customer relationship. After taking basis in a synthesis of transaction cost economics and relational exchange theory, the study first explains how formal contracts and relational norms govern a supplier-customer relationship, as well as what is the principal driver behind such types of governance. Further, the study posits that variables from the strategic positioning paradigm and organizational capabilities perspective provide additional, complementary explanations when one tries to explain what makes firms raise such governance mechanisms. The study develops an integrating conceptual model that includes variables from each of the theoretical perspectives.

The conceptual model was empirically tested on a sample of international customer relationships of Norwegian, Swedish, and Finnish wood products exporters and Norwegian fish exporters. I used data from key informants in 160 exporting firms. The results show that variables from each of the chosen perspectives are important determinants for the extent to which closer customer relationships are formed. The evidence corroborates earlier research in showing that relationship specific investments are central factors, but also demonstrates that strategic positioning and organizational capability factors provide significant additional explanations in explaining formal and relational governance of a customer relationship. Managerial and theoretical implications are derived on the basis of the results, and suggestions for future research are provided.



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This dissertation follows the spirit of Ghosh and John's (1999) Governance Value Analysis (GVA) framework. It attempts to bring in elements from the paradigms of organizational capabilities and strategic positioning, and provide statistically founded answers to some of the matters raised by Ghosh and John (1999) conceptual contribution. In so doing, it is desirable to establish a relationship governance *base model*, of which the robustness has been demonstrated across different settings. Such a model may serve as a theoretical anchor on which to deduce additional effects of variables from the perspectives of organizational capabilities and strategic positioning. The effects of these variables may for example be related to (i) either or both of the dimensions of relationship governance (formal and relational contracts), as well as (ii) those governance antecedents for which the larger empirical literature shows corroborative results. This dissertation claims the importance of investigating both these kinds of influences, and presents refutable hypotheses in regards to both of these matters. Together, the results of this testing will provide statistically founded answers to each of the three questions above.

The dual model of relationship governance offers a wealth of insight to the organizing of customer relationships - but only when the characteristics of the exchange are known. But what can explain the characteristics of the exchange? In other words, what impact the level of investment in those assets that determine the size of appropriable quasi-rents? Answering this question implies treating asset specificity as a decision variable, and then as an endogenous variable in the statistical analyses (Masten 1996). Day and Klein (1987) claimed that the characteristics of the transaction reflect strategic choices made outside the confines of the TCE model. Ghosh and John (1999) built on this idea and argued that the firm's positioning considerations impact the extent to which asset specific investments are made. Simply put, different strategic positions require different levels of specific investments in the customer interface. In turn, this impacts the firm's design of the supply chain governance form (and then also its approaches to bringing their product to market). This dissertation will develop this assertion and subject it to empirical testing. While doing this, it will also be attempted to take into account the characteristics of the industry in which the customer operates. In this regard, it is proposed that the firm is more inclined to invest in a specific customer interface (and then also in turn develop and implement more advanced governance apparatus) if the market in which the customer operates has a promising future.

Williamson has repeatedly reminded us how TCE explicitly acknowledges Simon's bounded rationality theorem as one of its central fundamentals. Nevertheless, when analyzing how this theorem is applied, one realizes that the theory does not stand up to scrutiny in

regards to a range of different matters (see, e.g., Dow 1987; Demsetz 1988; Winter 1988; Hodgson 2004). For the purposes of this dissertation, there are at least two important aspects that are left outside the confines of TCE in this regard. First, TCE does not take into account the *ability* of the focal firm to develop and adopt more advanced governance apparatus in the face of higher exchange hazards. In the face of higher exchange hazards it is assumed that a governance apparatus with higher safeguarding, adaptation, and evaluation capabilities are more or less automatically adopted. The firm's ability to develop and implement such governance apparatus is taken as given. Second, assuming away the potential for misunderstandings, confusion, and cognitive matters, TCE misses the educational aspect of governance. According to Hodgson (2004), "the essential and general problem is one of interpretation. The communication of an instruction always carries the possibility of default, because it can always be interpreted in a different way" (p.409). Accordingly, a more detailed set of instructions are not only needed in order to defeat opportunism, but also to minimize the scope and effect of all potentially distorting transitions, including misinterpretations and misunderstandings. When attempting to cast light on these two matters, perspective is cast on *the firm's channel resources*. In particular, it is argued that relevant and broad experience with governing closer relationships enhances the firm's ability to develop, at less cost, a more complete set of instructions for educational purposes in order to minimize the scope and effect of (honest) misunderstandings. In this regard, refutable hypotheses will be developed, and subjected to empirical testing.

1.2 Research questions

An integratory approach to the study of inter-firm governance is certainly not new. Foss (1999) described the literature as "a bouillabaisse consisting of numerous ingredients ... combined in ways that are not always transparent" (p.1). Further, researchers "normally piece together their own toolbox, of which transaction cost economics is surely an important instrument but seldom the only one. (One might add that these eclectic exercises rarely go beyond loosely combining diverse insights; there is little theoretical development) (p.9). Needless to say, combining different theoretical perspectives is not unproblematic. The downside is that the clarity and precision in the theory's assumptions are reduced in the pursuit for more realism. The upside is the potential for new insights; it is a rather general recognition that one way in which science may make progress is by demonstrating that

seemingly opposed theories in reality are closer to each other than was immediately apparent (Laudan 1977). Hence, great attention must be devoted to how the different elements are put together, and how they are related to each other. Also, there is a need to clarify the inevitable respecifications in assumptions following an integratory approach, as the assumptions made will always be the basics of any theory (Simon 1991). This dissertation attempts to meet these requirements by digging down and put emphasis on specifying how the different constructs and accompanying logics are related to each other. Doing so will strengthen the underlying logic in the theoretical model that is to be developed and empirically tested.

In accordance with the discussion above, the model will be built in order to answer the following empirical research questions:

1. Why do firms in the same industry use so different approaches in bringing their products to market?
2. How does the positioning strategy of a firm influence the design of their supply chain governance form?
3. How do the channel capabilities of a firm influence their supply chain governance form?
4. How does the attractiveness of a market influence the firms' supply chain governance form?

The first question is indeed a broad one, and is more or less reflected in the last three. The second and third question will be answered by bringing in elements from the strategic positioning paradigm. Similarly, the fourth question will be answered by bringing in elements from the organizational capabilities paradigm.

1.3 Setting of the study and related practical business problems

This study is set in an international distribution channel context. There are a number of ways for an exporting firm to organize an international distribution channel. For example, a company may decide to establish a wholly owned foreign sales subsidiary, serve the foreign market directly from a domestic location, involve in some kind of joint venture with another company to handle the sales of the product in the foreign market, or use different types of market arrangements such as commission agents and distributors (Klein et al. 1990).

In this study, the chosen industries are the Nordic wood products industry and the Norwegian fish industry. These industries typically consist of companies that involve in larger degrees of exporting, and most of their international customers are independent, i.e., there are

no equity cross-holdings. Hence, the larger number of exporters have most often not integrated vertically into international distribution, (except the big multinational Swedish and Finnish wood products companies). This makes the relationships to their international customers crucial. In this respect, we see that the degree to which these exporters have involved in closer relationships with their international customers varies considerably (see, e.g., Bunkholt et al. 1999; Jakobsen et al. 2001; Juslin and Hansen 2003; Hammervoll 2003). Hence, the setting should be ideal to study problems that are being dealt with in the inter-organizational literature. This literature pays special attention to the governance of interorganizational relationships, and what antecedents lead to different types of governance.

Given the nature of the setting, a plethora of questions related to the supplier-customer relationship can be asked. One of the most important might be how such relationships should be organized. For example, given an exporter's market strategy as defined by what kind of products it offers, how should the exporter relate to its most important international customers? And of special importance to stay ahead of the competitive race, given the importance of getting updated information about customer preferences in an ever-changing marketplace, should the company try to develop close bonds to the customers or should it refrain from making the extra effort of involving in such activities?

Further, the products exchanged in the B2B market are often complex and require substantial coordination and collaboration to realize potential value. In this respect, given their product strategy, should the exporter make any special adaptations or investments towards a given customer in order to realize such value? What implications do such special adaptations or investments have for the organizing of the relationship?

Another question is; does the degree to which such special adaptations or investments are made also depend on the future prospects of this customer market? Intuitively, one may think that it should be better for firms with limited resources to pay more attention to customers operating in markets they regard as having bright future prospects.

Finally, what can the exchanging parties do in order to avoid misunderstandings and misinterpretations and other problems that may destroy a supplier-customer relationship? Are more detailed contracts and collaboration agreements helpful in avoiding such problems or is it enough to relate to each other only on an arms length basis?

I believe these are some of the more important practical business problems with which regular exporters are faced. This study seeks to provide answers to these problems. In so doing, relevant theoretical literature is relied on to discuss and elaborate each of these matters,

and data from the setting is collected and analyzed. On the basis of the analyses, answers are provided, and theoretical and managerial implications are derived.

1.4 Organization of the dissertation

The dissertation is divided into five main parts, of which this is part I. Part II is the theoretical part of the study. In this part, emphasis is first put on developing a solid theoretical base model. Then, perspectives are taken in the strategic positioning and organizational capabilities paradigms, from which some variables are brought into the base model in order to deduce additional effects on relationship governance. The part closes with laying out the final research model in the form of refutable hypotheses. Part III presents and discusses the methodological approach of the dissertation. Part IV contains the statistical tests of the empirical data. Part V discusses the results in terms of theoretical and managerial implications, pinpoints the limitations of the study, and, finally, draws up some suggestions for future research.

PART II

2 RELATIONSHIP GOVERNANCE

Very broadly, governance can be looked upon as a “*mode of organizing transactions*” (Williamson and Ouchi 1981). Gundlach (1994) defined relationship governance as “an encompassing phenomenon characterizing the nature and approaches employed by parties to organize and regulate exchange conduct effectively” (p. 249). Admittedly, these definitions are very broad, reflecting that there is a vast array of different mechanisms and tools on which firms rely in order to establish, structure, monitor, and enforce transactions with other firms. For example, in pure market exchanges, the price mechanism is the dominating component of the control system (cf. Stern and Reve 1980). In other forms of exchanges, firms are likely to rely on a mix of contracts, pricing and credit programs, promotional programs, merchandising aids, training programs, amongst others (Frazier 1999). In addition, socialization processes in the population have been considered part of the overall governance of exchange relations (cf. Granovetter 1985; Scott 1995). Finally, developed norms of behavior between the exchange partners have been looked upon as important governance mechanisms per se (cf. Macneil 1980). Hence, it can be concluded that relationship governance is a heterogeneous syndrome (Heide 1994). A fundamental question then arises - how should one “dimensionalize” the notion of relationship governance? In order to answer this question, a brief and selective review of the background literature is offered below.

2.1 Review of background literature

“Non-conventional” channel relationships were during the 1980s described from a perspective that focused on conflict and power (cf. Pfeffer and Salancik 1978; Frazier 1983). During the last couple of decades, the pendulum has swung towards examining the use of administrative apparatus in inter-firm exchanges. In this shift, transaction cost economics (TCE) has played a central role, focusing on how market incentives are supplanted by hierarchical mechanisms (Williamson 1991). Claiming that “its emphasis on efficiency considerations ... [makes] it

particularly useful for analyzing channel systems” (John 1984: 278), the early studies in this stream (e.g., John 1984; Dwyer and Oh 1987, 1988) investigated the impact of asset specificity and uncertainty on, amongst others, the constructs of participation, formalization, and centralization¹. These constructs may be called “administrative dimensions”. When understanding these dimensions researchers have often relied on the works of Hall (1962) and Hage and Aiken (1967) and assumed these dimensions to represent hierarchical devices in the Weberian sense. In practice this meant that they regarded them as indicators of the movement of the transaction towards the hierarchical end of the continuum in the transaction cost framework.

Paralleling this research, the TCE paradigm was repeatedly up to scrutiny, and some heavy critiques were launched towards it (see, e.g., Granovetter 1985; Perrow 1986; Dow 1987). Observing that many long-term business relationships were actually informal, non-contractual, and tacit commitments to continue doing business (Durkheim 1933; Macaulay 1963), there seemed to be indications that pure-form TCE overstated the desirability of explicit contracts, mutual investments, and full vertical integration, in the face of exchange hazards. Indeed, when making economic decisions, actors are influenced by a lot of different factors, including developed norms between the exchange partners (Macneil 1980), the social embeddedness of the transaction (Granovetter 1985), the value of the reputation for being trustworthy (Gulati 1995; Anderson and Weitz 1992), as well as prospects of continuing interaction (Hill 1990), which enlarges “the shadow of the future” (Axelrod 1984: 124). Ignoring these effects means that the threat of opportunism appears more dominant than it really is. Hence, the extent to which TCE emphasizes the role of opportunism is not likely to be realistic. This ‘flaw’ was recognized by Williamson himself in his “Markets and Hierarchies” book from 1975. In this book, norms were dimensionalized along a continuum with opportunism and stewardship on the polar ends, and some hints were given in regards to how differences in such norms would impact on governance structures (p. 26). Then, he stated that

“... norms of trustworthy behavior sometimes extend to markets and are enforced, in some degree, by group pressures. [...] Repeated personal contacts across organizational boundaries support some minimum level of courtesy and consideration between the parties [...] In addition, expectations

¹ A similar approach can be found in studies within the political economy paradigm (see, e.g., Stern and Reve 1980; Achrol et al. 1983, Dwyer and Welsh 1985).

of repeat business discourage efforts to seek a narrow advantage in any particular transaction [...] Individual aggressiveness is curbed by the prospect of ostracism among peers, in both trade and social circumstances. The reputation of a firm for fairness is also a business asset not to be dissipated” (Williamson 1975: 106-108).

However, Williamson did not follow up on this treatment in later extensions of his early work. Instead, he assumed opportunism as exogenous to the model rather than as an evolving property of the relationship as it developed over time, influenced by both internal and external influences (see Hill 1990 for an elaboration on this matter).

Ouchi (1979, 1980) extended Williamson’s framework and developed a typology in which the role of socialization processes were acknowledged, and manifested in the recognition of a “clan” governance, which existed alongside with the traditional notions of hierarchy and market governance. At about the same time, Macneil (1978, 1980) developed a relational exchange theory (RET), viewing exchanges on a continuum with discrete to relational exchanges on the polar ends. On this continuum, the discrete exchange is characterized by “sharp in by clear agreement, sharp out by clear performance” (Macneil 1974: 738), whereas the relational exchange takes on the properties of a “minisociety with a vast array of norms beyond those centered on the exchange and its immediate processes” (Macneil 1978: 901). In this mini-society, the mind-set of the decision-makers is inclined to forgo short-term payoffs and instead behave according to specialized codes of conduct or customized norms having developed over time in the relationship. This implies that the norms are to be treated as governance mechanisms in their ‘own right’ (Powell 1990). The viability of this assertion has been repeatedly confirmed in empirical studies (Anderson and Narus 1984, 1990; Palay 1984; Heide and John 1990, 1992; Anderson and Weitz 1992; Gundlach et al. 1995, Lusch and Brown 1996; Haugland et al. 2004).

On this basis, it seems that both economic as well as more relational attributes have impact on the governance of an inter-firm relationship. A fruitful approach may then be to regard inter-organizational relationship governance as consisting of at least two fundamental features, each dominated by its own logic. On the one hand, due to a risk of opportunistic behavior from the counterpart, the firm needs to protect itself by establishing contracts in which are stipulated hierarchical elements that are to be followed by law. These hierarchical elements together are regarded to constitute one side of relationship governance, and are termed “formal contracts” herein. On the other hand, extant codes of conduct between the

exchange partners developed through socialization processes also effectively regulate and control exchange behavior, though in an informal manner. This dissertation will term these codes of conduct “relational contracts”. Since the late 1980s, a significant number of empirical studies have followed this conceptualization of relationship governance (e.g., Dwyer et al. 1987; Haugland 1988; Noordewier et al. 1990; Heide and John 1990, 1992; Dahlstrom et al. 1996; Lusch and Brown 1996; Bello and Gilliland 1997; Joshi and Stump 1999a,b,c; Cannon et al. 2000; Poppo and Zenger 2002; Haugland et al. 2004). This dissertation is positioned in this stream.

Considering the fundamentally different logic on which the two types of governance rely – can they be combined into one coherent theoretical framework? Is it possible to assume that man has both opportunistic inclinations and a desire to feel socially committed at the same time? I suggest that John’s (1984) study on opportunism in inter-firm exchanges demonstrates that this is not only possible, but also a good approximation. He concluded that “opportunism can be viewed usefully as an endogenous variable that is evoked by certain antecedents within a long-run relationship. In other words, individuals may not always behave opportunistically even if conditions permit such behavior” (p. 287). Anderson’s (1988) study on antecedents to opportunism supports this conclusion. Accordingly, the behavior of man may sometimes be most appropriately described as dominated by ‘opportunistic elements’, and other times as dominated by the desire to follow social norms. Simply put, behavior of man is inconsistent. Macneil provides a deeper explanation of this issue;

“humans are – cannot otherwise be – inconsistently selfish and socially committed at the same time. No amount of close community can ever do away with this fundamental individuality; and no separation can ever do away with this living through others” (1986: 568).

Further, humans are living as half-Hobbesians, sometimes thinking like Hobbesians and sometimes not. If researchers slip into a full Hobbesian pattern of discrete thought (cf. the discrete contract), important patterns of human behavior are assumed away;

“As students of man in society, we are faced with an illogicality. Man is both an entirely selfish creature and an entirely social creature in that man puts the interests of his fellows ahead of his own interests at the same time

that he puts his own interests first. Such a creature is schizophrenic, and will ... constantly alternate between inconsistent behaviors – selfish one-second and self-sacrificing the next. Man is, in the most fundamental sense of the word, irrational” (Macneil 1983: 348)².

Accordingly, when studying the consequences of human decision making, i.e. when studying relationship governance, one has to accommodate both the ‘entirely selfish’ side, as well as the ‘entirely social’ side of man. In this study, this is done by regarding both formal contracts and relational contracts to constitute the governance of each separate exchange.

Now, the stage is set for digging deeper down into the theoretical underpinnings on which each of the two types of governance are based as well as the logic they follow. In the following, I will first present the role of formal contracts, which is associated with the TCE framework, and then the role of relational contracts, which is associated with the RET framework.

2.2 Transaction cost economics and formal contracts

According to Williamson (1985), “[c]ontractual variety is the source of numerous puzzles with which the study of the economic institutions of capitalism is appropriately concerned. Transaction cost economics maintains that such variety is mainly explained by underlying differences in the attributes of transactions” (p. 68). The principal idea is to craft governance arrangements that ensure delivery of the desired quantity, price, and quality of the supplier’s services, while simultaneously minimize the cost with which this is fulfilled. Given bounded rationality, limits are placed on the extent to which adequate contract ramifications in terms of responses to future contingencies can be spelled out ex ante. This fact has dramatic consequences. First, in situations where relationship specific investments have been made, exchange hazards are inevitable. Second, increasing degrees of environmental uncertainty will exacerbate this problem, as the relevant contingencies of the future states for which the contract is to be designed is even harder to anticipate or accurately predict (Pfeffer and Salancik 1978: 67). This gives rise to an adaptation problem. Third, if it is hard to measure performance so that rewards cannot be effectively linked to productivity (Alchian and Demsetz 1972), an evaluation problem is posed (Heide 1994). Taken together, these problems

² Notice the parallel to Granovetter’s (1985) notions of the undersocialized and oversocialized man.

constitute the extant exchange hazards. With increased exchange hazards, risk of being exposed to opportunistic behavior will rise (Williamson 1985). Following TCE logic, if the accumulated opportunistic threat of these sources is serious, the transaction will be moved towards the hierarchy, due to its superior safeguarding, adaptation, and evaluation capabilities (Heide 1994).

In distribution channel relationships, all three sources to exchange hazards are likely to figure prominently. For example, a given manufacturer may have made investments dedicated towards the customer, such as having invested in special equipment, adapted their internal procedures and logistics systems towards that of the agent, and given their sales personnel special training. Further, as markets and technologies change ever faster, it becomes harder to predict all relevant contingencies *ex ante* (Klein et al. 1990; Bello et al. 1996). Finally, geographical and cultural distances as well as increased complexity of the different markets and technologies make it difficult to confirm contractual compliance *ex post* (Bello and Gilliland 1997; Klein and Roth 1990; Anderson and Gatignon 1986). Assumingly, then, the transaction will frequently be pushed towards the hierarchy.

When trying to interpret the implications of this in the present context, one question arises - what does it mean that the inter-firm transaction is pushed towards the hierarchy? To answer this question, there is a need to separate between first-order governance mechanisms and second-order governance structures. In the original TCE framework, the dependent variable is the governance structure *per se*, i.e. the market, an intermediate form, or the hierarchy, utilized to organize a transaction. The major part of transaction cost empirical studies has followed such a design. Later, in the distribution channel literature, these forms have been considered "second-order" constructs, that manifest themselves empirically in terms of "first-order" governance mechanisms (Heide 1994; Robicheaux and Coleman 1994; Joshi and Stump 1999a). According to Heide (1994), knowledge regarding the nature of and inter-relations between these processes is still scant, but rather explained in general terms of a predominant reliance on price mechanism, bureaucratic structures, and socialization processes. The first-order governance mechanisms at focus here are bureaucratic structures in inter-organizational exchanges.

But what is meant by bureaucratic structures in inter-organizational exchanges? And how can such structures be applied in inter-firm exchanges? To better understand these matters, it is illustrative to elaborate on Stinchcombe's (1985) classic 'Contracts as hierarchical documents'. Here, it was demonstrated how contracts are deployed as governance devices when exchange hazards logic predicts vertical integration. These contracts are

constructed so that inter-firm exchanges take on the characteristics of hierarchical functioning. Hence, the risk of opportunism can be mitigated by stating contractual provisions which *produce the effects of hierarchies*. Such provisions can, for example, be in the form of more elaborate specification of promises, obligations, and processes for dispute resolution. As observed:

“A structure with legitimate authority, with a manipulable incentive system, with a method for adjusting costs, quantities, and prices, with a structure for dispute resolution, and with a set of standard operating procedures, looks very much like a hierarchy, very little like a competitive market. Yet all these features of hierarchy are routinely obtained by contracts between firms in some sector of the economy” (Stinchcombe 1985: 126).

Hence, to a variable degree, elements of a deliberate or formalized governance apparatus can be replaced for ‘the invisible hand of the market’, while at the same time acting as a functional substitute for the hierarchy. Further,

“[h]ierarchical elements” in contracts can be described as consisting of five structures: (a) command structures and authority systems, (b) incentive systems, supporting authority systems and also guiding the use of a ... [distributor’s] discretion by a structure of differential rewards partially isolated from the market, (c) standard operating procedures, which describe routines that involve action by both ... [distributors] and ... [suppliers], (d) dispute resolution procedures, partially isolated from the court system and from the market, and (e) pricing of variations in performances partially isolated from the market... Clearly, ...[this structure] is quite near to... a typical “hierarchy” (p. 156).

In regards to the ‘first order’ and ‘second order’ governance apparatus, these stipulations can be regarded to constitute the first order bureaucratic governance mechanisms. Assuming that such provisions are adequate as functional substitutes, they can be used to “describe the extent to which a market relationship has been replaced by an administrative relationship” (John and Reve 1982: 518).

Having described what it is, it is time to narrow the focus and give meaning to the construct (theoretical definition). When conceptualizing hierarchical governance, researchers have most often, more or less implicitly, taken basis in Weber's (1946, 1947) work on bureaucracy. The underlying dimensions of participation, formalization, centralization, and control, have been frequently studied as indicators of an administrative relationship, i.e., that the transaction is moved towards the hierarchy (e.g. John 1984; Dwyer and Welsh 1985; Reve 1980, 1986; Reve and Stern 1986; Dwyer and Oh 1987, 1988; Haugland 1988; Dahlstrom et al. 1996;). Formalization and participation seem to be the dominating dimensions, whereas the centralization construct does not appear to apply well in a channel context (Frazier 1999). Collectively, these studies have demonstrated that the impact of certain dimensions of the channel structure vary across channel contexts. Notably, however, is that the "area has received little attention of late and is deserving more. In the process, more attention must be devoted to the conceptual underpinnings of the elements of bureaucratic structure in a channels context... [In particular], formalization makes sense as a construct, but it must be connected to the existence of explicit and normative contracts and provides a promising avenue for future research" (Frazier 1999: 234). In the traditional literature, formalization "represents the relative emphasis on the use of rules, the 'red tape of bureaucracy'" (Hage and Aiken (1967: 73). Studies within the channel context have modified this definition of formalization to make it refer to "the extent to which written rules and procedures prescribe interfirm interaction" (Dahlstrom et al. 1996: 112). Being more explicit, the latter definition is relied on in this dissertation.

2.3 Relational exchange theory and relational contracts

In the empirical literature on inter-firm relationships, concepts such as 'trust' (Dwyer and Oh 1987), 'relational syndrome' (Noordewier et al. 1990), 'relationalism' (Kaufmann and Dant 1992), 'exchange characteristics' (Simpson 1990), and 'norms of exchange' (Reve and Stern 1986) have been popularized during the last couple of decades. This increasing impact demonstrates the role of more relation-based, non-promissory projections (Nevin 1995) in the governance of exchange relationships. Indeed, contracts are worth little if they are not embedded in social structures with significant incentives for contractual compliance and sanctions in case of opportunistic behavior (Achrol and Gundlach 1999). As Karl Llewellyn (1931) stated it:

The major importance of a legal contract is to provide a framework ... a framework highly adjustable, a framework which almost never accurately indicates real working relations, but which affords a rough indication around which such relations vary, an occasional guide in case of doubt, and a norm of ultimate appeal when the relations cease in fact to work (p. 736-737).

Hence, the importance of more relational sentiments has been recognized for a long time. According to Heide and John (1992), the 'norms' concept has been at the core of several streams of research within the social sciences ever since Sherif's (1936) early studies. This has resulted in a plethora of different definitions. Gibbs (1981) reviewed this literature and found that a consistent definition of such norms was a belief shared to some extent by members of a social unit as to what conduct ought to be in particular situations or circumstances. Later, Heide and John's (1992) predominant definition largely concurred with the one of Gibbs' (1981). They further stated that norms applied on different levels, including societies, industries, firms, and groups of individuals. Important in this context is that norms have been shown to govern individual exchange relationships (Stinchcombe 1986).

In a path-breaking study, Macaulay (1963) found that 'contracts-in-action' are largely 'non-contractual'; business persons often failed to completely formalize the terms of their transactions and rarely used legal sanctions in the ongoing adjustment or over occasional dispute settlement during relationship life cycle.

Businessmen often prefer to rely on "a man's word in a brief letter, a handshake, or "common honesty and decency" - even when the transaction involves exposure to serious risks (p. 58)

In a subsequent study, Beale and Dugdale (1975) studied negotiation behavior and confirmed Macaulay's findings in intra-industry exchanges, whereas in inter-industry exchanges the reliance on formal contracts increased (Kaufmann 1987). This should indicate that the importance of such norms varies across exchange characteristics.

Macneil (1978; 1980) further developed the implications of these findings. For him, a contract meant "no more and no less than the relations among parties to the process of projecting exchange into the future", thus making the contract more than a simple promise as is common in the traditional definition: "A contract is a promise or a set of promises for the

breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty” (1980: 4). Subsequently, he presented the rational underpinnings of this meaning, saying that all contracts are necessarily incomplete; promissory projectors are always accompanied by nonpromissory exchange projectors, such as custom, status, or habit, because promises are inherently fragmentary, and can never encompass more than a fragment of the total situation due to bounded rationality (p. 8). Using such logic he devised a continuum for categorizing exchange relationships on the basis of their contracting norms. On the one end, a discrete transaction is the typical transaction in which there is money on the one side and an easily measured commodity on the other (p. 61);

[d]iscreteness is the separating of a transaction for all else between the participant at the same time and before and after. Its ideal, never achieved in life, occurs when there is nothing else between the parties, never has been, and never will be (p. 60).

Following this logic, a discrete transaction is exclusively based upon promissory projection of exchange into the future. This type of transaction is in accordance with classical contract law, “which entails comprehensive contracting whereby all relevant future contingencies pertaining to the supply of a good or service are described and discounted with respect to both likelihood and futurity” (Williamson 1985: 69). Hence, the identity of the parties is irrelevant, their interaction is likely to be characterized as individualistic and competitive as prescribed by the attributes of economic man, and they remain autonomous throughout the ‘relationship’. I maintain that, even though this kind of exchange “is idealized fiction”³ (Dwyer et al. 1987), this type of exchange constitute a usable reference point to which otherwise ‘normal’ exchanges can be compared along different dimensions. Then, on this end, transactions are viewed as discrete. On the other end, when transactions are predominantly or exclusively based on nonpromissory projection of exchange into the future, they are characterized as relational exchange transactions. This type of transaction is based on relational contract law, whose foundation is the principle of norms. Such norms, viewed as “principles of right action” (Macneil 1980: 38) bond the exchange partners to each other and guide, control, and regulate their behavior. Hence, the contract is deeply embedded within the relationship, and

³ It is idealized fiction because “even the simplest model of discrete exchange must postulate what Macneil (1980) calls a “social matrix”: an effective means of communication, a system of order to preclude killing and stealing, a currency, and a mechanism for enforcement of promises” (Dwyer et al. 1987: 12, 14),

“contractual obligations are often modified, supplemented or completely supplanted by the norms of the ongoing relation” (Hadfield 1990: 929).

Accordingly, norms manifested in established values and agreed-upon processes largely constitute the ongoing governance of the relational exchange relationship, functioning as a governance mechanism in their own right (Macneil 1980; Noordewier et al. 1990). This is manifested in both *ex ante* prescription of behavior as well as an *ex post* function of reference points in case of non-compliant behavior. First, norms’ acceptance by contractually linked parties, as well as their harmonization with fundamental society values, makes them effective (Cannon et al. 2000) and enables them to specify permissible limits on behavior, so that deviant behavior, if recognized, is punished (Ouchi 1979; Stinchcombe 1986). This makes them capable of serving an *ex ante role* of prescribing socially accepted behavior directed toward maintaining the relationship as a whole and curtailing behavior promoting the goals of both parties (Heide and John 1992). Second, as “in a truly relational approach the reference point is the entire relation as it has developed” (Macneil 1978: 890), norms have the capacity to serve an *ex post role* in the evaluation of whether, and to what degree, a firm’s behavior is in conformity to established standards (Ivens 2002). This implies that the enforcement of obligations and expectations occurs through bilaterally socialized processes based on mutuality of interest, and where stewardship behavior has been prescribed (Heide and John 1992). The enforcement mechanism transpires when internal elements of the established norms, such as honesty, fairness, and equity, guide behavior towards that of a mutually beneficial outcome (Bello and Gilliland 2002).

Even though Macneil put down considerable effort in further developing the norm concept (1981; 1983), the fact remains that they are only discussed in general terms, such as relating them to the particular contractual behavior to which they are most pertinent. His work has resulted in a plethora of different norm dimensions along which the governance of transactions may vary (Ivens 2002), and, admittedly, he states that “[t]his cake can undoubtedly be sliced in many ways” (Macneil 1980: 40). In a review of empirical studies on governance norms in relational exchange, Ivens (2002) identified the norms of ‘flexibility’, ‘solidarity’, ‘information exchange’, and ‘long term orientation’ to be norms on which a large number of empirical studies have focused (see, e.g., Lusch and Brown 1996; Antia and Frazier 2001; Bello et al. 2003; Joshi and Stump 1999; Rokkan et al. 2003; Heide and Miner 1992; Lusch and Brown 1996; Johnson 1999; Rokkan et al. 2003).

This study seeks to examine the use of relational contracts. To this end, Gibbs’ (1981) definition is applied. A relational contract describes the extent to which the channel members

share a belief as to what conduct ought to be in particular situations or circumstances. As no particular norm is focused on in this study, it seems appropriate to create a construct which includes central elements from a number of central norms. For this purpose, one may construct a scale which taps elements from a number of different norms, e.g. those of flexibility, solidarity, information exchange, and long term orientation. This matter will be further elaborated in chapter 8.2.1.1.

2.4 Summary

It is a rather general recognition that one way in which science may make progress is by demonstrating that seemingly opposed theories in reality are closer to each other than was immediately apparent (Laudan 1977). Notwithstanding the fact that there are both compelling arguments and empirical evidence concerning the incompatibilities between legal and social governance mechanisms (see Poppo and Zenger (2002) for an overview), I argue that the preceding elaboration has shown that one may regard Macneil's relational exchange theory and Williamson's TCE paradigm to complement one another, instead of being antagonistically irreconcilable. Given that man is both an entirely selfish creature and an entirely social creature at the same time (Macneil 1983), there is a need to accommodate both types of behavior when building a theory of relationship governance. As a consequence, when following this all-embracing approach of relationship governance, it becomes important to specify the conditions under which each of the two separate approaches comes into play. Under such conditions, neither of the theories force the researcher into an either-or situation, so that the question does not become what theories to use, but, rather, to what degree and when each theory should be used (Lambe et al. 2000).

In this dissertation, emphasis will be made on making such clarifications. On the one hand, due to its emphasis on the role of more 'soft values' (Robicheaux and Coleman 1994), relational exchange theory is powerful when focusing on governance on the basis of norms and personal relations. Such issues represent an area where TCE's explanatory power is limited due to its assumption of opportunism. On the other hand, TCE is robust when concentrating on the role of the legal contract, which affords a rough indication around which inter-firm relations vary, and an occasional guide (Llewellyn 1931) or 'safety net' (Lambe et al. 2000) if relational governance temporarily or permanently breaks down.

3 REVIEW OF STUDIES ON GOVERNANCE MECHANISMS

The purpose of this chapter is to identify some central findings in the literature on relationship governance. For this purpose, a review is necessary. However, there have been done a large number of empirical studies that examine different types of antecedents to varying types of governance mechanisms, and it would be out of scope of this dissertation to review the larger number of these articles. Instead, I identify a few but central findings that are largely consistent throughout the literature. These findings may serve as a basis on which to deduce additional antecedents to relationship governance in the effort of bringing the research further. The review draws heavily on the review articles by Shelanski and Klein (1995), Rindfleisch and Heide (1997), Ivens (2002), and David and Han (2004).

Rindfleisch and Heide (1997) identified four main contextual domains within which empirical TCE studies can be classified; vertical integration, vertical interorganizational relationships, horizontal interorganizational relationships, and tests of the assumptions of TCE. There are a significant number of studies within each of these domains. Albeit theoretically related, the focus here will only be on one of these domains, that is, that of vertical interorganizational relationships. When studying Ivens' (2002) review on RET studies, one finds that these studies largely have been conducted in this same contextual domain; most studies have focused on how governance problems can be managed without common ownership.

Note that the following review is, in no way, meant to be exhaustive. Rather, the purpose is to identify some selected issues about which the empirical literature is corroborative, and some of the (many) issues about which the literature is inconclusive.

3.1.1 The safeguarding problem

The safeguarding problem revolves around the extent to which resources are deployed to facilitate a particular transaction. The logic is well-known. If one tailors one's investments to fit the idiosyncratic requirement of the particular exchange partner, cost savings are likely to accrue. At the same time, the investments made cannot be easily redeployed if the exchange relation is temporarily interrupted or prematurely terminated. Further, due to a fear that the exchange partner may opportunistically exploit these investments and incur ex post out-of-the-pocket costs on behalf of the focal party (Ghosh and John 1999), a safeguarding problem

arises. In turn, this gives the focal party incentives to set up a governance apparatus that possess the necessary safeguards. Hence, given that the threat of opportunism is non-negligible, idiosyncratic investments are a major driver behind the adoption of non-standard contracting practices (Williamson 1985).

Rindfleisch and Heide (1997) found that empirical studies provide considerable support for the hypothesized effect of asset specificity on higher degrees of hierarchical governance (vertical integration, contractual authority etc.). David and Han (2004) and Shelanski and Klein (1995) largely concurred with this conclusion. Thus, the empirical reviews largely provide support for this tenet of the theory. Hence, this tenet can be used as a foundation for further theory building.

Rindfleisch and Heide (1997) also concluded that studies have provided evidence that bilateral hybrid governance structures (norms) in combination with different unilateral governance mechanisms also appear to possess safeguarding capacities (Heide and John 1990, 1992; Anderson and Weitz 1992). Other and later studies have presented evidence that is consistent with this conclusion (see, e.g., Gundlach et al. 1995; Lusch and Brown 1996; Bello and Gilliland 1997; Cannon et al. 2000; Bello et al. 2003; Haugland et al. 2004). This supports the assertion that relational contracts can be framed as a governance mechanism in their own right. Hence, this tenet may then also function as a fundamental building block for further theory building.

In regards to opportunism, Rindfleisch and Heide (1997) concluded that the studies seem to provide only mixed support for the assumption of opportunistic actors. David and Han's (2004) review supports this conclusion. Hence, John's (1984) and Anderson's (1988) findings, that opportunism may be usefully viewed as an endogenous variable rather than something that is exogenous to the theoretical model, appears to be a viable assumption in future research. Considering opportunism as a variable also fits nicely with Macneil's claim that man is both 'entirely selfish and entirely social' at the same time (1983; 348). In short, the extent to which it is perceived that the counterpart may act opportunistically depends on a number of factors, of which the transaction characteristics are only some of many. Hence, it is more viable to consider opportunism as a variable and not outside the frame of reference in exchange models.

3.1.2 The adaptation problem

Another issue to which Williamson has given great attention, is the adaptation problem. The central tenet is that governance structures differ in their abilities to respond to external disturbances. The central variable is environmental uncertainty, which is defined as “the degree to which future states of the world cannot be anticipated and accurately predicted” (Pfeffer and Salancik 1978: 67). A more context-specific definition is the degree to which “unanticipated changes in circumstances surrounding an exchange” (Noordewier et al. 1990: 82).

Higher levels of environmental uncertainty give rise to difficulties with modifying or adapting agreements to changing circumstances. In cases where the degree of asset specificity is trivial, this does not represent any problem because continuity matters little, and new transaction arrangements can easily be arranged by either party if necessary (Williamson 1985). However, in cases where asset specificity is present to a non-trivial degree, continuity matters, and it becomes more important for the exchange partners to adopt a governance arrangement with adaptive capabilities. Higher uncertainty increases difficulties with specifying responses to future circumstances *ex ante* makes it “more imperative that the parties devise a machinery to “work things out”- since contractual gaps will be larger and the occasions for sequential adaptations will increase in number and importance as the degree of uncertainty increases” (Williamson 1985: 60). In such situations, TCE maintains that the relative attractiveness of more vertical structures increases because they are better able to absorb distortions and curb costly haggling and maladaptiveness.

The empirical literature provides mixed support to the effect of uncertainty on governance form. For example, environmental uncertainty has been found to be positively related (e.g. John and Weitz 1988; Levy 1985), not related (e.g. Maltz 1994; Anderson and Schmittlein 1984), and negatively related (e.g. Aulakh and Kotabe 1997; Klein 1989; Balakrishnan and Wernerfelt 1986) to either vertical integration or hybrid forms of governance. Accordingly, Rindfleisch and Heide (1997) concluded that “the role of governance as a means of adapting to uncertain environments receives mixed support from the studies in [their] review” (p. 45). David and Han (2004) concurred with this conclusion; “there does not seem to be a clear relationship between uncertainty and either the choice of governance form or the level of transaction costs” (p.52). In their meta-testing, there seemed to be no direct effects of uncertainty on the choice of governance. Of the studies that

explicitly tested the interaction effect between asset specificity and uncertainty, the results were still mixed, providing 50% support.

Considering that my purpose with this brief review was to identify findings that are largely consistent across settings, the effect of environmental uncertainty on the choice governance is clearly not an appropriate candidate. When bringing in elements from other perspectives, some firm ground is needed. Hence, it is not apt to use this tenet of TCE as a basis on which to deduce and test additional effects.

3.1.3 Relational contracts – as an antecedent and as an outcome

In chapter 2, it was explained how social norms have the capacity to function as both an ex ante role of prescribing socially accepted behavior, as well as an ex post role in the evaluation of whether, and to what degree, behavior conforms to established standards. Hence, social norms have the capacity to function as governance mechanisms in their own right. Considering them as such, a number of studies have demonstrated that such norms have safeguarding capacity, i.e. that they are positively related to the degree to which asset specific investments have been made (Heide and John 1990, 1992; Anderson and Weitz 1992; Gundlach et al. 1995; Lusch and Brown 1996; Bello and Gilliland 1997). Further, Haugland et al. (2004) found that such norms were positively related to the extent to which ‘soft’, but specific, investments had been made in the relationship.

But for what type of exchange transactions are (different types of) social norms particularly useful? In general, RET are most concerned about the problems caused by the continuity of business relationships (Ivens 2002). Norms between exchange partners develop over time, and exist alongside with any formal contracts. But when it comes to which type of exchanges norms are particularly beneficial, the literature does not offer much guidance. Neither does it say much about which type of norms arise in response to different circumstances. Rather, the norms of ‘flexibility’, ‘solidarity’, ‘information exchange’, and ‘long term orientation’ seem to be the most commonly used.

Empirical studies have focused on a number of different aspects, and reached largely conclusive results in regards to the positive influence of norms on outcomes perceptions (Kaufmann and Stern 1988; Doney and Cannon 1997; Jap and Ganesan 2000) as well as on outcome behaviors (Dant and Schul 1992; Dwyer 1993; Gundlach et al. 1995). There seems

to be evidence, then, that a certain degree of norms is desirable in order to enjoy potential benefits of the exchange relation.

However, when considering the effect of norms on some relationship or firm level variables, for example in regards to relationship performance, there are mixed results (see, e.g., Noordewier et al. 1990, Lusch and Brown 1996; Bello and Gilliland 1997; Cannon et al. 2000). Mooi (2005) provides a possible explanation to this confusion. He found very strong norms were not beneficial for the relationship, because this would curb the objectivity of the partners to evaluate new possibilities, thereby forgoing new, and potentially big, earnings, whereas exchange relations with weak norms between the parties were typically also characterized by high degrees of opportunism. On this basis, considering the empirical evidence, it seems that only a certain degree of norms is desirable between exchange partners. Some readers may however find this conclusion controversial.

Different types of antecedents have been studied. For example, Heide and John (1990) and Bello and Gilliland (1997) studied the effect of environmental uncertainty, Lusch and Brown (1996) studied the effects of relationship duration and dependence structures, and Bello and Gilliland (1997) studied the effect of human investments. Ivens et al. (2002: 12-13) provides an overview of the different types of antecedents that have been studied. He concludes that “the knowledge generated by these studies must be qualified as fragmentary”. Hence, it is very difficult to draw any specific conclusions about any central antecedent of norms that I can bring with me in the building of a model.

In regards to future research, the literature on relational contracts largely appears too fragmented to use as a base for future research. One exception can be made, however; the results are largely corroborative in regards to the safeguarding capacity of norms. Also, one might make an exception for the desirability of norms between the exchange partners.

3.1.4 Summary

To sum up, the selective review demonstrates that great confusion exists in regards to the effect of environmental uncertainty on governance (the adaptation problem), whereas the norms literature, although promising, generally appears too fragmented to use as a solid basis for deducing additional effects. In regards to some other matters, however, there seems to be considerable consistency. First, higher degrees of relationship specific investments generally lead to more vertical integration, or, alternatively, higher degrees of formal contracts. Second,

although more stringent TCE-adherents may find this conclusion hard to accept, the empirical literature seems to suggest that asset specific investments are related to higher degrees of bilateral governance mechanisms. Third, there are strong theoretical reasons to regard opportunism as a variable and not as something which is exogenous to the theoretical model (see chapter 2), and this assertion receives support by the empirical literature. It should be noted in passing that, as discussed in chapter 2, the latter gives support to treating relationship governance as being dimensionalized by formal and relational contracts. Indeed, some studies have demonstrated that formal contracts and relational sentiments function as complements, and can be regarded as independent governance mechanisms (Poppo and Zenger 2002; Cannon et al. 2000)⁴. This assertion is also backed up by a significant number of empirical studies that have demonstrated the robustness of such a dual model of channel governance (see, e.g., Palay 1984; Heide and John 1992; Lusch and Brown 1996; Dahlstrom et al. 1996; Cannon and Perrault 1999; Jap and Ganesan 2000; Haugland et al. 2004). Finally, it seems that established norms between the exchange partners are generally desirable, as it is positively related to outcomes perceptions, outcome behaviors, and, for the most part, some relationship or firm level variables such as relationship performance.

The consistency in the literature in regards to these matters gives me confidence to bring them further and use them as a foundation on which to bring in additional constructs from other theoretical camps. In other words, having established a robust foundation of (i) how relationship governance is conceptualized into formal and relational contracts, as well as (ii) what seems to be the major factor (asset specificity) influencing these types of contracts, one may import constructs from other perspectives and posit them to influence one or more of the elements in this base model. Either, one may posit these imported constructs to influence one or both of the relationship governance dimensions, or one may posit them to influence the level of asset specificity. The logic of the base model is then taken as a theoretical anchor. This is likely to make it easier to clarify how constructs from different theoretical perspectives relate to each other. This will be the focus of the next chapter.

⁴ See Bradach and Eccles (1989) for a conceptual elaboration on this matter.

4 ALTERNATIVE PERSPECTIVES ON RELATIONSHIP GOVERNANCE

A distinct characteristic of the research on inter-firm relations is that it is broad-ranging. Scholars from widely different disciplines have brought in their theoretical tools, having different foci and different purposes. The focus of this work is antecedents to formal and relational governance. Having this purpose, it is positioned in a tradition of a large number of studies that have combined various elements from one or more of the economic organization disciplines, as well as elements from some other disciplines.

The empirical support of its most central tenet (see last chapter) makes it possible to apply this part of TCE as a theoretical anchor for deducing additional effects on either the dimensions of relationship governance or on those of its antecedents for which empirical support has been found. Indeed, such contributions are needed; “TCE is appealing, but very narrow as currently developed. Constructs other than specialized investments, environmental uncertainty, and performance ambiguity will, no doubt, influence transaction costs, that is the costs of governing exchange relationships” (Frazier 1999: 232). In order to identify those ‘other constructs’, one may get inspiration from some of the critiques of the TCE literature. This literature is large, and virtually all aspects of the TCE framework are, in some way or another, heavily criticized. Hence, I concentrated on the critiques that identified other sources of impact while at the same time acknowledged the fundamentals of TCE. For this matter, the seminal paper by Ghosh and John (1999) was considered to be one of the top candidates. After having reviewed the TCE literature and established that its most central tenets hold, they concluded that “the effects of strategic choices and heterogeneous resources of firms on the alignment of exchange with governance are conspicuously absent in the standard TCA model” (p. 135). Fusing TCE with RET to cover both formal and relational governance of inter-organizational relationships does not relieve the resulting governance model from this deficiency, because RET only addresses how (and to a certain degree why) the two exchanging firms relate to each other on the basis of norms.

In the following two alternative perspectives on relationship governance will be brought in. First, I will take an outside-in perspective and develop theoretical arguments in regards to how (i) the attributes of a given industry structure and (ii) the product positioning strategies are important when studying relationship governance. Second, I will take an inside-out perspective and devote particular attention to the firm’s abilities to ‘master the art of cooperation’ (Day 1994).

The author is aware that great challenges and intricacies must be dealt with when trying to integrate perspectives. In the pursuit of clarifying the underlying issues, the following discussion will largely have a conceptual character. This decision was made due to a desire to meet Foss' (1999) critique. He noted that in the literature on inter-firm relations "the perhaps dominant theoretical approach to the study of inter-firm relations ... is a bouillabaisse consisting of numerous ingredients [and] these ingredients are combined in ways that are not always transparent " (p. 1). Further, researchers "normally piece together their own toolbox, in which transaction cost economics is surely an important instrument but seldom the only one. (One might add that these eclectic exercises rarely go beyond loosely combining diverse insights; there is little theoretical development)" (p. 9). Hence, there is a need to dig down and investigate in what way the various perspectives can be combined, and how the different logics and constructs relate to each other. This will be done in the next two sections (chapter 4.1 and 4.2).

4.1 Strategic positioning

In the following, I will first briefly present the industrial organization (IO) paradigm, with a particular emphasis on Porter's (1980) contribution. Second, I will demonstrate the complementary value of TCE and the strategic positioning perspective.

4.1.1 Industrial organization and Porter

The field of industrial organization is the field within economics which has dealt with the structure of the market, the behavior of firms operating in that structure, and the costs associated with various forms of market structure and firm behavior (Teece 1984). The most visible of the theoretical schools within this field is the structure-conduct-performance (SCP) paradigm, to which Mason and Bain gave the most important early contributions. This tradition claims that industry structure (e.g., number of buyers and sellers, the degree of product differentiation, the degree of entry barriers) determines firm conduct (pricing practices and policies, tacit and overt inter-firm coordination and cooperation, R&D commitments, advertising etc), which in turn determines economic performance (profitability, efficiency) (see, e.g., Scherer 1980). The causality runs from structure to conduct to

performance. In reality, however, industry structure is hold as the critical factor from which both firm conduct as well as performance can be explained (Teece 1984). The focus of the theory was to increase profits of the individual firm through the exercise of market power, implying that a relatively greater deadweight loss is imposed on society.

Porter (1980) developed the IO paradigm further. He outlined a framework to analyze the performance of an individual firm as a function of its positioning within a particular industry given the industry's specific characteristics. The book paid special attention to how structural forces make up the competitive intensity in a market, and how the forces impact firm performance;

The goal of competitive strategy for a business unit in an industry is to find a position in the industry where the company can best defend itself against these competitive forces or can influence them in its own favor. ...Knowledge of those underlying sources of competitive pressure highlights the critical strengths and weaknesses of the company, animates its positioning in its industry, clarifies the areas where strategic changes may yield the greatest payoff, and highlights the areas where industry trends promise to hold the greatest significance as either opportunities or threats (Porter 1980: 4).

Hence, as in the traditional IO paradigm, the principle purpose of Porter's (1980) model was to draw up a normative theory for firm profit maximization, by trying to build market power to its own benefit. Furthermore, given that the characteristics of the industry determined the competitive rules of the game, these characteristics also provided the strategies potentially available to the firm. Porter (1980) identified a typology of generic strategies (cost-leadership, differentiation, or focus)⁵, from which firms should optimally choose and implement only one in their pursuit for maximizing performance.

A short description of each of these generic strategies is needed. When following a cost leadership strategy, the firm strives to produce products at less cost than its competitors. The focus is to cut costs wherever possible, and sell standard high-volume products. The aim of the differentiation strategy is to create a product that is perceived as uniquely attractive. Important factors are strong marketing abilities, reputation for quality, high-quality products,

⁵ Note that this typology is only one among a number of typologies suggested in the literature. Other typologies of strategy are for instance the ones by Miles and Snow (1978), McGee and Thomas (1986), and Miller (1986).

and strong cooperation from marketing channels. When following a focus strategy, the firm is concentrating the attention on some specific type of customer, product or geographic locale (Miller 1986).

The Porter typology has served the basis for a large number of empirical studies. Assuming that the industry forces determine the rules of the game, and in turn the strategies available to the firms, most of the studies have tried to identify a link between environment, strategy, structure, and performance. In particular, significant theoretical and empirical attention has been devoted to (i) the link between generic strategies and performance (Hambrick 1983; Snow and Hrebiniak 1980; Douglas and Rhee 1989; Miller and Friesen 1986; Miller and Friesen 1986), (ii) the type of environmental conditions under which different types of competitive strategy are most successful (White 1986; Miller 1988; Davis and Schul 1993), and (iii) what kind of organization seems to be associated with each strategy (Miller 1986; White 1986; Douglas and Rhee 1993). An important theoretical tenet that has been empirically thoroughly investigated was that a match between the chosen strategy and organization structure should imply higher performance. However, this empirical research has been exclusively focused on the *internal* structures of the firm (Lassar and Kerr 1996). A typical example is Miller's (1986) synthesis of how different kinds of organization structures facilitated a particular strategy. The nature of the firm's relation to other companies is generally not given any attention.

Considering the increased popularity of close B2B-relationships, which has actually been one of the major industry changes during the last decades (Keep et al. 1998), there is a need to regard such arrangements as an important dimension to which companies need to relate their competitive strategy. Accordingly, the research on generic strategies ought to be extended to explain how such considerations relate to the inter-firm governance apparatus that have been, or should be, raised.

4.1.2 The complementary value of industry positioning analysis to the TCE framework

The following discussion will be of conceptual character. It is organized in three sections. The first two sections identify and explore the ramifications of two suspicious practices in traditional TCE empirical work, as well as indicate how these problems can be dealt with. The first section focuses on the failure to taken into account environmental factors. The second

section addresses the treatment of transaction characteristics as exogenous factors. The third section demonstrates how the adding of elements from strategic perspective to the TCE framework may alleviate the model from these problems.

Suspicious practice no. 1: The neglect of competitive factors.

A suspicious practice within the TCE channel literature is that competitive factors are generally not considered explicitly; “[n]oticeably absent is any concern for competitive factors. Strategic behavior, whose objective is to avoid competition or rivalry, is relegated by Williamson (1985) to a role only in cases of dominant firms or tightly oligopolistic industries” (Day and Klein 1987: 55).

Consider the following example of how competitive factors are missed in the TCE framework, and subsumed in some higher-order constructs. A central logic within the TCE framework is that of the fundamental transformation, the causal chain of which is well known; when the focal party makes a transaction specific investment, this party needs to raise appropriate safeguards of this investment due to increased risks of being exposed to opportunistic behavior. What was before a competitive market (a ‘large number condition’ because the identity of counterpart is irrelevant) has now been fundamentally transformed to a bilateral monopoly (a ‘small number condition’ because the identity of counterpart is crucial) through investments made during contract execution (Williamson 1985: 12). Hence, Williamson adopts a structural perspective in which a ‘small numbers bargaining’ argument plays a pivotal role, although in the after-math of asset specificity.

In effect, the nature of the industry structure is reduced to having a supportive role to the overall theoretical argument of TCE. Either the structure is a perfectly competitive market in which no particular safeguards are required, or the structure has been transformed to a bilateral monopoly so that safeguards must be raised. In a sense, then, the TCE framework endogenizes the structure characteristics, because the (part of) industry structure at which focus is placed (the inter-firm relation), changes from a perfect market to a bilateral monopoly when the firm makes an investment. I assert that this logic is suspiciously myopic and misses important aspects of the industry structure per se. For example, what happens if the market has a very promising future or if the market is perceived as fiercely competitive? Will such industry characteristics have any effects on the degree to which the firm makes investments in the market or adopts more advanced governance apparatus? And, of prime importance in this context, will such forces impact the extent to which the firm enters closer vertical relationships, for example in order to secure a stable supply of products or capture better

intelligence about market and technology? Such considerations reflect *competitive behavior*, which is the focus of the strategic positioning paradigm. Unfortunately, its purely dyadic, narrow focus makes the TCE framework incapable of addressing such questions.

Suspicious practice 2: Treating transaction characteristics as given.

A second suspicious practice of empirical TCE studies is that transaction characteristics are normally not treated as decision variables. To understand the ramifications of this practice and make the necessary ‘adjustments’ in the model design, it is necessary to start from a more basic level of argumentation.

When designing their business strategy, the firms need to make a lot of choices in regards to how to position themselves relative to their competitors. *What kind of* activities should we perform? And *how* should we perform them? For example, they need to decide what products and services to offer, determine how to compete in product markets, and choose an appropriate level of scope and diversity (Rumelt et al. 1991). Obviously, underneath all these activities lies a world of transaction costs. For example, it is not costless to sell and deliver product or services to customers; “it is ultimately economizing with these costs that yield the outcomes described in the theories based on market power” (Foss 2002: 20).

It seems that transaction costs and strategic choices in regards to for example product markets are inextricably intertwined. Accordingly, one is faced with a need for some guidance when trying to disentangle the matters to make them ready for critical analysis. Nickerson (2000) provides a useful starting point in this respect. He drew up a four-tuple of strategic choices which he called the economizing theory of strategy. These choices all needed to be considered if a firm wanted to maximize its profits. The four sets of choices were (1) targeting a specific set of customers (i.e. positioning in terms of product choice), (2) choosing a production-cost technology, (3) making specific investments or not to support the customer transaction, and (4) selecting an organizational structure. These four sets of choices were seen as interdependent, and the optimal strategy is the tuple that generates the greatest net receipts.

Considering my present purposes, Nickerson’s (2000) framework appears particularly useful in two respects. First, there is an explicit recognition of the need to embrace additional contextual factors that *lead to different transaction attributes*, of which asset specificity is of primary importance (Klein et al. 1978; Williamson 1979). Admittedly though, he was not the first to advocate this point. Amongst others, Masten (1996) noted that

“[t]he specificity of assets and the level of investment in those assets that determine the size of appropriable quasi-rents ... are themselves decision variables. The location of facilities, the adoption of specialized designs or equipment, and the scale of investments should all, by rights, be treated as endogenous variables” (p. 60).

In practically all empirical studies, the transaction attributes have been taken as given. The reason for this may be that the theory offer little insight into this matter other than that specific investments are made in order to maximize efficiency. Day and Klein (1987) provided the following diagnosis of this problem;

“The transaction cost analysis framework affords a wealth of insights into the organization of vertical relationships - *but only when the characteristics of the transaction are known*. However, these characteristics *reflect strategic choices made partially outside the confines of the model*. As a result we can expect transaction cost considerations to provide only part of the rationale for cooperative behavior” (p. 55, *my emphasis*).

Considering that TCE is an ‘empirical success story’ (Shelanski and Klein 1995; Williamson 1996), this critique may seem odd. The point is that most often only a reduced-form version of the TCE model has been subjected to testing, namely, that larger specific investments are associated with stronger governance safeguards (Ghosh and John 1999). Almost no empirical studies treat transaction attributes as endogenous. Hence, the antecedents of the specific transaction-governance pair remain an open question (Masten 1996).

The second point at which Nickerson (2000) appears particularly useful, is the guidance provided in analyzing the tensions between the different parts of the model. Acknowledging that the increase in model complexity makes it more difficult to disentangle the effects of the different constructs, and that a simultaneous analysis seemed too difficult, he resorted to a staged process of analysis. His four-tuple framework has three stages. The first stage parallels a marketing function which considers the implementation of a range of positions, or in Porter’s (1996) terms, which activities should be executed in what way. The second stage evaluates the specific investments for each position and aligns each of the

resulting transactions with a governance form. In the third stage, the position that yields the highest expected payoffs is selected.

Admittedly, this approach is quite similar to the heavily criticized SCP model, of which complete decision making rationality was only one of some unrealistic underpinnings. However, in lack of anything better, this dissertation will allude to such a staged approach. Notice that this is not to say that complete decision making rationality is assumed herein. Rather, a stage-wise approach is taken due to analytical purposes, as well as because it “captures the spirit of the comprehensive [governance] model” (cf. Ghosh and John 1999: 142).

Considering my present purposes, the first two stages in Nickerson’s (2000) framework appear most interesting. Here, the asset specific investments are endogenized by assuming that each position leads to a different level of investment. In other words, the positioning strategy is treated as an antecedent to asset specificity. Does such an approach make sense? I believe it does. Consider the following example. A firm is selling a high quality product in a specific product market, and the perceived value of the product throughout the value chain will increase if supported by specific investments in the relationship with the chosen customer. The function of these investments may for example be to enhance the product’s unique attributes. According to TCE, if these investments are done, such investments need to be protected by raising a governance apparatus that has the required safeguarding capacities. But the larger part of the empirical studies within TCE misses the first half of this causal chain because the transaction characteristics are taken as given.

The following scenario further clarifies my position. Firm A and firm B operate in the same product market. Both firms have decided to pursue a specific product strategy in a market. Firm A offers a specific assortment of differentiated high quality products to some customers, whereas firm B offers more standardized products to the some other customers. Further, firm A decides to make some *significant* investments in the relationship in order to build up under and support its product strategy (e.g., promote its image or support crucial features of the high-quality product) as well as deal more efficiently with the customer in general (e.g., support just-in-time initiatives, improve delivery schedules, adapt internal procurement procedures). Firm B, which sells more standardized products, decides to make *only minor* customer specific investments, the purpose of which is primarily to deal more efficiently with the chosen customer. The different levels of asset specific investment will, in turn, induce the firms to raise different types of safeguards.

The standard approach of relating higher degrees of asset specificity to higher degrees of formal contracts or quasi-integration will miss the first half of this sequence. Accordingly, such an approach is unable to explain why the two firms have different levels of investments in the relationship and, as a consequence, choose different governance solutions, even though they operate in the same market. Obviously, such a model is unsatisfactory. As argued herein, the way out of this problem is to open for the possibility that the two firms may have different positions in the product market, which entail different levels of investments in order to maximize value (cf., the Coase theorem (Coase 1960)⁶). In turn, the different levels of asset specificity induce firms to choose different governance forms.

Another serious concern is that, as Ghosh and John (1999) points out, by testing the reduced-form only, the value-maximizing logic behind the sequence of choices is suppressed. Consider firm A again. Selling high quality product to an important customer, it has decided to support these transactions by some specific investments. The effects of these investments can be categorized in terms of (i) the resulting reduction in the marginal cost of the product, and (ii) an enhancement of the appeal of the product further down the value chain. The total sum of the effects of these investments is the increase in joint value for the exchange parties. Alternatively, the firm will not invest in the relationship if the investment costs exceed joint value increase. Which level of investment will be chosen? Following the Coase theorem, the firm will choose the level of specific investment that maximizes joint value. Not doing so means inefficiency, because opportunities to realize value are not pursued. This is the value creation aspect of TCE, an aspect which is curbed by the popularized approach of testing only the reduced-form in empirical studies. If asset specificity is not treated as an endogenous variable, this logic is suppressed because attention is drawn only to the costs of the frictions of the exchange. Hence, it is not surprising that some harsh critiques (see, e.g., Zajac and Olsen 1993) have been launched against the apparently obsessive single-minded cost-minimizing focus of TCE (Ghosh and John 1999).

To sum up, I claim the usefulness of this stage-wise approach due to its potential to (i) investigate the antecedents to transaction attributes, (ii) thus treating these as decision variables, (iii) implying that the value maximizing logic of the TCE framework is magnified rather than suppressed.

⁶ This theorem simply states that in a world where all agents can bargain without costs, the contracting parties will implement the mix of activities that maximizes value.

Why TCE should be complemented with positioning analysis.

In this dissertation, I claim that by complementing the TCE framework with elements from the positioning paradigm we are provided with some tools that have the potential to address these matters. Noteworthy, the assertion of the conceptual complementary value of the two perspectives has certainly been made before. Teece (1984) was arguably the first author who pointed out the conceptual complementarity of the two perspectives. Still awaiting empirical contributions, Day and Klein (1987) repeated his claim, and concluded that the complementary value had yet to be fully recognized or exploited. Porter (1996) claimed that both operational effectiveness, which includes efficiency, and strategic positioning are essential to superior performance. Hence, he concurred with the others in his assertion of the complementary value of the efficiency-oriented TCE framework and strategic positioning analysis. Ghosh and John (1999) repeated these claims and strengthened them by unpacking and clarifying the underlying conceptual intricacies. In lack of supportive empirical material, however, they had to illustrate the points made by anecdotal examples. Other important contributors have been Nickerson and colleagues (Nickerson 1997; Nickerson and Silverman 1997; Nickerson 2000).

Due to his historical significance in strategic management and his recognition that efficiency is an important aspect of strategic management, Porter is taken as a starting point of argumentation. According to Porter (1996), strategic positioning is about being different. It means performing *different* activities from rivals' or performing similar activities in *different ways*. Further, the positions can be related to a number of matters, including customer needs, customer accessibility, or the variety of a company's products or services. The activities along which to differentiate itself, are those functions that create, produce, sell, and deliver products or services to customers.

The strategic positioning perspective bases competitive strategy on the avoidance of competition. The firm designs a strategy, the purpose of which is to find a position that is maximally shielded from competition, because such a position will assumedly maximize profits. It is important to recognize that transaction costs may not be simply implicit in this search for such a position. Rather, the transaction costs are the result of firms striving for competitive advantage. For example, customer specific investments may arise as a result of the pursuit for differentiation. This is the point at which the TCE calculus can be appreciated.

Let us see why increased transaction costs often follow from a differentiation strategy. Assume that a firm is operating in a number of product markets, but, for analytical purposes, that we concentrate on only one of these markets. Porter (1980) emphasized the value of value

chain relations as part of a differentiation strategy. There are, namely, a number of positive strategic effects that can be gained by developing relations to customer and suppliers. First, better coordination with channel members may be an important element of a firm's differentiation strategy, for example in fulfilling buyer needs or supporting a just-in-time philosophy. Second, the firm might capture better intelligence about market and technology, which may be crucial factors in order to stay ahead of the competitive race. Third, closer value chain relations may secure a more stable and reliable supply of products in difficult periods, thereby improving the credibility of its products and its capacity to deliver at all times. Fourth, it might be able to raise barriers of entry to the market. Potential entrants might perceive it to be difficult to enter relationships with suppliers and distributors that already have entered close (and maybe exclusive) relationships with their competitors, and they may perceive the close relationships as a signal of commitment, thus deterring their market entrance⁷. The close relationship then functions to maintain its position in the market. Fifth, strong relationships may defend the focal firm itself against such foreclosure tactics, strengthening the credibility of its image by securing its ability to deliver in tight periods (Day and Klein 1987). These are all issues that have been frequently stated as reasons to enter closer vertical relationship in a product market⁸. On this basis, it seems strange that a structuralist approach generally has not been applied for the analysis of closer, cooperative vertical relations. Important in this context, however, is that the formation of closer relationships often implies that some special adaptations are made, so that transaction costs increase⁹. In turn, this has important ramifications for the organizing of the transaction.

Overall, the strategic positioning approach has the potential to offer valuable insight to the analysis of vertical linkages. However, all the above-mentioned reasons to enter closer value chain relationships are deduced from a strategic behavior rationale, so that transaction costs implied by the different decisions are ignored. As the focus is only on how to relate the firm to its competitive environment, only half of the problem is addressed (Teece 1984). Little assistance is provided in regards to how to organize the resulting relationships. For example,

⁷ Note that this argument is parallel to one central tenet within the IO paradigm. By vertical integration, firms can create market imperfections so that barriers to entry are raised, because potential entrants will have to spend more resources to effectively compete with the incumbent (Bain 1956).

⁸ Note that reference is made to the individual product market. Decisions are assumed to be made in regards to this product market only. Nickerson's (2000) model assumes that the firm makes one giant transaction over all product markets in which the firm is operating. In contrast, by taking reference to a specific product market, Ghosh and John (1999) addresses "individual marketing strategy choices in individual product markets" (p. 136). Hence, this dissertation alludes to the latter of these approaches. This approach also implies a mixed-level model.

⁹ Parenthetically, we note that only when considering this part of the coin, one may realize that the resulting transaction costs may override the potential competitive advantage. Thus, the company may need to scale back its initial investment so that less costly governance solutions are required (Ghosh and John 1999).

consider the case that a firm has decided to forge closer relationships upstream and downstream to a few of the supply chain members and that some adaptations need to be made. How should one govern these relationships? What sort of contracts should be written? And who should have the decision making authority in regards to what activities? Such 'lower-level' logic falls outside the range of this framework; the theory is completely silent in regards to the assessment of the (appropriate) behavioral response of the firm (Day and Klein 1987). This is the situation in which the value of the TCE calculus becomes crucial. Given the characteristics of the transaction that have resulted from some strategic decisions in the particular product market, it provides a rigorous framework regarding what governance apparatus should be raised as a response to claim the focal firm's share of the (joint) value. Incidentally, notice the resulting mixed-level model; some differentiation strategy in a given product market provides the starting point of argumentation, whereupon the lower-level logic of specific adaptations and governance form follows.

In sum, when analyzing distribution channel linkages, there is a need to understand both (i) how industry characteristics and positioning strategy relate to the formation of closer value chain relationships, as well as (ii) how the resulting market failure impacts the organization of these relationships. As elaborated above, disregarding either element necessarily means that important matters are missed. Applying the two perspectives in combination enables an analysis of the implications of industry matters, as well as when and how strategically important activities should be supported with specific investments and organized most efficiently.

Porter's (1980) most fundamental proposition was that firms should strive to find an optimal position within the industry. This position was to be maximally shielded from the five forces of competition. On this basis, I assert that there are two decision criteria that appear most obvious. First, one must assess *the implications of the chosen strategy in terms of the adaptations made between the channel partners*. Second, one must address the role of *the attractiveness of the market*. In chapter 6, I will deduce refutable hypotheses in these respects.

4.2 Organizational capabilities

In this section I will first briefly present the organizational capabilities paradigm's central underpinnings and some selected aspects of its research agenda. Second, I will demonstrate

that elements in this perspective enable an analysis of some matters that fall out of range of standard TCE reasoning, thus representing a second source of complementary value.

4.2.1 Its underpinnings and central tenets

Compared to the TCE and strategic positioning literature, the OC approach is messy and internally fragmented. Nevertheless, there seem to be some commonly acknowledged tenets across the different fractions. In order to understand these, it is apt to start with what this paradigm is definitely not about. To this end, mainstream economics is taken as a point of reference; its assumption of perfect insight and zero transaction costs implies a given and fully transparent production function free of idiosyncratic elements. In its utter implication, all relevant knowledge about the production function is easily encapsulated in a 'blueprint' (Robinson 1956). This view was early on considered unsatisfactory.

Richardson (1972), arguably one of the most important contributors to the OC paradigm, claim that mainstream economics "abstracts totally from the roles of organization, knowledge, experience, and skills" (p. 888), and renders the organization to a black box. Nelson and Winter (1982) provided a more elaborate outlining of the new paradigm. Explicitly taking distance from orthodox economic theory, and by taking basis in Simon's (1957) bounded rationality theorem and Polanyi's (1966) notion of tacit knowledge, they attempted to dig into this black box organization. While doing this, they kept the notions of skill and routine central. By a 'skill' was meant "a capability for a smooth sequence of coordinated behavior that is ordinarily effective relative to its objectives, given the context in which it normally occurs" (p. 73). Further, "... skills, organization, and 'technology' are intimately intertwined in a functioning routine, and it is difficult to say where one aspect ends and another begins" (1982: 104). Hence, there is a link between individual and organization routine. In fact, routines can be cast in terms of "the skills of an organization".

The skills or, at the organizational level, routines, can be associated with the (core) competences, intangible resources, or dynamic capabilities of their respective management theories¹⁰. In fact, these "skills of an organization" are the central concepts of the OC

¹⁰ This is not to say that these concepts are identical, rather that they entail similar features. As claimed by Barney, arguably the most important contributor behind the RBV school of thought; "In principle, distinctions among terms like 'resources,' 'competencies,' 'capabilities,' 'dynamic capabilities,' and 'knowledge' can be drawn. ... [however], while each of these 'theories' have slightly different ways of characterizing firm attributes, they share the same underlying theoretical structure. All focus on similar kinds of firm attributes as critical independent variables, specify about the same conditions under which these firm attributes will generate persistent superior performance, and lead to largely interchangeable empirically testable assertions. Battles over

perspective. In contrast to being a production function, the firm is regarded as a repository of organization and production knowledge, more or less tacit and complex in nature. The capabilities constitute the knowledge base of the firm, and are defined as “complex bundles of skills and accumulated knowledge, exercised through organizational processes, that enable firms to coordinate activities and make use of their assets” (Day 1994: 38). These capabilities have been cultivated slowly over time, and their present nature is a result of a path-dependent knowledge accumulation process in which chance, history, and lock-in to idiosyncratic trajectories have played a central role (Foss 1996). As a result of the many forces exerting impact on these path-dependent long-term processes, the capabilities observed are heterogeneous across firms. In brief, then, the OC paradigm takes basis in some behavioralist decision rules (cf. Cyert and March 1963) and combines so doing with acknowledging the significance of tacit knowledge embodied in skilled behavior. This skilled behavior is then brought to the level of an organizational skill, and termed ‘organizational capability’.

Admittedly, the concept of an organizational capability is vague. To gain a better understanding of it, it is instructive to think in terms of activities. As noted in the market positioning section, the firm has to make a large number of choices in regards to *what* activities to carry out and *how* to fulfill the carrying out of these activities. In these respects, the OC paradigm provides completely different rationale than does the positioning perspective. The OC paradigm states that the firm needs to hold certain kinds of underlying capabilities in order to be actually able to execute these activities in the first place. Further, the manner by which these activities are carried out is determined by the nature of these underlying capabilities. It is these capabilities that coordinate the activities and *enable the carrying out of the related processes*. Alternatively, one may say that the capabilities are *manifested in terms of such activities*.

When looking at the research agenda, one sees that a broad range of issues have been cast in light of the notions of the OC paradigm. It would be out of scope to provide a review of all these topics, but, at the same time, some treatment is needed to provide an understanding of how to apply the framework. Neither intending to accommodate all topics studied, nor claiming that the categories provided are mutually unrelated, the studies are classified into the two broad groups. Even though the reader may feel uncomfortable with this classification, I find it to serve the purposes of this dissertation.

the label of this common theoretical framework are an extreme example of a classic academic ‘tempest in a tea pot’ - full of sound and fury but signifying nothing” (Barney and Arian 2001:139).

The first category of research has focused on *production-related* matters. The focus of this stream of studies is most related to, but not exclusively so, *what activities* the firm carries out or should carry out. Research on the make-buy decision is a typical example of this category. Applying OC thinking on this matter, it is claimed that a firm has internalized an activity because it can carry out the production processes in a more cost-efficient way than the market (i.e. the other firms) is able to. Alternatively, given that the market is able to compete, the tacitness, complexity and idiosyncrasy of much productive knowledge make it difficult to make contracts with potential suppliers and educate them about crucial product characteristics. The costs associated with such activities may be too high to justify a buy-decision. Similar logic explains the flip-side of the coin; the focal firm may lack adequate understanding of the production processes or technology behind the product, so that it takes considerable time and spending of resources before it will be able to learn how to carry out the production processes to effectively perform the activity (Gulbransen 1998). This renders buying the product to be the only available choice¹¹.

As this dissertation studies antecedents to formal and relational governance, the question of which (production) activities to carry out (whether it should make or buy) is taken as given. Nevertheless, the fundamental logic underlying these studies has an important functioning because it casts light on some suspicious practices in empirical work within the channel governance literature. This matter will be saved for elaboration in chapter 4.2.2.

The second group of studies may be broadly characterized as *organizational* matters. These studies are mostly focused on *how* the activities are carried out. Consider, for example, a set of activities that tend to be carried out by most businesses, activities such as order fulfillment, service delivery, logistics, and the management of supplier and customer relationships. An important tenet of the OC paradigm is that firms' past experiences with these activities, as well as activities by which similar capabilities have been exercised, determine their knowledge base, which in turn impacts how these activities will be carried out in the future. The carrying out of these activities *constitutes* the capability of the firm. As each firm has a unique history, and then exercises these underlying capabilities differently, the capabilities will be *heterogeneous* across firms.

Now, consider this insight in the domain of closer B2B-relationships. The change towards focusing on creating and maintaining long-term B2B relationships inevitably implies that some *capabilities* of a different nature are required to handle such relationships. Of

¹¹ It should be noted that such reasoning represents an opportunism-independent theory of the firm, which have been advocated by a number of researchers (see, e.g., Conner 1991; Kogut and Zander 1992, 1996; Grant 1996).

particular relevance are the firm's capabilities related to the creation and management of close customer relationships. Day (1994) argued that such capabilities are likely to be a particularly important feature of market-driven organization. In this respect, he set focus on the need for close communication, joint problem solving, and enhanced coordination of activities. The firms must work together in a very different way than what was common before; joint product development processes, production planning and scheduling to support just-in-time initiatives, inter-firm integration of information management systems, and adaptation of product and internal processes are only some of the important matters. Obviously, the carrying out of such processes implies escalated requirements on the quality of the interface between the firms. Now, the firms *need to master the art of cooperation*. Glancing to the failure rates of strategic alliances (see, e.g., Child and Faulkner 1998) there are reasons to believe that these same firms do not possess these capabilities necessary for mastering these relationships. Much too often, trading relationships temporarily or prematurely break down, so that potential competitive advantages are not realized. This may be due to inferior channel management skills, or as termed by Day (1994), customer linking capabilities.

4.2.2 The complementary value of the OC paradigm to the TCE framework

This section will follow the same structure as the parallel section on the complementary value of market positioning and TCE. Three sub-sections follow, the first two of which demonstrate that the notion of bounded rationality is only partially taken into account in the traditional TCE framework, with the implication that faulty analysis may follow. The third section demonstrates how the adding of elements from the OC paradigm to the TCE framework results in a more realistic model.

Williamson has repeatedly reminded us how TCE explicitly acknowledges Simon's bounded rationality theorem as one of its central fundamentals. Nevertheless, when analyzing how this theorem is applied, one realizes that the theory does not stand up to scrutiny; the notion of bounded rationality has only partially been applied, at best. One can cast this critique in terms of both production and governance related matters, of which only the latter is at focus in this dissertation. However, in order to shed light on bounded rationality for

governance matters, it is instructive to start with the production matters¹². Parenthetically, by making this distinction, it is not meant that these matters are unrelated. The distinction is made for analytical and instructive purposes only.

Asymmetrical invocation of bounded rationality – production purposes

An implicit, though central, assumption in transaction cost theory is the divisibility of the production sequence. Assuming that the production stages could be separated, Williamson was able to carve out the most relevant transaction attributes that represented each particular production sequence. In turn, this enabled his famous theorem of how the nature of the good or service to be delivered should be held constant, so that economizing takes place with reference to the sum of production and transaction costs (Williamson 1985: 22).

By digging into the characteristics of the transaction, Williamson took exception from neo-classical theory. However, by ‘the holding of the nature of the product or service constant’, bounded rationality was *not assumed* in regards to the production processes of the organization. Implicit in his treatment, namely, there is an asymmetry in the invocation of the assumption of bounded rationality; while bounded rationality considerations are at focus when considering governance structures (knowledge for governance purposes is scarce), they are absent when considering the production process itself (knowledge for production purposes is free). It is still implicitly assumed that what one firm can do, another firm may do equally well¹³. This implicitness is best explained by Demsetz (1988);

“”Implicitly,” because the “other” firm is represented by the “market,” and the market is treated as a perfect substitute in production for a firm. The only comparison sought is between the cost of transacting across this market and the cost of in-house managing. ... [Then] [i]n some respects, information remains full and free. Although information is treated as being costly for transaction or management control purposes, it is implicitly presumed to be free for production purposes. What one firm can produce, another can produce equally well, so that the make-or-

¹² Most of the work on capabilities of the firm has started from production rather than exchange (see, e.g., Richardson 1972; Kogut and Zander 1992; Loasby 1994; Grant 1996; Teece et al. 1997). Even though largely the same principles and reasoning constitute the analysis (tacit and social components of knowledge as embodied in capabilities, learning by doing, heterogeneity, non-tradability etc), it seems to be more intuitive to understand from this point of view.

¹³ This also implies inability to explain firm differences (Dosi and Marengo 2000), due to an ignorance of the role of tacit knowledge, social complexity, path-dependence, time-compression diseconomies, asset stock interconnectedness etc.

buy decision is not allowed to turn on differences in production cost” (p. 164).

The legacy of mainstream economics is then still dominant in the standard TCE framework. As two different firms generally do not have the same costs of carrying out the 'same' productive operation (Richardson, 1972), this oversimplification has important consequences, for example, when focusing on the make-buy decision. As one is not allowed to turn on differences in firms' endowments of productive knowledge, one greatly reduces the ability to explain the institutional structure of production, which in fact is largely explained by the relative costs of organizing particular activities (Coase 1988)¹⁴. In fact, such differences in productive costs are what specialization and division of labour are all about. Hence, the benefits of some fundamental principles in economics fall outside the range of the model.

In sum, important matters are lost through a skewed invocation of the bounded rationality principle. Important differences between firms are lost, and the model loses predictive power. This insight made Teece assert that “[i]n order to fully develop its capabilities, transaction cost economics must be joined with a theory of knowledge and production” (1990: 59). Such an integrative approach has lately been followed in empirical research (see, e.g., Monteverde 1995; Combs and Ketchen 1999, Gulbrandsen 1998; Poppo and Zenger 1998; Argyres 1996; White 2001; Schilling and Steensma 2002; Leiblein et al. 2003; Leiblein and Miller 2003), and seems to be generally accepted.

Asymmetrical invocation of bounded rationality - governance purposes:

Whereas it seems to be generally acknowledged that TCE has retained the neo-classical hyper-rationality for production purposes, less attention has been devoted to how the bounded rationality principle is applied for governance purposes. Below, it is argued that bounded rationality is only partially taken into account for governance purposes as well. In particular, it is claimed that complete rationality is assumed in regards to the perception and understanding of the contractual parties. In order to illustrate this claim, basis in Hodgson (2004). Being considerably less cited than the articles focusing on production-related matters, the principal message and underlying reasoning of this article is not well known. Hence, the

¹⁴ This argumentation may in fact be traced back to Richardson's (1972) classic, in which was claimed that “organizations will tend to specialize in activities for which their capabilities offer some comparative advantage” (p. 888), that “it will pay most firms for most of the time to expand into areas of activity for which their particular capabilities lend them comparative advantage” (p.889), and that “activities [...] do require specialized organizational capabilities for their undertaking” (p.890), issues pertaining to incentive alignment excluded.

matters are briefly presented below. Doing so will lay open suspicious assumptions and practices within TCE literature and pave the way for how elements from the OC paradigm may at least partially alleviate from this problem.

Hodgson (2004) started with Williamson's repeated claim that all governance structures arise principally to deal with opportunism (see, e.g., Williamson 1975, 1979, 1985, 1993, 1999, 2000), and convincingly explained how *matters of perception and interpretation* were additional reasons for the existence of differences in governance structures; even though agents act with good intentions, misinterpretations often arise due to differences in cognitive frameworks, with the implication that agents may not, and in general do not, act "in the same fully committed way" (Williamson 1999: 1099) in the absence of opportunism. When the interpretations of the counterpart differ from the intentions behind a message, all kinds of outcomes may occur, though for other reasons than opportunism. Further, these matters only increase in importance when communication is increasingly non-codifiable, because the scope for misinterpretation is greater¹⁵. As he claimed;

The essential and general problem is one of interpretation. The communication of an instruction always carries the possibility of default, because it can always be interpreted in a different way. Communication itself is costly, and there is a trade-off between the principal providing a more complete set of instructions, thus reducing ... the possibility of misinterpretation, and the provision of a shorter instruction that is not so time consuming in its articulation (p. 409).

Following this logic, a contract default may arise due to opportunism, as well as misinterpretations resulting from different knowledge or cognitive frameworks. Accordingly, the role of governance is then both to (i) provide checks against opportunism, as well as (ii) provide guidance in order to "minimize the scope and effect of all potentially distorting transitions" (Hodgson 2004: 408). Such distortions may arise as a result of honest, but nevertheless important, misinterpretations and misunderstandings, in which cases the

¹⁵ In fact, Hodgson claimed that, "within broad boundaries, employment becomes less a matter of contract compliance and more a matter of the growth of capabilities and knowledge" (412). Note the resemblance to the rationale for firm boundaries provided by, amongst others, Conner (1991), Kogut and Zander (1992), and Conner and Prahalad (1996). Hodgson's critique may then be interpreted in light of the tenets of this tradition, whose grand theory may be called 'knowledge-based theory of the firm'.

opportunism rationale is not the fundamental matter. Reasoning which exclusively relies on opportunism then only provides half the picture. Such reasoning needs to be complemented with an assessment of problems related to matters of cognition and interpretation. In this respect, it is argued herein that a firm's *relevant accumulated contracting experience* at least partially addresses this matter. More detail on this respect will be provided in the next section.

Why TCE should be complemented with the OC paradigm.

In this dissertation, I claim that by complementing the TCE framework with elements from the OC paradigm we are provided with some tools that have the potential to at least partially alleviate the theoretical model from these fundamental matters.

To an increasing degree, one sees constructs such as 'market-based assets' (Srivastava et al. 1998), 'market knowledge competence' (Li and Calantone 1998), 'general marketing management expertise' (Capron and Hulland 1999), and 'export marketing capabilities' (Zou et al. 2003), in the marketing literature. Basically, these studies import ideas or constructs originating from the OC perspective within the strategy literature. These studies have typically focused on the antecedents to or implications of firms' marketing-related capabilities, them being called market knowledge competence or the like. In this study, the construct 'relational capability' (cf. Dyer and Singh 1998) is adopted to denote a firm's abilities for initiating, developing, and maintaining long-term B2B relationships. As "research has shown that experiential learning is a key to developing an alliance competence" (Lambe et al. 2002: 154), the construct is conceptualized in terms of broad experience with a range of aspects relevant for the handling of the customer relations. Such aspects include for example selection of customers, negotiation of future exchanges, maintenance of the exchange relationship, and general experience with management of similar inter-firm exchange relationships.

The central aspect that this construct intends to capture is that firms' past experiences with these activities, as well as activities by which similar capabilities have been exercised, determine their relevant experiential knowledge base, which in turn should increase their abilities related to initiating, developing, and managing long-term relationships with other firms (for similar argumentation, see e.g., Day 1994, 1995, 2000; Dyer and Singh 1998; Kale et al. 2002; Simonin 1997; Lambe et al. 2000, 2002; Johnson et al. 2004; Anand and Khanna 2000; Kale and Singh 1999).

But how can this relational capability construct offer a (partial) remedy for this flaw in TCE theory? To answer this question, basis will be taken in Hodgson's (2004) argumentation.

He was principally concerned about matters of perception, interpretation, and cognitive framing of information. A result was that a more complete set of instructions should be given in order to reduce possibility of misinterpretation. However, provision of such instructions is time consuming and costly. For example, consider the perceived uncertainty because the firm is inexperienced in the market. The great uncertainty may make it difficult to provide a rather 'complete set of instructions'. For example, unambiguous inter-firm coordination-enhancing routines may be very difficult to draw up, just because the firm does not have the necessary insight or experience to do so. Further, such an experiential base should lessen the barriers related to designing roles and responsibilities that are clear-cut, so that the scope of confusion is lessened. It may also be better able to foresee hazardous situations and impose unambiguous safeguards against these of which related contingencies may turn into effect in its disfavour (Delios and Henisz 2000).

Following the argumentation of Hodgson (2004), the desirability of such clear-cut and unambiguous routines and roles may not only be related to the degree to which there is a risk of opportunism. Also, such routines and plans may be desirable per se, because they constitute a more complete set of instructions, decreasing the scope and effect of all 'potentially distorting transitions'. A *broad experiential base* with issues related to close long-term cooperation might facilitate the set-up of such clear-cut and unambiguous roles and routines. Also, a broad experiential knowledge base would make it *less costly* for the focal firm to provide a *more complete set of instructions*¹⁶.

Focusing on firms' differential abilities to organize, manage, coordinate or govern sets of activities, the OC paradigm represents the second source from which a standard TCE approach may usefully draw insight. On the basis of the above, it is claimed that by adopting a construct that represents a firm's relevant accumulated contracting experience, one is at least partially able to address matters related to misunderstanding and misinterpretation resulting from differences in perception, interpretation, and cognitive framing of information. Excluding this aspect implies making some very implausible assumptions in the construction of a relationship governance model.

¹⁶ Admittedly, the 'relational capability' construct does not at all fully capture matters related to cognition and interpretation. I argue, however, that partly taking into account these matters is better than total ignorance.

5 SUMMARY

The literature on inter-firm relations is extremely broad, encompassing a number of disciplines. This dissertation pursues to combine elements from a number of the research paradigms. Throughout part I, focus has been cast on the research question from various perspectives. In particular, I have advocated the potentially significant additive insight of each of the elements of the research model. I will present the final research model in the next chapter. In this chapter, I will briefly review the different matters on which focus has been placed.

In chapter 2, relationship governance was first defined to be “an encompassing phenomenon characterizing the nature and approaches employed by parties to organize and regulate exchange conduct effectively” (Gundlach 1994: 249). A preliminary challenge was then to dimensionalize this phenomenon. A review of the literature strongly suggested that one should consider at least two dimensions, i.e. formal and relational governance, or as they are termed herein, formal and relational contracts.

In chapter 3, a selective review of the empirical literature on formal and relational contracts was presented. On the basis of this review, some conclusions could be made in regards to the consistency of findings related to central principles. First, it seemed that higher degrees of asset specificity generally led to higher degrees of vertical integration, formal contracts, or the like. Second, it seemed that relational contracts also arised as a response to higher degrees of asset specificity, suggesting that norms possess safeguarding capacities on their own. Third, it appeared to be a viable approach to consider opportunism as an evolving property of the relationship, rather than something which was outside the confines of the theoretical model. At the same time, such an approach was found to be consistent with the assertion that formal and relational contracts exist in tandem, constituting a dual model of channel governance. These findings were taken further, and assumed to make up a ‘base model’ of channel governance.

In chapter 4, I brought in two new perspectives to cast additional light on this base model. I took a thorough conceptual approach in order to sort out the intricacies of the different perspectives and demonstrated that important insights can be added by each of the two new perspectives.

Applying the strategic positioning (“outside-in”) perspective demonstrated that, when analyzing distribution channel linkages, there is a need to understand how industry characteristics and positioning strategy have impact on the formation of closer value chain relationships. To these ends, it was suggested that (i) the attractiveness of a market, and (ii) an assessment of the implications of the chosen strategy in terms of the adaptations made between the channel partners, appeared to be fruitful avenues for research.

Applying the organizational capabilities (“inside-out”) perspective first clarified that firms possess differential abilities in regards to organize, manage, coordinate or govern sets of activities. Further, by adopting a construct that represents a firm’s relevant accumulated contracting experience, one is at least partially able to address matters related to misunderstanding and misinterpretation resulting from differences in perception, interpretation, and cognitive framing of information.

5.1.1 Assumptions

Implicit in the adding new perspectives to the core TCE model, core assumptions have been respecified. Throughout chapter 2 and 4, I argued that these new assumptions are more realistic. For instructive purposes, these new assumptions are briefly clarified below.

The first new assumption is that (the threat of) opportunism is considered to be an evolving property of the relationship, rather than as something exogenous to the model. As demonstrated, this respecification is closely linked to the assertion that both formal and relational contracts constitute the overall channel governance. Also, it is linked to the insight that man is ‘both an entirely selfish creature and an entirely social creature’ at the same time (Macneil 1983: 348).

The second new assumption is that the notion of bounded rationality is broadened to also capture issues related to misinterpretations, and confusion between exchange partners. Standard TCE assumes away such problems, which implies assuming unrealistic cognitive capacities of human decision makers (Hodgson 2004).

The third new assumption is that the transaction characteristic of asset specificity is treated as a decision variable, rather than given beforehand. In turn, this assumption opens up for considering asset specificity as a mediating variable between its antecedents and the resulting governance mechanisms respectively. This contrasts the popularized approach within TCE literature.

The fourth new assumption is that industry characteristics have impact on the degree to which the firm makes investments in that market, i.e., the counterpart. Hence, it assumed that the human decision makers take into account the characteristics of the industry when they make decisions about what level of investments they should undertake in each market. I believe that assuming away such considerations is a myopic approach.

5.1.2 Unit of analysis

The unit of analysis in this study is the relation between a buyer and a seller. This approach is in accordance with most inter-organizational research, such as work within the political economy framework (Stern and Reve 1980; Achrol, Reve and Stern 1983), as well as work on buyer-seller relationships from either or both of the TCE and RET perspectives.

Bringing in two new perspectives, there might be a risk that the resulting model is a mixed-level model. Let us see if this is the case herein. The firm's relational capability is rooted in firm's experience with exchange relationships. As such, the construct has its primary basis in the firm, and not the exchange relation. One might argue that this experience is on the same level, because it is considered in the association with this particular exchange. However, as it is the firm's *prior* experience with exchanges that constitutes its present relational capability, the fact remains that this construct is only partially rooted in the particular exchange at focus; the experience with this exchange only make up a part of the firm's total experience. Same reasoning can be applied in regards to both industry and product characteristics. As argued in chapter 4, the industry characteristics are of relevance when studying relationship governance, but these characteristics still exist independently of the exchange relation at focus. Attributes of the product operate at the level of the product market.

Accordingly, it must be concluded that the research model to be outlined in chapter 6 is a mixed-level model. This is in accordance with Ghosh and John's (1999) conclusion about their Governance Value Analysis (GVA) model, a model from which this research model has been inspired to a great deal. In my point of view, the only way to make up a single-level model in this context is to assume that the firm is making 'one giant transaction' (Ghosh and John 1999), and then make all considerations on the level of the exchange or transaction. This assumption is unrealistic and, therefore, unwarranted.

5.1.3 Constructs affecting relationship governance

Obviously, a lot of constructs impact formal and relational contracts. Throughout part I, it has been argued that certain constructs are more theoretically interesting than others. In this study, these are considered to be ‘asset specificity’, which is related to TCE (cf. chapter 3); ‘product differentiation’ and ‘market attractiveness’, which is related to the strategic positioning paradigm (cf. chapter 4.1); and ‘relational capability’, which is related to the organizational capabilities paradigm (cf. chapter 4.2). The hypothesized relationships between these variables, as well as the explanatory logic that connects them, will be presented in the next chapter.

6 RESEARCH MODEL AND HYPOTHESES

In chapter 2-4, the theoretical background of the study was presented. In particular, emphasis was placed on the potential for additive insight by bringing in constructs from the positioning analysis and organizational capabilities paradigms. Now it is time bring these arguments together and construct a model that can be subjected to empirical testing.

In the first section, the base model (cf. chapter 2 and 3) will be established. In the second section, constructs from the positioning analysis (cf. chapter 4.1) and OC paradigm (cf. chapter 4.2) will be defined and 'added to' the base model. Finally, a summary of the hypotheses will be provided and visually displayed (Figure X).

6.1 Hypotheses - the base model

In chapter 3, I demonstrated that the literature was largely consistent in regards to the effect of asset specificity on formal and relational contracts. The theoretic rationale is laid out below.

The effect of asset specificity on formal contracting. A central concern in transaction cost economics is the extent to which resources are deployed to facilitate a particular transaction. As demonstrated in chapter 4.1.2, if one tailors one's investments to fit the idiosyncratic requirements of the particular exchange partner, cost savings and/or value creation are likely to accrue. These benefits have a down-side if they are specific to that transaction, because then they cannot be easily redeployed if the contract governing the transaction should be temporarily interrupted or prematurely terminated. The trade-off is then that specific assets provide benefits in the form of cost reduction and/or value creation in a particular transaction, while simultaneously giving rise to a strategic risk due to low salvage value outside this same transaction.

As the firm, due to limited redeployability, cannot costlessly exit the relationship, a lock-in effect occurs. This lock-in effect transforms the exchange as characterized ex ante by classical contracting (identity of the parties is irrelevant), into neoclassical contracting (identity of the parties is crucial). As a result of being locked-in to the exchange partner, the firm exposes itself to opportunistic behavior by the counterpart, such as failure to perform or seeking to renegotiate terms to appropriate a relatively larger share of the increased cake. Such behavior must be safe-guarded against; the firm needs to protect its investments and

prevent the counterpart's (assumedly) inherent inclinations to appropriate "quasi-rents" (Klein et al. 1978). This protection can come in many forms, including stipulating 'hierarchical elements' in the contract, demanding mutual investments, and, in the most extreme, fully internalizing the transaction.

Considering my present purposes, I revolve around the incorporation of hierarchical elements in a contract. For illustrative purposes, consider the following scenario. A supplier makes significant investments in equipment dedicated to a particular transaction in a customer relationship. Following this investment, extensive internal adjustments are done, new routines are built, and logistics systems are tailored, in order to deal as efficiently as possible with this firm. Finally, the personnel have been trained in order to meet this customer's idiosyncratic requirements and needs in the best possible way. In such a situation, exchange hazards logic maintains that the partner is inclined to act opportunistically, such as taking advantage of "holes" in the contract (Rokkan et al. 2003), wilfully under-perform (Joshi and Stump 1999a), lie about important issues to protect their own interest, or otherwise fail to act with good intentions, in order to appropriate a larger share of the 'cake' (Jap 2001). These threats induce firms to safeguard their investments against such hold-up behavior and adopt neoclassical contracts wherein rules, fixed policies, and standard operating procedures related to the particular transaction are specified. In the terms of this paper, this means that the degree of formal contracting is rising.

Hypothesis 1: Asset specificity is positively related to formal contracting

The effect of asset specificity on relational contracting. In general, the same logic can be followed in regards to the effect of asset specificity on relational contracts. If asset specific investments are made, the firm exposes itself to opportunistic behavior by the counterpart, and the firm needs to safeguard these investments.

It has been documented that formal contracts often is of little significance in inter-organizational relationships (e.g., Macaulay 1963). Even if a contract exists, it is normally augmented by norms and informal agreements (Heide and John 1992). In chapter 2.3, it was argued that relational contracts should be considered to be governance mechanisms in 'their own right' (Powell 1990). First, relational contracts had the capacity to *ex ante* prescribe socially accepted behavior directed toward maintaining the relationship as a whole and curtailing behavior to promote the goals of both parties (Heide and John 1992). Second, relational contracts had the ability to serve an *ex post* role as a point of reference in case of

non-compliant behavior, i.e. in the evaluation of whether, and to what degree, a firm's behavior is in conformity to established standards (Ivens 2002).

How do such relational contracts come about to serve as safeguards? Anderson and Weitz (1992) found that the commitment between the parties was raised following such investments. This suggests that higher degrees credible investments provided an impetus for the building of relational sentiments. In association with asset specific investments and the following lock-in effect, the firm is likely to initiate socialization processes to establish limits on socially accepted behavior and make clear that deviant behavior will be punished. Strong norms are then developed through a positive iterative cycle, whereby positive behavior is reciprocated by similarly-minded behavior by the counterpart. Trust and reciprocity between the parties develop. Eventually, such norms have significant safeguarding capacity. This capacity has been repeatedly confirmed in empirical studies (see, e.g., Noordewier et al. 1990; Heide and John 1990, 1992; Gundlach et al. 1995; Heide and Stump 1995; Lusch and Brown 1996; Bello and Gilliland 1997; Cannon et al. 2000; Artz and Brush 2000; Bello et al. 2003). Haugland et al. (2004) reported similar effects, though for asset specificity on the level of organization and strategy.

The social bonding between the parties resulting from increasing degrees of adaptation towards the counterpart has gained increased attention in the management literature, including the IMP Group (Håkansson 1982, Anderson et al. 1994), the relationship development model (Dwyer et al. 1987), the commitment-trust model (Morgan and Hunt 1994), and the buyer-seller relationship model (Wilson 1995). Antecedent to such productive relationship is that the parties make investments in the relationship (Mattson 1995).

Hypothesis 2: Asset specificity is positively related to relational contracting.

6.2 Hypotheses - the extended model

6.2.1 Industry positioning effects

In this sub-chapter, I will first concentrate on two likely effects of a firm's product differentiation and subsequently on one likely effect of market attractiveness.

A differentiation strategy refers to developing a unique image for a firm's products (Aulakh and Kotabe 1997), so that the customer will perceive the value of this product to be higher compared to the offerings of the competitors (Myers and Harvey 2001). Important factors in this regard are strong marketing abilities, reputation for quality, high-quality products, and strong cooperation in marketing channels (Miller 1986).

The effect of product differentiation on asset specificity. A product differentiation strategy is accompanied by a need to justify the higher prices of the assumedly added value products. I claim that by making asset specific investments in its customer relationships, such justification can be at least partially brought about. Arguments supporting this claim are presented below.

First, one effect of asset specific investment is that the perceived value of the product throughout the value chain may increase (cf. chapter 4.1.2, see also Ghosh and John 1999). Such investments may for example support and enhance crucial product attributes. In turn, this may secure that one “convey to the customer an image of quality and prestige that is congruent with overall product strategy” (Lassar and Kerr 1996: 619). There is also a psychological effect of the demonstrated commitment by such investments. The customer may be more convinced about both the product's unique attributes as well as its supplier's honest intentions. This should further support the image of the product in the eyes of the customer. These effects are particularly beneficial if a potential competitor is considering trying to enter this specific market segment. The investments made should make it more difficult for this actor to gain a similar position in the market. If the customer distributes the product further down-stream, it may also be more willing to act in accordance with the differentiation strategy and promote the uniqueness of the product to its own customers. Second, successful implementation of a product differentiation strategy requires a ‘well-orchestrated’ marketing strategy and value chain (Myers and Harvey 2001). Customer specific investments may enable dealing more efficiently with the customer, such as being more able to support just-in-time initiatives and improve on delivery schedules. Also, such investments supports coordination across inter-firm boundaries, so that the required “coherent behaviour from production to consumption” (Haugland et al. 2004) can be facilitated and more easily brought about. This is an important point. For example, better coordination may give down-stream actors a more stable and reliable supply of products, also in tight periods, supporting the credibility of the manufacturer's products as well as its capacity to deliver at all times. Third, the deployment of asset specific investments may be taken as a signal of

commitment by its competitors, thus deterring their entrance to this particular product segment. The investments made then serve to protect the firm's market position.

Overall, the number of arguments suggests that asset specific investments supports and is a part of a firm's strategy when it is trying to differentiate itself from its competitors in a product market.

Hypothesis 3: product differentiation is positively related to asset specificity

The effect of product differentiation on relational contracting. In order to develop the unique image for a firm's products that a differentiation strategy requires (Aulakh and Kotabe 1997), the firm needs to make products that are attractive in the market place. On which basis of information should one design these products, and find a favourable position relative to its competitors? Asserting that such strategies are associated with increased market orientation, Anderson and Coughlan (1987) and Lilien (1979) argue that pursuing a differentiation strategy requires extensive knowledge about customer needs and preferences as well as a high level of before and after-sales services. It also needs to be able to continually update this information in markets that change rapidly (Haugland et al. 2004). Hence, higher degrees of product differentiation amplify the need for deeper information about the idiosyncrasies of the local market. In turn, this places requirements on the quality of the information channels to that market.

Following the same line of reasoning, information about customer preferences, which may be characterized as "sticky" (von Hippel 1994), must be acquired through ties characterized by close interaction and coordination. Day and Klein (1987) concurred with this, emphasizing that closer vertical relations may be a means for capturing better intelligence about market and technology, which in turn are crucial factors in the staying ahead of the competitive race. Anderson and Coughlan (1987) speculated that "complex products also require the development, deepening, and specialization of working relationships in order to be distributed effectively" (p. 80). I argue that such close ties and deep working relationships are closely related to a exchange climate where strong mutually accepted codes of conduct has been built over time.

Strong ties are traditionally associated with the exchange of high-quality information and tacit knowledge. Uzzi's (1996) study in the New York apparel industry demonstrated that strong ties (cf. Granovetter 1973) provide rich exchanges of customized information, enabling firms to exchange fine-grained knowledge. Similarly, Larson (1992) and Helper (1990)

reported that “thick information” on issues such as strategy and production know-how must be transferred through embedded ties. For this purpose, market structures is not effective or available (Meldrum 1995), because the tacit know-how involved is difficult to transfer without personal contact involving teaching, demonstration, and participation (Polanyi 1962). In general, then, tacit knowledge is more readily transferred between firms between which the boundaries are blurred (Hagg and Johanson 1983). Accordingly;

Hypothesis 4: product differentiation is positively related to relational contracting

The attractiveness of a market refers to “the potential for the market to contribute to overall corporate objectives” (Burke 1984: 347). Market attractiveness is a dimension of the external environment which is taken into account in most portfolio models (e.g., the Product Portfolio of the Boston Consulting Group) (Genturck and Aulakh 1995), and it is a function of the overall industry structure in which the firm is competing (cf. Porter 1985). Usually, attractive markets are growth markets or markets that have growth potential. In a situation of market growth or great potential for market growth, greater investments are required in order to keep pace with the development in the market and maintain its position in the market. “Hence, business units with a strategic thrust of build should be in more attractive markets than business units with hold or pull back strategies” (Burke 1984: 347).

The moderating effect of market attractiveness. Making asset specific investments are done to decrease costs and/or increase value. At the same time, these investments cannot easily be redeployed if the contract governing the transaction should be temporarily interrupted or prematurely terminated. Hence, the trade-off is that specific assets have the potential to bring about significant benefits, while at the same time give rise to a strategic risk.

On what basis should one make the decision to invest in a customer relationship? The likelihood of positive future returns is the principal driver in the fundamental net present value (NPV) model; if the present value of future incomes is positive, the model advises one to make the investment. Similar reasoning can be applied in this context. Earlier it was shown that product differentiation is likely to be a significant driver behind asset specific investments. I argue that one may perceive these returns to be larger in a market with a more promising future; sales are not anticipated to decrease, and joint profits are expected to increase. Compared to a market where competition is cut-throat, the counterpart may also be

more willing to share its profits. Accordingly, if the potential in this market is high, and the prospect will increase in the future, then a reasonable assumption is that the focal firm will consider it more likely that the potential future payoffs from this market will more than compensate the present outlay in customer specific investments. It is therefore easier to justify the risks of such investments if the firm is considering the market to have a promising future (Coughlan et al. 2001). The firm should then be more predisposed to invest in attractive markets¹⁷.

Would more attractive markets generally lead to more investments? I argue that higher market attractiveness does not lead to more investment on its own. Instead, there needs to be an upside in making such investments in the first place, for example as part of a product differentiation strategy. Absent a need to make adaptations towards a specific customer there is nothing to win by taking on more risk, the market being highly attractive or not. The opposite argumentation can also be laid out; in the face of low market attractiveness, the firm would face a darker future in terms of higher returns on its non-redeployable committed resources. Hence, this darker future should curb the incentive to invest in a particular customer relationship. Still, however, it is assumed that the firm has an incentive to invest in the market (represented by a particular customer) in the first place.

Accordingly, I hypothesize that perceived market attractiveness positively moderates the incentives or drivers behind the making of non-redeployable investments.

Hypothesis 5: The positive association between product differentiation and asset specificity will be greater for larger degrees of market attractiveness.

6.2.2 The effect of alliance management experience

Relational capability refers to firm's ability for initiating, developing, and maintaining B2B relationships. Earlier research has shown that "experiential learning is a key to developing an alliance competence" (Lambe et al. 2002: 154). Hence, the construct is conceptualized in

¹⁷ Note that this way of reasoning is dissimilar from the usual reckonings in this regard. Normally, researchers have posited a direct relationship between competitive intensity (the opposite of market attractiveness) or market attractiveness on relationship governance mechanisms (see, e.g., Joshi and Stump 1999a, Genturck and Aulack 1995) or on performance (see, e.g., Cavusgil and Zou 1994; Morgan et al. 2004; Myers and Harvey 2001). The findings of these studies are inconclusive. I suggest that the reason for this conclusion is that market attractiveness (or the like) in fact has another role; its pivotal role must be considered in relation to strategic decisions, which are made outside the confines of a dyadic frame of reference.

terms of broad experience with some aspects relevant for the handling of the customer relations, including selection of customers, negotiation of future exchanges, maintenance of the relationship, as well as broad, general experience with management of similar inter-firm exchanges.

Following the logic of the OC paradigm, a firm's relational capability should enhance firm's ability to develop and manage long-term B2B relationships. For example, Day (1995) noted that, firms that has good 'relational capability' (or the like) "have a deep base of experience that is woven into a core competency that enables them to outperform rivals in many aspects of alliance management" (p. 299). Similarly, Powell et al. (1996) argued that "experience at collaborating is necessary to manage a diverse portfolio of ties. Hence, ... firms learn from exploration and experience how to recognize and structure different types of alliances" (p. 120-121). The rationale for these arguments is that experience with similar transactions or activities helps the firm get a better understanding of a number of aspects of B2B relationship management; over time, they have incrementally adjusted their reactions to similar problems and absorbed feedback from past decisions. Such aspects include the phases through which the relationship evolves, the hazards involved, how the potential benefits can be realized, and a general understanding of the counterpart. Even though books and training programs on the topic exist, the art of alliance management is 'tacit' (Polanyi 1966), so that firms must learn by doing (Anand and Khanna 2000; Spekman et al. 1999).

The effect of relational capability on relational contracting. Cooperative norms have been noted to have a positive effect on performance in a number of settings, regardless of the level of exchange hazards (Cannon et al. 2000; Bello et al. 2003; Bello and Gilliland 1997; Poppo and Zenger 2002). Hence, such cooperative norms should be regarded a positive characteristic of an exchange relationship that is deemed important for the focal firm. Can all firms easily develop such cooperative norms with the counterpart? A requirement for relational governance is *the ability* to actually establish and rely on relational sentiments. There seems to be strong indications in the literature that a broad base of experience with similar exchanges will make it easier for the focal party do so. As noted earlier on, such experience enhances the parties' abilities to initiate, develop, and manage long-term relationships with other firms. Given that it is beneficial but difficult to develop cooperative exchange norms, such experience helps the firm to (i) choose partners who will abide by relational norms, as well as (ii) better understand themselves the value following relational norms (Weitz and Jap 1995). Furthermore, a finding in the export literature is that less internationally experienced

firms show less commitment to and involvement in foreign market operations (Zou and Stan 1998). This thwarts the development of relational norms (Bello et al. 2003). Finally, as a broad base of experience with similar exchanges helps the firm to get a better understanding of the counterpart, such experience is also likely to be crucial in the reciprocative process by which trust and relational norms are developed. Taken together, a positive-minded partner who will abide by relational norms, an understanding of the value of relational norms, and a better understanding of the counterpart all help facilitate the development of norms through a positive cycle of reciprocative self-enforcing behaviour, whereby positive responses are met by increasingly positive responses by the counterpart.

To sum up, firms with limited experience will have difficulties in the development of strong cooperative norms and face a more constrained and unattractive set of choices in regards to relational governance. Lambe et al. (2002) even assert that “firms such expect some of their initial [alliance management] attempts to fail - and [that] this will comprise part of the learning experience” (p. 145). More experienced firms, on the other hand, are more likely to have developed an ability to establish and manage their business on the basis of such sentiments. However, Lambe et al. (2002) did not test this assertion, but encouraged future studies to examine this effect (p. 154). Hence;

Hypotheses 6: relational capability is positively related to relational contracting.

The effect of relational capability on formal contracting. As shown above, there has been some research on how experiential knowledge facilitates the development of relational sentiments. Much less attention has been given to how such experience relates to formal contracting. In chapter 4.2.2, I provided conceptual arguments in regards to how a ‘relational capability’ construct had the potential to provide additional insight to the TCE model. I demonstrated theoretically that this construct had the potential to partially “cover up” for a fundamental imperfection that was a direct consequence of the way by which the bounded rationality principle had been applied in the standard TCE framework. This imperfection will be taken as a basis in the following argumentation for how relational capability relates to formal contracting.

In the building of the TCE framework, Williamson assumed away the existence of perception and interpretation difficulties. Hodgson (2004), in contrast, pointed out that such matters are of great importance, and that the scope and effect of them should be minimized by providing a more complete set of instructions. How does this reasoning relate to formal

contracting? A fundamental concern in the TCE logic is that firms need an *incentive* to undertake a costly activity. The writing of contracts can be considered as such a costly activity. Increasing the specificity of contracts is then assumed to be undertaken only if there is an incentive to do so. I argue that such incentives may come from at least two sources. First, given nontrivial degrees of asset specificity, the firm are more motivated to increase contractual specificity because of the risk of being exposed to opportunism. Second, inspired by Hodgson (2004), provision of a more complete set of instructions is desirable per se, because it reduces the possibility for confusion, misinterpretations, and misunderstandings. In chapter 4.1.2, some examples were given in regards to coordination-enhancing routines, roles and responsibilities; in order to reduce the potential ambiguities facing the different parties, the different routines, roles and responsibilities should be clear-cut. Following the argumentation of Hodgson (2004), the desirability of such clear-cut and unambiguous routines and roles may not only be related to the degree to which there is a risk of opportunism; such routines and plans are desirable per se, because they constitute a more complete set of instructions which functions to decrease the scope and effect of all potentially distorting transitions (which may have nothing to do with opportunism). For example, the potential for misunderstandings due to fuzziness of roles and responsibilities makes it important to clarify the fundamentals of the exchange, which in turn is important to promote cooperation and trust (Poppo and Zenger 2002) and then also firm performance.

However, the task of providing a more complete and clear-cut set of instructions may prove burdensome. First, such clear-cut instructions may simply be difficult to draw up if the company does not have an experiential base to rely on in doing so. Second, inexperienced companies may underestimate the scope and effect associated with these matters. Third, the costs related to the provision of such instructions may be considerable for someone new in the game. A *broad experiential base* with issues related to close long-term cooperation is related to all of these matters. First, such experience would facilitate the set-up of such clear-cut and unambiguous roles and routines. Second, a broader experiential base may make the company better able to understand the counterpart, evaluate its likely responses in different situations, and understand how confusion and misunderstandings may arise, which in turn makes it realize the necessity of providing an unambiguous guide of reference. Third, a broad experiential knowledge base would make it *less costly* for the focal firm to provide a *more complete set of instructions*; if the firm has drawn up such procedures a number of times before, on the other hand, less cost is entailed in doing so again.

To sum up, arguments suggest that more experience with initiating, developing, and managing alliances makes the parties more aware of the dangers related to confusion and misunderstandings, more able to recognize these dangers, and face less cost of increasing the degrees of formal contracting as a tool to minimize the scope and effect of these dangers¹⁸. Also, higher relational capability makes it easier to overcome cognitive limitations associated with selecting a partner with which more advanced formal governance apparatus can be effectively worked out, as well as the cognitive limitations associated with the actual working out of such governance per se¹⁹. Accordingly,

Hypothesis 7: Relational capability is positively related to formal contracting.

6.3 The full model

In sum, the model consists of 6 variables, of which 1 is a moderator, 2 are dependent variables, 2 are independent variables, and 1 is an intermediate variable (both a predictor and a dependent variable). Asset specificity is hypothesized to positively impact the degree of formal and relational contracts. This is the base model of relationship governance.

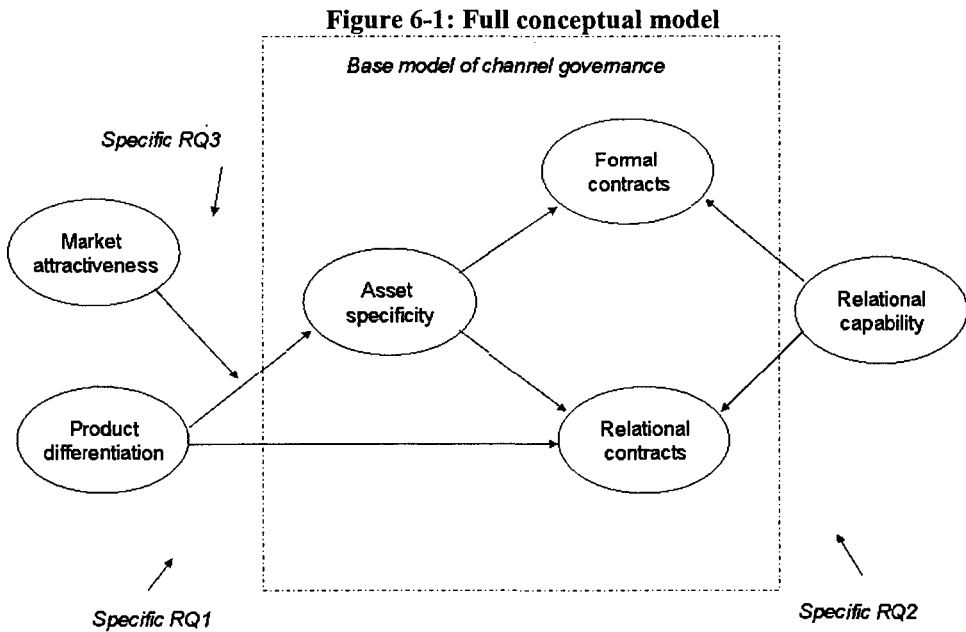
Product differentiation is hypothesized to increase the degrees of relational contracts as well as the level of asset specificity, the latter of which in turn increase the degrees of formal contracts. Market attractiveness is asserted to positively moderate the positive association between product differentiation and asset specificity. As outlined in chapter 4.1, there are strong theoretical and intuitive reasons to believe that strategic positioning considerations are relevant when studying governance of channel relationships. The testing of these three relations will give us knowledge of how such considerations (research question 2)

¹⁸ A parallel argument is that of the proponents of an internationalization process (see, e.g., Johanson and Vahlne 1977); this strand typically claims that experienced firms have gone through the initial stages of risk aversion in entering the unknown and are more willing to enter more high-involvement modes of operation. Indeed, a number of empirical studies have found that more international experience are associated with higher contractual involvement (see, e.g., Delios and Henisz 2000; Aulakh and Kotabe 1997; Myers 1999). A reasonable assumption in this regard is that such higher-involvement operation modes typically are characterized by 'a more complete set of instructions'.

¹⁹ Parallel arguments for hypotheses 6 and 7 can be found in the international business literature. For example, early export literature found that firms with internationally experienced decision makers are more likely to be regular exporters (Cavusgil 1980), and that such individuals are consistently linked to export activities (Reid 1981). An explanation may be that such individuals have a higher ability to acquire, transmit, and use foreign market information that is important for being successful in exporting. Obviously, possessing such abilities is crucial for bonding with the personnel of foreign companies as well as write contracts and cooperation plans where one takes into account the hazards related to misinterpretation and misunderstandings and other problems that may destroy the relationship.

and industry characteristics (research question 4) impact relationship governance. This has the potential to provide important knowledge about how to apply a strategic positioning framework in a relationship governance context.

Relational capability is hypothesized to positively affect both relational and formal contracts. Similar justifications are given for including these relations in the model. Chapter 4.2 outlined the theoretical reasons for believing that organizational capability considerations are relevant when studying governance of channel relationships. The testing of these two relations will give us knowledge about how a firm's relational capability relates to channel governance (research question 3). The full conceptual model is shown below.



PART III

7 METHODOLOGY

This chapter presents the research design, the empirical setting, data collection procedures, and measurement of the variables. The first section lays out criteria for choosing research designs, and then argues that the correlational design is the only real alternative for the chosen model. The second section describes the empirical setting, whereas the third section describes sample frame and procedures. The fourth section addresses measurement issues, the fifth section deals with control variables, and the sixth section describes and presents some considerations around the data collection procedures.

7.1 *Research design*

When designing a research project, there are a number of designs among which to choose. What is the most appropriate design depends on the features of the model. This model is a causal one, and the objective is to test the causal relations of the model. What designs are available for this purpose? And on what basis should a choice be made among these alternatives? It is most convenient to start with the latter. The relevant criteria for choosing a research design are those of validity and causality. In the following these criteria will be presented and discussed in this context. Further, the criteria will be used to make a choice among the design alternatives which are found available. Finally, the chosen design will be evaluated along the validity and causality criteria.

7.1.1 **Criteria of validity and causality**

According to McGrath (1982), “[t]he research process can be viewed as a *series of interlocking choices*, in which we try *simultaneously to maximize several conflicting desiderata*” (p. 69, *original emphasis*). The desiderata to which he refers are various forms of

validity. According to Cook and Campbell (1979), there are mainly four forms of validity; statistical conclusion, internal, construct, and external validity. Statistical conclusion validity refers to whether it can be assumed covariation between two variables. Internal validity is concerned about the relationship between the two variables; given that they covary, can it be claimed that the changes in the independent variable produces the changes in the dependent variable? This implies that (i) the effect of other factors must be ruled out, and (ii) directionality must be established. Construct validity is related to the “confounding” problem; can the measures of the constructs be construed otherwise? External validity is related to the generalizability of the results.

Ideally, a study should score high on the dimensions of all these forms of validity. Doing so is not possible, because of the true dilemmas with which researchers are presented (McGrath 1982). Typically, if a study scores high on one type of validity, it does so at the expense of other(s). For example, increasing construct validity by having multiple measures is likely to decrease the motivation to fill out the questionnaire and then introduce halo or bias (Mitchell 1985). Hence, an important part of the research process is to make grounded choices; one should focus on scoring high on the types of validity that are especially important given the purpose of the study (Calder et al. 1981). In this study the purpose is to test a model. This implies an explicit focus on construct validity and internal validity while at the same time keeping statistical conclusion validity sufficiently high. External validity is not of priority²⁰.

The assumption about causality is central in the theoretical model. To understand the nature of causality as used in research models, one must focus on its three components; isolation, association, and direction of influence (Bollen 1989). Isolation means that other influences except from those included in the model, are ruled out. Association means that there is a covariation between the presumed cause and effect. Direction of influence means that the presumed cause precedes the presumed effect in time. Of these three criteria, association is related to statistical conclusion validity, whereas isolation and directionality are most related to internal and construct validity. The research designs available in social science vary in regards to the degree to which they are able to deal with these criteria. However, given a pre-specified significance level and obtained variances, the association criterion seems to be

²⁰ This compromise is generally accepted in the social sciences; “[f]ew theories specify crucial target settings, populations, or times to or across which generalization is desired. Consequently, external validity is of relatively little importance. In practice it is often sacrificed for the greater statistical power that comes through having isolated settings, standardized procedures, and homogeneous respondent populations” (Cook and Campbell 1979: 83). It may seem that external validity is sacrificed for the sake of increasing the other types of validity. Instead, external validity can be established through many studies in different contexts.

the most easy to establish whatever research design is used. The isolation and directionality criteria are more difficult to deal with.

7.1.2 Research designs – options and choice

There are three broad categories of quantitative research designs among which to choose; the classical experiment, the quasi-experiment, and the non-experimental field study. Generally, the classical experiment is preferred over the rest because this design allows the strongest test of the theory (Calder et al. 1981). The non-experimental field study is the least preferred for the same reason. Below I will explain why it was still necessary to choose the latter among the three on this occasion.

The classical experiment allows the researcher to control the situation, use standardized procedures, manipulate the treatment while controlling the stimuli imposed on the respondents, and compare groups having received different stimuli. This makes the classical experiment superior in terms of both (i) minimizing the possibility of spurious effects on the dependent variable, as well as (ii) establishing that the independent variable (cause) precedes the dependent variable (effect) in time (Calder et al. 1981). In effect, this means that the threats to the internal validity are minimized (Cook and Campbell 1979). Further, the laboratory setting provides the researcher with the opportunity to get multiple operationalizations of the different variables at a lower cost than in the field, thus facilitating better statistical conclusion validity and construct validity (Calder et al. 1981).

The downsides of the classical experiment for testing causal models are just as obvious. The biggest obstacle is the need to reproduce complex social events (e.g., cross-border B2B relationships) in laboratory settings. Also, given that it actually was possible to arrange such settings, the limited time perspective of the classical experiment makes it very difficult to study variables which develop slowly over time (e.g., relational norms and relational capability), especially when firms represent the level of analysis (McGrath 1982). Due to these obstacles, the classical experiment is not regarded as an available option.

In *the quasi-experiment*, the classical experiment is “brought out” to natural settings, while still preserving the main idea of the classical experiment (Campbell and Stanley 1963). The researcher is assumed a large degree of control of some of the variables, whereas some other variables cannot be controlled. If the critical variables can be controlled to a large degree, the

same kind of *ex ante* manipulation and *ex post* comparison are assumed as under the classical experiment. Hypothetically, such a setting would keep internal, statistical conclusion, and construct validity at high levels, while at the same time making the setting more natural.

Unfortunately, the obstacles of the quasi-experiment in this context rule it out as an available alternative. Using such a design for the model in this study would imply that the levels of relational capability and asset specificity were to be manipulated in a subset of the groups, and then the effect on the governance mechanisms should be studied *ex post*. The time perspective issue would also be a major obstacle in regards to this design. Alternatively, the researcher could be provided access to a large number of situations wherein these processes occurred naturally. None of these possibilities are available, eliminating the quasi-experiment as a realistic option.

The *non-experimental field* design is left as the only available category of design. In this category there are a number of options. To demonstrate direction of influence some sort of panel design should be applied, i.e., the researcher should collect observations from at least two periods in order to statistically demonstrate that the alleged cause precedes effect. Unfortunately, the time and resources available for this study rule out this option. We are then left with the correlation design as the only available design for testing the model quantitatively.

7.1.3 The correlation design

As the correlation design seems to be the weakest design available for testing causal models, it is important to be aware of its limitations, and take the necessary actions to cover up for these. In this regard, Campbell and Stanley (1963) and Cook and Campbell (1979) have provided a checklist for researchers applying an experimental design. Mitchell (1985) developed a similar guide for researchers using a correlational design. In the following I will evaluate the degree to which a correlational design satisfies the criteria of causality and validity of the research model.

To establish *isolation* one needs to rule out other explanations for the correlation between the independent and dependent variable. Such elimination appears difficult in correlational research, and the most salient threat to internal validity (Mitchell 1985). Nevertheless, the widespread use of the notion of ‘*ceteris paribus*’ indicate that researchers regard the criterion

to be met. How can they do that? Often, actions are taken in order to cover up for the weaknesses of the design. According to Cook and Campbell (1979), “the threats can be ruled out in nondesign ways. This is especially the case when particular threats seem implausible in light of accepted theory or common sense or when the threats are validly measured and it is shown in the statistical analysis that they are not operating” (p. 96). Hence, the necessary actions to be taken appear to be systematic thinking and theory review to identify third variables, and then either (i) demonstrate theoretically that the threats identified through this process seem implausible, or, even better, (ii) measure these variables and show *ex post* through statistical analysis that they do not have any effect. In this study, both these actions are undertaken in order to strengthen the design in regards to the isolation criterion.

As mentioned earlier, *association* seems to be the easiest criterion to fulfill. If changes in the independent variable are associated with changes in the dependent variable, one can claim that the two variables are related. In order to obtain such association, the researcher faces two important requirements when studying inter-organizational relations.

First, a certain degree of variance over critical constructs is needed (Calder et al. 1981). For example, if the chosen industry generally has not done any adaptations towards its most important customers, the variance of asset specificity may be too small. This is a critical aspect, because asset specificity is assumed to be the main driver away from arms-length relationships and towards the adoption of more complex governance mechanisms. Considering the current account of distribution channel studies, it seems that sufficient levels of variance over the critical variables (formal and relational contracts, asset specificity, and product differentiation) will be obtained in most contexts. Further, theory states that a firm’s relational capability is heterogeneously distributed within any industry (see, e.g., Wernerfelt 1984; Slater and Narver 1994), and that market attractiveness varies across markets (cf. Porter 1985). For these reasons, variance of the critical variables should be expected in most contexts.

Second, it is important that the inter-organizational relationship has existed long enough so that the values of the independent and dependent variables have been allowed to change, adapt, and reach a stable state (system equilibrium). Normal practice in correlational studies is to assume that this equilibrium has been achieved in the empirical context. Some corrective measures can be taken, however. It is important to realize that reaching this equilibrium takes time. Accordingly, there is to be a time lag between the changes in the independent variable and the resultant effect on the dependent variable. In this study, it is

assumed that product differentiation impacts asset specificity which in turn impacts formal and relational contracting. The first relation is positively moderated by market attractiveness. Relational capability is assumed to positively impact both formal and relational contracts. Also, it is assumed that product differentiation has a direct effect on relational contracts. Of these relations, it seems that relational contracts need the longest time to develop and reach a stable equilibrium; the actors need time to develop mutually accepted norms as responses to increased needs. In this study, this matter is dealt with by restricting the focus to relationships having lasted more than three years.

Concerning the *directionality* criterion, there is an old saying that correlation does not prove causation, because the correlational design does not enable the researcher to meet the third criterion, i.e. that of directionality of influence. As there should be a time lag between the alleged cause and effect, simultaneous relations are ruled out (Bollen 1989). For this reason, McGrath (1982) describes the design as a 'blunt instrument' for interpreting the causal direction (p. 82). The researcher has no opportunity to establish on statistical grounds whether the relationship is one way or the other, or, alternatively, reciprocal. Instead, the researcher has to draw on earlier substantive or theoretical work, or alternatively, on its own logic.

Most empirical work on antecedents to relationship governance has used a cross-sectional approach. Therefore, little empirical evidence exists which can prove that the directionality of the hypothesized relationships. Accordingly, I have to resort to theory or logic when claiming the directionality of the relationships. In regards to using theory as a basis for such claim, the underlying theoretical rationale of the different associations have been laid out throughout chapter 2-6. Theory, then, supports the directionality. If these a priori statements are supported in the correlational design, this confirmation should give support to the directionality claim on the basis of theory. Is this enough? Hoyle (1995) stated that the "use of theory to justify an inference of directionality is the most problematic because often there are competing theories that offer different account of the association among two or more variables" (p. 10). However, if such other theories could be ruled out, the theoretical claim can be made. Do such other theories exist? One obvious candidate is the industrial organization paradigm. Is it possible from this perspective to argue that formal contracting leads to higher degrees of asset specificity? To my knowledge, no. Similarly, if one cannot provide theoretical argumentation behind an opposite directionality for the other hypothesized relationships, this should support the claim of directionality of the hypotheses on the basis of theory. To my knowledge, such theories are not available. Similar conclusion is made in

regards to claiming the directionality on the basis of logic. To my knowledge, it is not possible to logically deduce the hypothesized influences, but in the opposite direction²¹. Naturally, the power of this statement rests fundamentally on the ability of others to prove the existence of such theories, then providing rival, but reciprocal explanations with theoretical rigidity.

7.1.4 Summary

To sum up, only the classic experiment has the qualities that make the researcher able to infer causality. In this context, however, only the correlational design was available as a research design. This leaves me with moderate abilities to establish isolation and association, and weak abilities to establish causality; when applying a correlational design, the researcher is left with establishing association rather than causation on statistical grounds. However, one may strengthen the directionality argument on theoretical and logical grounds; to my knowledge, no other theories provide causal explanations with close to the same strength as is demonstrated in chapter 2 through 6. Also, if the hypotheses are empirically supported, this should lend increased support to the causality argument on the basis of theory.

7.2 Empirical setting

Calder et al. (1981) made a fundamental distinction between two types of application in research. The first type is called *effects application*, the focus of which is a desire for knowledge about some particular real-world context. The second type is called *theory application*, and refers to the desire for more general and scientific knowledge about the real world. This type of research calls for falsification procedures to test the particular theory or model in a certain context. As argued earlier, the purpose of this project is theory testing, hence, the study must be classified as a theory application.

The theories from which the different elements of the research model were attained are general. To test this model, internal validity and statistical conclusion validity have priority over external validity. This means that it is important that the sample has variation over the variables at focus, and that the sample is as homogenous as possible for other non-relevant factors (Calder et al. 1981). This dual goal is often a trade-off for the researcher; sampling

²¹ An exception might be the effect of asset specificity on relational contracting.

from a heterogeneous population is likely to ensure sufficient variation over the focal theoretical variables, but an unfortunate side-effect is that variation over extraneous variables increases. On the one side, if the population is too homogenous, sufficient variation over critical variables is not likely to be obtained. On the other side, if the population is too heterogeneous, it will be more difficult to (i) rule out alternative explanations, as well as (ii) establish any statistically significant effects of the focal independent variables in the model.²²

If the researcher is aware of these dangers, one can make sure that the chosen mix of industries gives variation over critical variables while extraneous sources are kept as constant as possible. The chosen industries in this study are the Nordic wood products industry and the Norwegian fish industry. These firms are for the most part small and medium-sized firms²³. They are mostly old and traditional firms with local production units and administrative units with a small number of people responsible for sales, procurement, budgeting etc. Only a small number of firms have foreign sales offices and just a very few of them have made any form of vertical integration backwards in the chain (this would imply that they took care of the management of the natural resources in the first stage of the value chain). The firms sell products based on renewable resources. Services are generally not a part of their offerings. Most firms have been exporting for a lot of years, and their export products can be described as everything from highly differentiated products to pure commodities.

However, there are also some differences between the different industries in the sample. For example, the degree to which the different 'clusters' of firms have involved in any long-term committed customer relationships vary, as does also their experience with the initiation and management of such relationships. Norwegian wood products exporters often have limited international experience with closer, long-term international customer relationships, their export share is often not more 30-40%, meaning that their main focus is the domestic market (Jakobsen et al. 2001; Bunkholt et al. 1999). The Swedish and Finnish wood products exporters are often bigger, they have often larger export shares, and they have long experience with managing closer international customer relationships (Jakobsen et al. 2001; Juslin and Hansen 2003). Norwegian fish exporters also often have long experience with managing closer international customer relationships, and they have often very high

²² A 'side effect' of increased heterogeneity is that the external validity of the study increases (see Calder et al. (1981, 1982, 1983), Lynch (1982, 1999), McGrath and Brinberg (1983), and Winer (1999) for a discussion of this issue). As argued earlier, external validity is not of importance. Instead, external validity can be established by doing several similar studies in different contexts.

²³ However, some forest products firms are very big, and have offices and production units in several countries. In these cases, I have sampled on each exporting business unit, i.e. treated each business unit as one case.

export shares, sometimes up to 100%. This makes it one of the most export-intensive industries of Norway. Some of the exporters have involved in closer customer relationship with investments on both sides of the relationships, but there are great internal differences as well among the fish exporters (Hammervoll 2003). Note, however, that these considerations are more general trends, and that each of the industrial 'clusters' is far from homogenous along the variables at focus in this study. Overall, the firms appear to meet Calder et al.'s (1981) recommendation; they share a lot of features related to non-relevant factors, whereas the focal variables appear to show a certain degree of variance.

Originally, the Nordic wood products industry constituted the empirical setting. The Norwegian fish industry was included due to a wish to secure a large enough sample to enable a test of the theoretical model. The desire for a single-industry homogenous setting was then traded off against the need for a larger sample. Obviously, the inclusion of another industry to the sample decreases the control over extraneous sources of variation due to industry characteristics and environmental noise. Literature in the industrial organization paradigm claims the existence of industry effects (Porter 1980; 1990). For instance, the degree of competitive intensity in the market is assumed to affect the importance of delivering differentiated products to the customers (Fornell 1992), thus indirectly increasing the degree to which the respective governance mechanisms are relied on. Alternatively, one could argue that higher degrees of competitive intensity in the market should increase the seller's desires to forge a closer relationship to the customer, because the latter's higher number of alternatives might increase its inclinations to behave opportunistically. Hence, the degree of competitive intensity may be associated with both the independent and dependent variable in the model. If such effects could be predicted through systematic thinking a priori, they could be included as control variables (see section 7.5).

Earlier was demonstrated the high degree of similarity over non-relevant factors between the two industries. Hence, even though industry effects can never be completely ruled out in multi-industry studies, I argue that such threats are acceptable in this particular context. On this basis, I claim that the trade-off made can be justified; the sample has lost some of its homogeneity in return for a larger sample which increased the probability of being able to test the model statistically.

7.3 Sample frame and sample procedures

Using various data bases on the internet, the industries were found to consist of approximately 690 business units. Most of these units were independent firms, while a smaller number of the units (mostly Swedish and Finnish saw mills) belonged to the same multinational enterprise. Only the firms that exported a larger share of their production were included in the sample²⁴. Further, the unit needed to have administrative personnel that were responsible for the exports from this unit²⁵. These requirements reduced the sampling frame to approximately 500 units.

7.3.1 Sample size

A study's appropriate sample size depends on a number of factors. In general, there is "no hard and fast rule" (Bollen 1989: 268) on which to determine the appropriate sample size. There are two alternative ways to determine the appropriate sample size. The first alternative, which may be the easiest way, is to take into account the experience from previous studies. There have been a large number of empirical studies on more or less closely related topics within distribution channel relationships. Looking at the studies, there does not seem to be any unspoken rule in this sense; the studies' sample size range from less than a hundred to more than a thousand subjects. Most studies, however, seem to have 100 cases or more.

The second alternative is to base the estimate on a number of suggested heuristics. Simulations have suggested that sample sizes should be above 100 cases in order to give reliable test statistics (Anderson and Gerbing 1984). Further, the greater number of free parameters to be estimated, the greater the sample size (n) is needed (Bollen 1989). This study has a maximum of 30 indicators to be estimated²⁶. Bentler and Chou (1987) suggested one rule-of-thumb in this regard; there should be at least a 5 : 1 ratio between sample size and the number of free parameters. Following this requirement gives a sample size of at least $5 * 30 = 150$.

When testing moderator effects in structural equation modelling, the picture gets somewhat complicated. Different testing strategies have different sample size requirements.

²⁴ Non-standard contracting practices (higher degrees of formal and relational contracting) are assumed to be too costly to set up and administer if the business governed by them is small.

²⁵ Some units had a common sales unit that was responsible for the sales. On such occasions, one person in the sales unit was identified and asked to complete the questionnaire with respect to the production unit s/he represented.

²⁶ As is normal in studies such as this one, the final measurement model may look different than what was originally intended. Also, the dimensionality of the relational contracts scale must be established through statistical analysis, so that one cannot know the number of variables in this scale. These matters will be dealt with in chapter 8.2.

Multigroup analysis may be preferred from a simplicity point of view, but splitting the sample reduces the sample size to half, at best. This study will use latent variable scores (LVS) (Jöreskog 2000) and Jöreskog-Yang's (1996) single-indicator method. According to Yang-Wallentin et al. (2003), these methods do not require very large samples (as do the full information methods, see Schumacker and Marcoulides (1998) for a review of the methods available for testing latent interaction effects in structural equation modelling). Other than saying that these methods accept smaller sample sizes, the literature does not, to my knowledge, provide any specific guidelines.

7.4 Measurement

In this section, the measurement procedures of the study are addressed. The section has two parts. First, the measurement process is described. Second, the dimensions of the relevant variables are operationalized²⁷.

7.4.1 The measurement process

The measurement process starts with the concept that you want to measure. When you have identified the concept, there are four steps to follow (Bollen 1989: 180):

- (1) give the meaning of the concept
- (2) identify the dimensions and latent variables to represent it
- (3) form measures
- (4) specify the relation between the measures and the latent variables

The first two steps of this process were accomplished in the theoretical part of the dissertation. First, all of the theoretical constructs (concepts) were defined and explained in precise terms. Second, the dimensions and latent variables representing the construct were explained. In this case, all of the variables except relational contracts were found a priori to have only one dimension²⁸. As there needs to be one latent variable for each dimension of the

²⁷ The questionnaire is presented in Appendix A. Here is the full set of measures representing the constructs of the study. Note that the questionnaire is presented in Norwegian, even though the questionnaires also had Swedish, and Finnish wordings. English translation of the measures used in this study can be found in appendix B.

²⁸ The dimensionality of relational contracts will be addressed in chapter 8.2.1.

construct, there is only one latent variable per construct. Hence, the model contains six latent variables.

The third step of Bollen's (1989) procedure is to form the measures. In a classic article, Churchill (1979) claimed that "the use of different definitions makes it difficult to compare and accumulate findings and thereby develop syntheses of what is known ... [In fact] ... researchers should have good reasons for proposing additional *new* measures given the many available for most marketing constructs of interest" (p. 67). Similarly, in cases where the existing measures do not appear appropriate, the researcher needs to present convincing arguments why any new measure should be adopted over the old one(s). Accordingly, constructs in other empirical studies should be replicated wherever possible. On the basis of theory, operational definitions²⁹, and operationalizations in previous empirical studies, construct item pools were created. From this pool, items that did not fit the context at hand were eliminated. Then, the pools of the remaining items were subjected to a number of peer review iterations by using some academic experts in the field, as well as four people with special knowledge of the empirical context. During this process, ambiguous questions and inappropriate vocabulary were detected, and some obviously irrelevant items were eliminated. Further, the questionnaire was pre-checked through in-depth interviews with three export sales managers in different companies. During these interviews, the wording of the items was checked, study objectives were discussed in general terms, and information regarding the relational capability scale was solicited. Overall, none of the existing items at that point appeared irrelevant in the interviews.

Even though the small number of cases (three interviews) made it impossible to validate the measures statistically, the collected information enabled inspection of item content and variation, as well as a check if the constructs appeared to have sufficient convergent and divergent validity (smaller intraconstruct variation and larger interconstruct variation). As the scales of the constructs were largely established in the literature, I claim that it is less necessary to conduct formal statistical tests to ensure convergent and divergent validity.

Step four was to specify the relation between the measure and the latent variable. Normally, a measurement model is constructed to formalize these relationships. I will present the measurement model in chapter 8.2. At this stage, two brief comments can be made. First,

²⁹ "The operational definition describes the procedures to follow to form measures of the latent variable(s) that represent a concept" (Bollen 1989: 181)

all of the latent variables were measured using reflective rather than formative scales³⁰. Second, all of the observed variables were measured by perceptual data.

7.4.2 The measures

According to Peter (1979): “most constructs by definition are too complex to be measured effectively with a single item, and multi-item scales are necessary for appropriate reliability and validity assessment” (p. 16). Bollen (1989) suggested that a confirmatory factor analysis model, which will be assessed in chapter 8, should incorporate at least two indicators per latent variable. However, most methodologists recommend at least three, because “[r]esearch strategies with two indicators have the potential for analytic complications resulting from empirical underidentification” (Jaccard and Wan 1996: p. 69). Accordingly, the operationalizations of the constructs in the model are all multi-item constructs, with three or more items. The measures are presented below. Measures of the dependent variables are presented first, followed by the measures of the independent variables

7.4.2.1 Dependent variables

Formal contracts

The formal contracts scale refers to the extent to which the inter-organizational relation is regulated by rules, procedures, and fixed policies. The literature appears quite consistent in the operationalization of this scale (see, e.g., Haugland et al. 2004; Lusch and Brown 1996; Heide and Weiss 1995; Bello and Gilliland 1997; Heide 2003; Buvik and Haugland 2003; Bucklin and Sengupta 1993; Klein 1989; Paswan et al. 1998; John 1984; Dwyer and Oh 1987,

³⁰ In a reflective scale all observed indicators are viewed as being caused by some underlying common dimension or construct (Bagozzi and Fornell 1982; Fornell and Bookstein 1982). Hence, each item is assumed to share a common core. An increase in the value of the construct translates into an increase in the value for all items representing the construct. Formative scales are used when a construct is viewed as an explanatory combination of its indicators (Bagozzi and Fornell 1982; Fornell and Bookstein 1982). The construct is not assumed to have a common dimension. The construct is defined as a total weighted score across all the items. Each of the items represents an independent dimension in its own right. Collectively, they exhaust the entire domain of the construct, i.e. they represent all its relevant aspects. Assuming that the items are independent, each item contributes to the total score of the construct regardless of the value of the other indicators. The different assumptions underlying each type of scale imply fundamentally different procedures when testing their validity. Formative scales are typically validated a priori on the basis of theory and expert opinion (e.g. Rossiter 2002), and unidimensionality is not an issue. In contrast, reflective measures are tested for unidimensionality a posteriori using a range of techniques, among which factor analysis is the most common in inter-organizational empirical research. As all the latent variables were measured using reflective scales, tests for unidimensionality by the use of, for instance, factor analysis will have to be conducted for all variables.

1988; Dahlstrom et al. 1996). Based on this literature, a scale was developed. The items are listed below (5 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

1. There is a written agreement that specifies the tasks and responsibilities of each party.
2. How to handle the day-to-day management of the relationship is expressed in a written agreement.
3. There are rules and procedures for most issues in this relationship.
4. It is expected that both parties behave according to the agreement.
5. It is important for us to behave formally accurate as according to the agreement.

Relational contracts

Relational contracts are beliefs shared to some extent by members of a social unit as to what conduct ought to be in particular situations or circumstances (cf. Gibbs 1981). These beliefs are related to the actors’ desire to carry on and further develop the relationship, as well as their willingness to make adaptations in the face of new contingencies. As no particular norm is focused on in this study, it was considered important to include aspects of the most commonly reported dimensions. For this purpose, two approaches seemed most relevant. First, a number of studies have formed a second-order construct, with solidarity, flexibility, and information exchange as first-order dimensions (cf. Heide and John 1992). A second approach has been to form a unidimensional construct of different items with wording similar to two or more of these aforementioned different norms of behaviour (see, e.g., Lusch and Brown 1996; Cannon et al. 2000; Poppo and Zenger 2002; Haugland et al. 2004). What approach to follow is an empirical matter. Hence, both approaches were accommodated in the measure development procedure; a multi-item scale was developed, using the measures developed by Heide and John (1992) and Heide and Miner (1992)³¹. The items are listed below (13 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

³¹ Note that these scales has been applied by a number of studies, including Lusch and Brown (1996), Antia and Frazier (2001), Bello et al. (2003), Joshi and Stump (1999a), Noordewier et al. (1990), and Heide and Miner (1992); Heide and John (1990); Rokkan et al. (2003); Joshi and Stump (1999c); Kim (2000).

1. We expect this relationship to last a long time.
2. We assume that renewal of agreements with this supplier will generally occur.
3. We make plans for the continuance of our relationship with this supplier, and not only for individual orders.
4. Problems that arise in the course of this relationship are treated by the parties as joint rather than individual responsibilities.
5. The parties are committed to improvements that may benefit the relationship as a whole and not only the individual parties.
6. The responsibility for making sure that the relationship works for both of us is shared jointly.
7. Flexibility in response to requests for changes is a characteristic of this relationship.
8. We expect to make adjustments in the ongoing relationship to cope with changing circumstances.
9. When some unexpected situation arises, we would rather work out a new deal together than hold each other to the original terms.
10. In this relationship, it is expected that any information that might help the other party will be provided to them.
11. Exchange of information in this relationship takes place frequently and informally.
12. It is expected that the parties will provide proprietary information if it can help the other party.
13. It is expected that we keep each other informed about events or changes that may affect the other party.

Asset specificity

The asset specificity scale refers to the extent to which physical and material assets are tailored to a specific relationship. Williamson (1985) identified four types of specificities; site specificity, physical asset specificity, human asset specificity, and dedicated assets. There appears to be considerable agreement in the literature in regards to the operationalization of this variable (see, e.g., Heide and John 1990; Buvik and John 2000; Jap and Ganesan 2000; Stump and Heide 1996; Haugland et al. 2004; Joshi and Stump 1999; Rokkan et al. 2003; Heide 2003). Based on this literature, a scale was developed. The items are listed below (4 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

1. In order to deliver to this customer it has been necessary to make special investments or adaptations in equipment.
2. It has been necessary to give employees who are working with this customer special training
3. It has been necessary to adapt our production system in order to deliver to this customer.

4. In order to deliver to this customer we have made specific investments or adaptations in our distribution systems.

7.4.2.2 Independent variables

Product differentiation

A firm following a product differentiation strategy wishes to create a unique image for its products (Porter 1980). The product differentiation scale refers to the extent to which the product was differentiated compared to products offered by competitors, or if it was a homogeneous product. This construct has been measured in a variety of ways, depending on the focus and context of the study. Hence, it was decided that primarily previous studies with a similar focus and distribution channel context should be relied on. Some of these (Anderson and Coughlan 1987; Coughlan and Flaherty 1983; Coughlan 1985) used a dummy variable as a proxy for differentiation, whereas other studies (Aulakh and Kotabe 1997; Aulakh et al. 2000; Myers and Harvey 2001; Haugland et al. 2004) used a multi-item scale. The latter category of studies was relied on in the development of the following scale (4 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

1. When buying this product, price is the only factor of real importance (R).
2. Our product is different from products offered by our competitors in this foreign market.
3. Our strategy can be best described as maintaining higher quality standards for our products.
4. When buying this product, there are more factors than price of real importance.

Relational capability

In this study, relational capability refers to the firm ability for initiating, developing, and maintaining B2B relationships. The construct is conceptualized in terms of broad experience with some aspects relevant for the handling of the customer relations, including selection of customers, negotiation of future exchanges, maintenance of the relationship, as well as broad, general experience with management of similar inter-firm exchanges. On this basis, a scale was developed. The items are new, but inspiration has been gained from a number of studies, including Delios and Henisz (2000), Leiblein and Miller (2003), Reuer et al. (2002), and Korth (1991). The items are listed below (3 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

1. We have broad experience with establishing and maintaining foreign customer relationships.
2. We have broad experience with negotiating with foreign customers.
3. Our firm has broad international experience.

Market attractiveness

Market attractiveness refers to “the potential for the market to contribute to overall corporate objectives” (Burke 1984: 347). The studies by Burke (1984) and Genturck and Aulakh (1995) were taken as basis when constructing the scale. Majumdar and Ramaswamy (1995) was also a source of influence. On the basis of these empirical works, a scale was developed. The items are listed below (4 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

1. There are prospects for great future profits in this market.
2. This market has a great demand potential.
3. This market will have a strong growth in the future.
4. Average margins in this market are high.

7.5 Control variables and rival predictors

In section 7.2, I argued that the industry mix both (i) ensured a sufficient variation over the focal theoretical variables, as well as (ii) appeared to be rather homogeneous over extraneous sources. As an additional step, I collected data on potential extraneous variables, so that the potential effect of these variables could be ruled out statistically. Doing so is necessary in order to, first, meet the requirement of isolation and identify potential causes of spurious associations, and second, meet the requirement of association and reduce the error term in the statistical model.

I collected data on variables that might be correlated with the dependent variable(s). I included variables from both the same theoretical perspective(s) as well as other paradigms. In regards to variables from other perspectives, I considered theories that offer competing explanations for varying degrees of governance mechanisms. If explanations from such theories can be ruled out statistically, the confidence in the theoretical model increases (Meehl 1990; Jöreskog and Sörbom 1993). In this dissertation, variables from the same perspective(s)

will be called control variables, whereas variables from paradigms offering competing explanations for governance mechanisms will be called rival predictors. Below, I will present variables from each of the categories.

7.5.1 Control variables

Customer asset specificity (CAS)

According to the theory, the customer's transaction specific investments may be correlated with higher degrees of formal contracting. Further, studies have demonstrated high correlation between the transaction specific investments of the seller and the customer (Heide and John 1990; Stump and Heide 1996; Ganesan 1994; Anderson and Weitz 1992). In turn, such correlation may have a negative effect on the degree of formal contracting, because the parties possess mutual hostages, which have an opportunism-curbing effect (Williamson 1983). Being correlated with both an independent and a dependent variable, the customer's transaction specific investments are a potential source of spurious associations and must be controlled for. A scale was developed by relying on a number of earlier empirical studies (Heide and John 1990; Jap and Ganesan 2000; Anderson and Weitz 1992; Stump and Heide 1996; Ganesan 1994; John and Weitz 1989; Rokkan et al. 2003). The items are listed below (4 item, 7-point scale, anchored by "to a very low degree" and "to a very high degree").

1. This customer has made significant investments in equipment towards our firm
2. This customer has given special training to employees that work towards our firm
3. This customer has done special adaptations in internal process in concern for the relationship to our firm
4. This customer has made adaptations in their distribution systems towards our firm

Environmental uncertainty (EU)

"There is ample support in the organization and institutional economics literatures that uncertainty is a key environmental dimension affecting organizations (their structure and internal processes), interorganizational relations, and the mode and costs of transacting" (Achrol et al. 1983). Given that asset specificity is present to a non-trivial degree, relationship continuity matters. Under such conditions, higher levels of environmental uncertainty results in an adaptation problem, because individuals face increased difficulties in specifying

contractual agreements *ex ante*. Such difficulties may have serious consequences. First, higher degrees of environmental uncertainty make it “more imperative that the parties devise a machinery to “work things out”- since contractual gaps will be larger and the occasions for sequential adaptations will increase in number and importance as the degree of uncertainty increases” (Williamson 1985: 60). Second, a “changing environment presents numerous occasions for agents to shirk and to renegotiate to their advantage” (Anderson and Gatignon 1986: 15). Environmental changes quickly render a simple contract unable to deal with changed circumstances. Hence, the firm is induced to increase control by making the contract more complex to cover every thinkable contingency. In this context, this means that the degree of formal contracting should increase. The following argumentation may also be carried out; in situations characterized by higher degrees of environmental uncertainty, firms have incentives to retain flexibility and lower the degree of contractual specificity (Balakrishnan and Wernerfelt 1986; Afuah 2001; Kogut 1991; Folta 1998), while also investing less in transaction specific assets (Mahoney 1992). Accordingly, environmental uncertainty must be included as a control variable.

Environmental uncertainty is defined as “the degree to which future states of the world cannot be anticipated and accurately predicted” (Pfeffer and Salancik 1978: 67). In their seminal article, Rindfleisch and Heide (1997) stated that “[a]mong all the TCA constructs, environmental uncertainty seems to be the most problematic from a measurement standpoint” (p. 42). Hence, the operationalization of the environmental uncertainty construct deserves extra attention.

When operationalizing the environmental uncertainty construct, the researcher must make a number of choices. First, one has a choice between treating the construct as an objective or perceptual measure. In this situation, one must keep in mind that the individual decision makers obviously base their decisions on their perceptions, not on some objective numbers (cf. Heide and John 1995)³². Regarding environmental uncertainty as inherently “in the eye of the beholder” (Wathne 2001: 40) is also in accordance with the transaction cost literature, although this literature stream has not directly addressed this issue (Sutcliffe and Zaheer 1998).

³² In this regard, Schommer (1995) states, in a review on the environmental uncertainty construct, that “[e]nvironmental uncertainty should not be viewed as just a property of the environment, but rather of the individual faced with a decision in his or her perceived environment” (p. 61). This contrasts some research within the strategy genre, which has relied on an objective measure of EU (e.g. Balakrishnan and Wernerfelt 1986; Child 1972; Keats and Hitt 1988).

Second, there is a need to determine in relation to what *sources* the construct should be studied, as well as the *types* of environmental uncertainty on which to focus related to these sources (Wathne 2001). In regards to the former, the environmental uncertainty construct should be studied in relation to the downstream foreign customer market. In regards to the latter, one must keep in mind that Pfeffer and Salancik's (1978) definition is relied on. Accordingly, customer market unpredictability seems to be the appropriate type of uncertainty on which to focus.

Having made these clarifications, previous studies' operationalizations of the construct were reviewed and a scale was constructed. From this pool of studies, some of them were selected; John and Weitz (1988, 1989), Wathne (2001), Celly and Frazier (1996), Anderson (1985), Haugland and Reve (1994), Buvik and Grønhaug (2000), and Heide and John (1990). On the basis of these studies, the following scale was constructed (3 item, 7-point scale, anchored by "to a very low degree" and "to a very high degree").

1. Market demand is hard to predict
2. The sales for this market is hard to predict
3. The competition in this market is hard to predict

Opportunism (OPP)

In this study, the construct of opportunism refers to "taking advantage of opportunities with little regard for principles or consequences" (Macneil 1981: 1023) or "self-seeking behaviours with guile" (Macneil 1981; Wathne and Heide 2000; Williamson 1975). Opportunism may destroy the cooperative climate of the relationship, and is then likely to be negatively related to relational contracts. Rokkan et al. (2003) developed a scale on the basis of a number of works (John 1984; Dwyer and Oh 1987; Anderson 1988; Provan and Skinner 1989; Gundlach et al. 1995; Brown et al. 2000), while still adding two new items to reflect Wathne and Heide's (2000) updated conceptualization of the construct. As Rokkan et al. (2003) reported success with this measure, their operationalization is adopted herein. The items are listed below (6 item, 7-point scale, anchored by "to a very low degree" and "to a very high degree").

1. On occasion, the customer lies about certain things in order to protect their interests.
2. The customer sometimes promises to do things without actually doing them later.
3. The customer does not always act in accordance with our contract or agreement.

4. The customer sometimes tries to breach informal agreements between our companies to maximize their own benefit.
5. The customer will try to take advantage of “holes” in our contract to further their own interests.
6. The customer sometimes uses unexpected events to extract concessions from our firm.

7.5.2 Rival predictors

Ethnocentricity

Ethnocentricity refers to the degree to which the local culture’s behaviour is characterized by the attitude that its own culture is superior. If the local culture is very ethnocentric, it is hard for foreign companies to be perceived as socially acceptable. The international business literature is full of examples where “things have gone wrong” due to misunderstanding the local customs and the local way of doing business, and misapprehensions of the value and implications of cultural values and norms in various contexts in general. The evidence of the importance of conforming to the local social expectations to gain legitimacy is overwhelming (see Deresky 2000 for a review).

If the local culture is characterized by ethnocentricity, the exporter may hesitate to enter closer relationships characterized by higher degrees of asset specificity, because it may not feel comfortable with making such investments in environments with such normative impediments. Accordingly, the construct is included as a control variable. On the basis of Yiu and Makino (2002), the following scale is constructed (2 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

1. Foreigners are often treated differently than local citizens in this market
2. In this market the national culture is closed towards other culture

State influences

State influences refer to the extent to which local regulative forces influence the activities of foreign firms in a host country. Yiu and Makino (2002) found that state influences had a significant positive impact on the choice of joint venture over wholly owned subsidiaries, i.e., higher degrees of state influences leads to less hierarchical contractual agreements. Likewise,

one might argue that stronger state influences make it more difficult to cooperate closely with a local customer. This might lead the manufacturer to invest less in a particular customer relationship, because of fearing that the local state might interfere, so that investments are lost. Likewise, one might claim that such conditions make it more difficult to develop higher degrees of contractual specificity and relational sentiments (see e.g., Grewal and Dharwadkar 2002). As the construct may negatively impact the dependent variables in the model, the construct is included as a control variable. On the basis of Yiu and Makino (2002), the following scale was constructed (3 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

1. Official bureaucracy makes it more difficult to export to this country
2. National protectionism makes it more difficult for us to export to this country
3. Governmental interference make it more difficult for us to export to this country

Customer dependence

Customer dependence is defined as the extent to which a manufacturer needs to maintain an exchange relationship with its exchange partner in order to reach its desired goals (Frazier 1983). If the supplier cannot easily replace the customer, the power relationship becomes asymmetric. Bello et al. (2003) found that such dependence tended to strengthen the relational bonds with its customer. The customer dependence construct is also frequently studied in distribution channel contexts (see, e.g., Bello et al. 1991, 2003; Sachdev et al. 1995; Boyle and Dwyer 1995; Dant and Schul 1992; Kim 2002; Johnson 1999; Joshi and Stump 1999c; Jap and Ganesan 2000; Ganesan 1994; Ross et al. 1987; Lusch and Brown 1996). As the construct may be correlated with one or both of the dependent variables, it needs to be included as a rival predictor of these. On the basis of the aforementioned studies, the following scale was constructed (4 item, 7-point scale, anchored by “to a very low degree” and “to a very high degree”).

1. Should the sales to this customer cease, it would be difficult for us to find alternative purchasers
2. Should the sales to this customer cease, we would face economic problems
3. We are dependent on this customer
4. There are other similar firms that may replace this customer (R)

7.6 Data collection

In this study, archival data was not available, so I had to collect primary data. Considering the nature of the variables, the use of structured questionnaires and key informant technique was assumed to be the only realistic option for a large-scale data collection. In the following the key informant technique will be presented, some relevant issues will be discussed, and, finally, the sampling procedures will be outlined.

7.6.1 Key informant technique

The key informant technique has been the most common technique when collecting data on the most common variables of interest for researchers on inter-organizational relations. The technique involves relying on one or a few individuals with special knowledge about the phenomena of interest for the researcher (Seidler 1974). The selection of informant is made on the basis of their allegedly unique knowledge of and ability to describe the phenomenon. Most often, Campbell's (1955) classic criteria for picking informants are relied on; one should identify and select individuals that are both (i) knowledgeable about the phenomena at focus and (ii) able and willing to communicate about them.

When using the key informant technique, it is assumed that the context of inquiry makes the representative survey respondent unable to provide in-depth information, so that reliance on key informants is the only alternative available. At the same time, this collection strategy requires that the characteristics of the phenomena reported by the informant exist independently of the organization members (Heide and John 1995). If the respondents typically provide information about themselves (e.g. job satisfaction), i.e. information that does not exist independently of the individual reporting on them, the researcher needs to obtain information from a representative sample of individuals belonging to the organization to which the reported phenomenon applies (Wathne 2001). In this context, the attributes of (i) the organization, (ii) the organization's relation to its most important foreign customer, and (iii) the market in which this customer operates, can be assumed to exist independently of the informant(s) reporting these attributes³³. Accordingly, the researcher can select informants on the basis of their alleged knowledge instead of their representativeness in a statistical sense.

³³ Exceptions may be the 'relational capability' and 'relational contracts' constructs if the key informant has been in the organization for a long time and represents the firm's only contact to international customers. However, in

7.6.2 Number of informants per each organization and unit of analysis

On a number of occasions, researchers have addressed the issue of whether the respondents provide valid information of the characteristics of the phenomena on which they report (John and Reve 1982; Brown and Lusch 1992; Heide and John 1995). Given the difficulties involved in providing information on complex issues, relying on one informant only implies that the researcher are left in the dark in regards to the accuracy of these data. Hence, it might be beneficial to obtain information from multiple informants on each case and then conduct some sort of cross-informant data validation for each business case by examining the convergence of the different reports given.

In general, the researcher can choose to (i) recruit one or more informants from each organization, as well as (ii) collect data on one or both sides of the dyad. Both these issues have been subjected to debate for a long time (see, e.g., Bagozzi et al. 1991; Philips 1981; John and Reve 1982; Brown and Lusch 1992; Heide and John 1995). In regards to the former, Phillips (1981) found low convergence among informants representing the same unit, and concluded that single-informant designs were suspect. Contrary to his recommendation of using multiple informants design, however, the use of single-informant design continues to be the dominant approach. There are two primary reasons for this inclination. First, time and resource constraints limit the use of such an approach in surveys. When using only one informant, the data can be registered directly on the basis of the report of that informant rather than aggregating the reports of multiple informants of the firm. This keeps the investigation at the structural level and saves money in the data collection process (Seidler 1974). Second, multiple informants in each unit may not be an option, because some firms may only “establish one person as the focal point for relations with a given supplier” (Heide and John 1990: 31) or customer. Other persons are only partially involved and do not actually qualify as key informants. In my case, both these types of limitations made me disregard more than one informant per organization as a viable alternative.

In regards to the latter, the matters seem more intricate. On the one hand, there seems to be obvious arguments for collecting data on both sides of the dyad. Consider, for example, the case of governance mechanisms. TCE holds that the most appropriate mix of governance mechanisms will prevail, because other forms have been ruled out by selection mechanisms.

these cases, it would not be a better choice to ask a random informant, because s/he would possess far less knowledge about the phenomena.

There are reasons to believe that *both* parties contribute to the overall constitution of these mechanisms. As there are potential discrepancies between how the parties perceive the issues of interest, it seems appropriate to collect data from both sides of the channel dyad so that the researcher may validate the data from one side against those from the other, in order to obtain an objectively more 'correct' value. A number of empirical studies have followed this approach (e.g. Reve 1980; Haugland 1988; Heide and John 1990; Anderson and Weitz 1992; Heide and Miner 1992; Nygaard 1992). On the other hand, if these discrepancies can be assumed to be of minor character, a single-side approach is sufficient. In my case, there are indications that this may be the case. Empirical studies have demonstrated correspondence between measures of variables such as vertical interaction, formalization, and centralization from both sides of the channel dyads. John and Reve (1982) reported that "[t]he results indicate that the key informants from different firms within channel dyads provided reliable and valid data about the structural form of the relationship..." (p. 522). Reve (1980) reported similar results. Anderson and Weitz (1992) studied and found empirical support for correspondence between buyer's and seller's perception of the counterpart's idiosyncratic investments and commitment in the relationship. Hence, there seems to be some evidence that, to some extent, there is a correspondence between buyer and seller perceptions of some of the variables in the model. On the basis of these empirical findings, it seems to be justifiable to sample from one side only in regards to these variables.

In addition to such empirical considerations, there are both practical and theoretical reasons for why sampling on one side only is the best choice in this particular context. In regards to the former, there are great practical obstacles associated with two-sided sampling. First, emphasis must be put on keeping the parts together in the analysis process. Second, the informants must select a contact person of the counterpart and agree upon the participation of this person. This task is complicated when dealing with cross-border relations³⁴. As the response rate of the sample of channel dyads is the product of the response rates of informants on each side of the dyad, this rate is obviously sensitive to refusal on either side (Buvik 1995). Issues related to confidentiality may also be aggravated if the counterpart is participating (Churchill 1979). In regards to the latter, sampling from both sides is not theoretically relevant for most variables in this particular context. In this study, the seller is assumed to deploy specific governance mechanisms as responses to some *perceived* changes in the level of the independent variables; the action taken by the organization is assumed to depend on

³⁴ Considering the highly international nature of the industries, the appointed customer would be in countries all over the world. The questionnaire would then have to be translated to all of the respective languages.

how that person perceives the level of transaction specific investments and differentiation of the product sold. Hence, the relevant values of the key independent variables are those perceived by the 'eye of the beholder', i.e. the exporter³⁵. How the customer perceives the levels of those variables would in this case not only be irrelevant but might also be misleading³⁶.

In conclusion, multi-informant sampling from each organization is practically impossible in my case, due to the small administrative units of the organizations. Further, one-sided sampling was chosen because (i) empirical evidence suggests that it is acceptable to collect data from one side only, (ii) two-sided sampling is theoretically irrelevant for most constructs, and (iii) the great practical difficulties associated with two-sided sampling on international relations are avoided.

7.6.3 Sampling procedures

A number of researchers have highlighted the key informant selection and recruitment as a critical part of the sampling procedures when deploying the key informant technique (John and Reve 1982; Kumar et al. 1993). For example, John and Reve (1982) reported "that careful selection of informants in conjunction with the use of internally consistent multi-item scales can provide reliable and valid data in a variety of channel settings" (p. 522). In this study, the 'marketing manager' or 'managing director'³⁷ of each company was contacted, as this person was assumed to meet Campbell's (1955) criteria to the largest degree. The wood products companies were all contacted by phone, and asked to participate if they were exporting regularly. On the basis of this process, a large number of potential cases were eliminated because they did not export on a regular basis. As we had more information about the Norwegian fish companies beforehand due to earlier similar studies, and as more information

³⁵ See Heide and John (1995) for more on this matter. They claimed that "firms will act upon their specific interpretation of a situation, regardless of whether the firm's perception is accurate or converges with that of its exchange partner. For the purpose of predicting responses to dependence, an individual firm's perception is, for all practical purposes, 'truth'. As such [...] dyadic comparisons may sometimes be meaningless" (p. 543-544).

³⁶ On the other hand, if the theoretical model had contained any variables that by definition are 'true dyadic traits', for example joint utility, it would be advantageous to tap the counterpart's evaluation of the construct to construct a score (Wathne 2001). There are no such dyadic properties in the theoretical model, maybe apart from the relational norms construct. One might argue that this is a true dyadic construct due to its bilateral nature. However, even though it might be theoretically relevant to sample on both sides in regards to this variables, the great practical difficulties still makes doing so a very difficult matter.

³⁷ Note that most of the companies in the population were small- and medium-sized companies. Often, they did not have a manager whose task and responsibility were the management of the relationships to foreign customers only. Rather, the managing director, or a general marketing director, was often the most appropriate informant.

was provided on their websites and on website of the Norwegian Seafood Export Council, these companies were only contacted by email.

In addition to the questionnaire, the packet contained a prepaid envelope, a cover letter, and a recommendation letter from the respective industry associations. To motivate the informants to respond a customized report was offered in return, which would describe the main results of the study and compare the respondent's reported data with the average.

On the basis of telephone and e-mailing rounds, a number of the 500 business units were eliminated from the population because they did not export on a regular basis, they had ceased to operate, or they made it clear that they did not want to participate in the study in the initial recruiting process. Also, a number of business units were eliminated from the population because they did not have administrative personnel responsible for exporting; being part of a multinational company, they left these tasks to a centralized function. After eliminating these business units, 395 units were left, making up the final population. Several call-ups and e-mailing rounds were conducted in order to increase the response rate. In total, 170 questionnaires were returned. 5 of them were not included due to excessive missing data, 2 were eliminated because the firm was not operative at the time of answering, and 3 were eliminated because the firm was considered too small (1-3 persons). 160 usable questionnaires were then used in the later analyses. The final response rate making up a final response rate is then 42%, which ranges favorably compared to similar channel studies.

PART IV

8 ANALYSIS

This chapter has four sections. The first section has some preliminary discussion and evaluates the descriptive statistics for the individual observed variables. LISREL 8.54 is used in the second section to establish a measurement model using confirmatory factor analysis, as well as in the third section to test the direct effects model. Finally, a summary of the results are provided.

8.1 *Descriptive statistics*

In general, the first step in any multivariate analysis is to inspect the input data and check their adequacy (Hair et al. 1998). According to West et al. (1995), “one major source of inappropriate usage [of multivariate techniques] has been the failure of investigators to satisfy the scaling and normality assumptions upon which estimation and testing are based” (p. 56). The adequacy can be assessed in terms of whether the input data meet some of the assumptions of multivariate analysis. The most common estimators, such as maximum likelihood and normal theory generalized least squares, assume the data are continuous and have a multivariate normal distribution. Often, applications of multivariate techniques to real data involve violations of these assumptions. Such violations may be serious as they affect the performance of the estimators, such as for example maximum likelihood (ML) and generalized least squares (GLS) for a variety of CFA models³⁸.

The Likert scales, which are most often used in empirical studies such as this one, are ordinal and not continuous. However, instead of treating the variables as ordinal, one usually assumes that there is a continuous variable underlying the ordinal variable, and formulates the measurement model in terms of the underlying continuous variable (e.g., Jöreskog 1993; Muthén 1984). This study will proceed likewise. Further, given that the data approximate a continuous scale, one must assure that the data does not depart too much from normality. By

³⁸ See West et al. (1995) for a review of studies examining the performance of such estimators under diverse conditions of nonnormality.

inspecting descriptive statistics of the data, deviations from normality can be detected. In particular, high kurtosis and high skewness indicate non-normality, because they cause biased parameter estimates, and then also unreliable standard error and overall model fit (Bagozzi and Yi 1988). Accordingly, data with high skewness or high kurtosis should be preferably deleted from further analysis.

The descriptive statistics of the data is reported in table 8.1. Overall, the data do not seem to suffer from non-normality. Some exceptions must be made. INFOEX4, RELCONT2, RELCONT3 have high kurtosis values and must be treated with caution in the following. Missing values is not a problem either. Only 5 cases were deleted due to an excess of missing values. Some of the cases had one or two missing values, whereas most of the questionnaires were fully completed. The pattern of missing data for the non-excluded cases was evaluated to be random, so that missing data on the remaining questionnaires was replaced by the mean of the observed variable.

Table 8-1: Descriptive statistics of the sample

	Mean	Std.dev.	Skewness	Kurtosis
Formal contracts				
FC1	4,46	2,45	-0,40	-1,52
FC2	3,34	2,25	0,40	-1,43
FC3	4,21	2,09	-0,21	-1,29
FC4	5,18	2,18	-1,00	-0,47
FC5	4,94	2,18	-,77	-0,85
Relational contracts				
SOL1	5,64	1,24	-0,76	-0,04
SOL2	5,94	1,01	-1,37	3,41
SOL3	5,91	1,03	-0,98	0,95
FLEX1	5,64	1,11	-0,83	0,70
FLEX2	5,23	1,36	-0,84	0,60
FLEX3	4,54	1,73	-0,49	-0,60
INFOEX1	5,61	1,22	-1,03	1,08
INFOEX2	5,61	1,33	-1,25	1,63
INFOEX3	5,61	1,29	-1,21	1,73
INFOEX4	5,79	1,19	-1,54	3,28
RELCONT1	6,16	0,93	-1,32	1,97
RELCONT2	6,09	1,12	-1,97	4,98
RELCONT3	6,22	1,06	-2,08	5,49
Asset specificity				
AS1	3,41	2,08	0,33	-1,23
AS2	3,68	2,11	0,18	-1,35
AS3	3,14	2,03	0,59	-0,96
AS4	3,18	1,90	0,47	-1,01

Product differentiation					
PD1 ^a	3,58	1,49	0,09	-0,67	
PD2	3,69	1,92	0,11	-1,24	
PD3	4,70	1,65	-0,63	-0,31	
PD4	5,42	1,43	-0,97	0,72	
Market attractiveness					
MA1	3,99	1,53	-0,02	-0,42	
MA2	4,89	1,37	-0,31	-0,54	
MA3	4,45	1,23	-0,06	-0,01	
MA4	3,54	1,53	0,23	-0,65	
Relational capability					
CAP1	5,68	1,37	-1,30	1,61	
CAP2	5,67	1,42	-1,31	1,41	
CAP3	5,64	1,49	-1,12	0,67	

^aReversed item

8.2 Measurement models for the theoretical model

When testing latent variable models, the issue of model fit is a major complication. If the model does not fit the data, this lack of fit can be attributable to an ill-fitting measurement model, an ill-fitting structural model, or both. Accordingly, the model should be tested in two stages; first one must assess the fit of the measurement model, and second, given that the measurement model has been confirmed, one can move on to inspect the a priori hypothesized structural paths (Gerbing and Anderson 1988).

Because the latent variable structural model incorporates the measurement model, the fit of the latter gives a baseline for the fit of the full latent variable model, which incorporates both the structural and measurement relationships. This means that the structural model cannot provide a better fit to the data than does the measurement model (Kelloway 1998). According to Jöreskog (1993), it may even be meaningless to test the structural model unless one has confirmed that the measurement model holds in the population. If the pre-specified indicators do not measure the construct they are intended to measure, the measurement model must be modified before one can move on to the structural model.

Accordingly, the set of a priori indicators making up the variables of the pre-specified theoretical model (see section 7.4.2) are subjected to a number of tests. Overall these tests are

assessing the overall fit of the model, the reliability and validity of the latent variables, and the reliability of the individual observed variables³⁹.

8.2.1 The overall measurement model

First, the dimensionality of the relational contracts scale is addressed. Second, the unidimensionality of the *a priori* identified measures are identified by inspecting various goodness-of-fit indices. Third, the constructs' reliability and validity are assessed. Finally, some comments are made to sum up.

8.2.1.1 The dimensionality of the relational contracts scale

In regards to the relational contracts construct, different practices have been followed. Often, relational contracts or the like (relational norms, relational governance etc) have been measured in terms of the different norms of behaviour, such as solidarity, mutuality, information exchange, conflict avoidance, relationship continuity, flexibility etc. Another normal approach has been to form a second-order construct with solidarity, flexibility, and information exchange as first-order dimensions (cf. Heide and John 1992). Yet, a third approach has been to form a unidimensional construct of a set of different items with wording similar to two or more of these aforementioned different norms (see, e.g., Lusch and Brown 1996; Cannon et al. 2000; Poppo and Zenger 2002; Haugland et al. 2004).

This study seeks to examine antecedents to relational contracts, considering such a contract to describe the extent to which the channel members share a belief as to what conduct ought to be in particular situations or circumstances. As no particular norm is focused on, it seems appropriate to create a construct which includes elements from a number of central norms. For this purpose, one may construct a second-order construct, following the practice of Heide and John (1992). Another approach is to construct a reflective scale which taps elements from a number of different norms, i.e. collapse items of flexibility, solidarity, information exchange, and long term orientation into one reflective construct (see, e.g. the aforementioned studies for similar approaches). Yet a third is to form a formative construct with such items if any of the reflective scales do not show internal consistency. Ultimately,

³⁹ ML is chosen as the estimator throughout the different parts of the analysis. According to Hoyle and Panter (1995), there is a "growing body of research indicates that ML performs reasonably well under a variety of less-than-optimal analytic conditions (e.g., small sample size, excessive kurtosis)" (p. 164). It also seems to perform better than generalized least squares (GLS) and asymptotic distribution-free (ADF) estimators. Hence, results from ML should be routinely reported.

what approach to follow is an empirical matter. Hence, the different alternatives are subjected to empirical tests using the confirmatory factor analysis technique in LISREL for each of the alternatives, and then comparing their goodness-of-fit indices⁴⁰.

The first measurement model subjected to testing was the three-dimensional relational contracts scale. The a priori model showed an unsatisfactory RMSEA measure. One item was excluded. The measures improved, but RMSEA was still rather unsatisfactory, while the other measures showed a good fit. As all scales had three items, further deletions were unwarranted. Accordingly, the model fitting procedure was stopped with model 2.

Table 8-2: Three-dimensional relational contracts scale

	Goodness of fit	Specification
Model 1	$\chi^2 = 78.56$ $df = 32$ RMSEA = 0.109 NNFI = 0.91 CFI = 0.94 IFI = 0.94	a priori measurement model
Model 2	$\chi^2 = 52.63$ $df = 24$ RMSEA = 0.098 NNFI = 0.93 CFI = 0.95 IFI = 0.95	INFOEX3 excluded

The second scale was constructed by taking one item from each of the different dimensions of relational contracts – solidarity, flexibility, information exchange, and relationship continuity. All thirteen a priori items on the relational contracts were thrown into the analysis.

⁴⁰ See appendix D for a justification of the choices of global fit criteria. A description of the criteria with accompanying cut-off rates is also offered.

Table 8-3: One-dimensional relational contracts scale

	Goodness of fit	Specification
Model 1	$\chi^2 = 68.31$ $df = 27$ RMSEA = 0.112 NNFI = 0.91 CFI = 0.93 IFI = 0.93	a priori measurement model
Model 2	$\chi^2 = 21.13$ $df = 15$ RMSEA = 0.064 NNFI = 0.98 CFI = 0.99 IFI = 0.99	FLEX2, FLEX3, and RELCONT1 deleted
Model 3	$\chi^2 = 0.66$ $df = 1$ RMSEA = 0.000 NNFI = 1.03 CFI = 1.00 IFI = 1.01	FLEX2, FLEX3, SOL3, INFOEX2, and SOL1, and RELCONT3 deleted

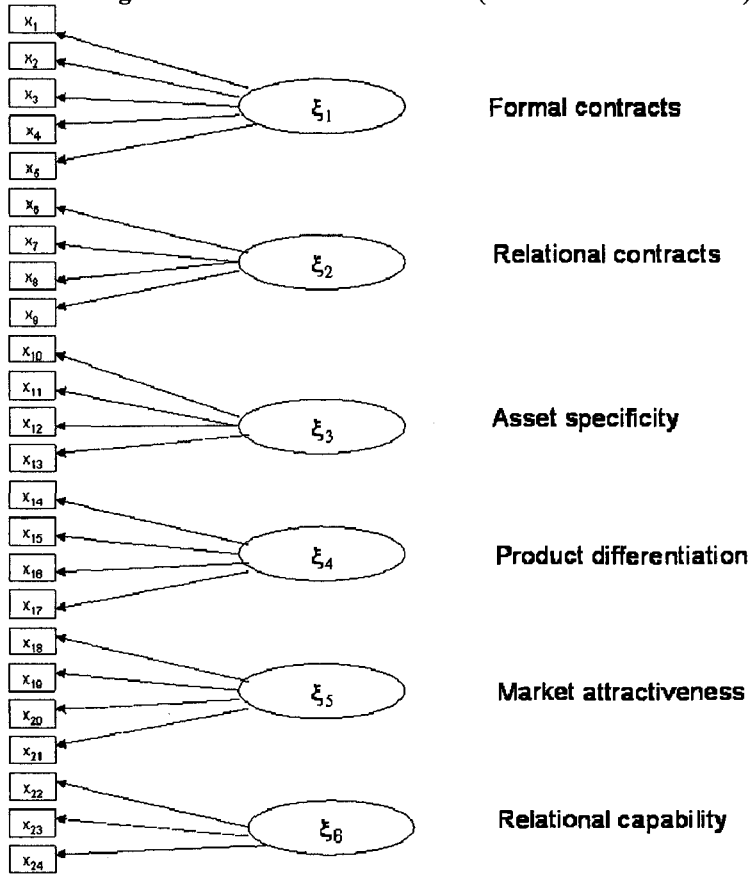
Table 8.3 shows that the first model is not satisfactory. The modification indices showed that FLEX2, FLEX3, and RELCONT3 did not seem work. Deleting these items drastically improved the fit, but the RMSEA measure was still somewhat high. SOL3, INFOEX2, SOL1, and RELCONT3 were deleted to further improve the fit. The final model shows close to perfect fit. Hence, this scale was chosen as the final relational contracts scale. This implies that relational contracts will be treated as a unidimensional construct in the further analyses.

8.2.1.2 Assessment of overall model fit

The latent constructs in the measurement model are formal contracts ($\xi_1 = FC$), relational contracts ($\xi_2 = RC$), asset specificity ($\xi_3 = AS$), product differentiation ($\xi_4 = PD$), market attractiveness ($\xi_5 = MA$), and relational capability ($\xi_6 = CAP$). These latent constructs, along with their observed indicators, make up the *a priori* measurement model (see figure 8.1), which is to be subjected to testing. The constructs themselves were allowed to freely

correlate, so that the covariance matrix of the constructs was unconstrained. Doing so allows the strongest test of the measurement model (Jöreskog 1993: 297).

Figure 8-1: Measurement model (evaluative dimensions)



A number of models were subjected to testing, and their measures of overall fit are reported in table 8.4. The first model is the a priori identified measurement model. As table 8.4 displays, the model scored poor on all dimensions. RMSEA suggests that the fit is mediocre, whereas NNFI, CFI, and IFI all recommend that the model should be rejected.

In this situation, I follow the recommendations by Gerbing and Anderson (1988). They stated that, “[g]iven a converged and proper solution but unacceptable overall fit, there are four basic ways to respecify indicators that have not “worked out as planned”; relate the indicator to a different factor, delete the indicator from the model, relate the indicator to multiple factors, or use correlated measurement errors” (p. 417). Of these, the first two ways

are preferred because they preserve unidimensionality. The last two ways do not preserve unidimensionality, because they may obfuscate the meaning of the underlying construct.

Accordingly, in the pursuit of getting a good model fit one should inspect modification indices of the measurement model, and look for high crossloadings with other latent constructs and/or items which appears to share a lot of the variance in their error terms. In such cases, pure statistical considerations suggest that one should consider letting such construct(s) be related to that factor instead of the original, or one should delete the construct. However, theoretical matters must also be taken into account in this model-fitting process;

“The evaluation of the model and the assessment of fit are not entirely statistical matters. If the model is judged not to be good on substantive or statistical grounds, it should be modified within a class of models suitable for the substantive problem. The goal is to find a model within this class of models that not only fits the data well from a statistical point of view, taking all aspects of error into account, but also has the property that every parameter of the model can be given a substantively meaningful interpretation” (Jöreskog 1993: 307).

An inspection of the observable variables in the *a priori* model gives the conclusion that none of them can be justifiably related to another construct on a theoretical basis. However, as all latent variables are multi-item constructs, one may justify a deletion of one or a few troublesome observed variables. Following Jöreskog (1993), the important matter in this regard is - is the theoretical meaning of the latent variable retained if the troubled observed variable is deleted? If the meaning of the latent variable *is* retained, the deletion of the observed variable can be justified on a theoretical basis. Moreover, if a good model fit is obtained by such theoretically justified deletion of observed variables showing (i) high crossloadings to other latent variables and/or (ii) correlated error terms with other observed variables, the use of correlated measurement errors may be avoided altogether⁴¹.

Inspecting the modification indices, it appeared that observed variables x_{12} (AS3) and x_{14} (PD1) were especially troublesome, having correlated error terms with error terms of a

⁴¹ Note that allowing correlated measurement errors is problematic, because so doing obfuscate the meaning of the underlying construct. In fact, Gerbing and Anderson (1988) suggested that allowing such correlation is only justified when specified a priori.

number of other observed variables from other latent constructs. Further, deleting these observed variables can be justified on a theoretical basis; observed variable x_{14} (PD1) is the reverse of observed variable x_{17} (PD4), and when deleting x_{12} (AS3), there are still three observed variables left of the asset specificity latent variable. Hence, the meanings of the theoretical constructs should be more or less retained by deletion of these observed variables.

Rerunning the measurement model without x_{12} (AS3) and x_{14} (PD1) resulted in some better measures overall, but the fit was still considered to be unsatisfactory (see table 8.4, model 2). An inspection of the modification indices showed that observed variable x_4 (FC4) had correlated error terms with a number of other observed variables. As the formal contracts scale has five items, and observed variable x_4 (FC) is largely reflected in the other observed variables for this scale, x_4 (FC4) is deleted from further analysis.

Rerunning the measurement model without x_4 (FC4), x_{12} (AS3), and x_{14} (PD1), gave an improved model fit; all measures reported acceptable fit, but the cut-off rates were only marginally passed (see table 8.4, model 3). Accordingly, modification indices were inspected again in order to identify other observed variables of which a deletion could be theoretically justified. The observed variable x_{21} (MA4) was identified as the biggest source of problems. As the meaning of the theoretical construct was more or less the same without this item, a deletion of this observed variable in order to improve model fit can be justified.

Rerunning the measurement model without x_4 (FC4), x_{12} (AS3), x_{14} (PD1), and x_{21} (MA4) gave a good model fit on all the reported indices (see table 8.4, model 4). An inspection of the modification indices revealed that x_{23} (CAP2) and x_{24} (CAP3), as well as x_3 (FC3) and x_5 (FC5), had some correlated error terms. Letting the error terms of these observed variables correlate might then increase model fit. This was done in a final attempt to improve model fit. Table 8.4 shows that the fit was only marginally improved. As previously argued, letting error terms correlate should be avoided due to the potential loss of interpretability and theoretical meaningfulness (cf. Gerbing and Anderson 1988). Because a good overall model fit is achieved without doing so, I choose not to allow such correlations in the final model. Hence, model 4 is chosen as the final measurement model of the evaluative dimensions of the constructs in the study.

Table 8-4: Fit indices of measurement models

	Goodness of fit	Specification
Model 1	$\chi^2 = 543.38$ df = 237 RMSEA = 0.090 NNFI = 0.88 CFI = 0.90 IFI = 0.90	a priori measurement model
Model 2	$\chi^2 = 410.67$ df = 194 RMSEA = 0.084 NNFI = 0.89 CFI = 0.91 IFI = 0.91	x12 (AS3) and x14 (PD1) excluded
Model 3	$\chi^2 = 309.66$ df = 174 RMSEA = 0.070 NNFI = 0.92 CFI = 0.93 IFI = 0.93	X12 (AS3), x14 (PD1), and x4 (FC4) excluded
Model 4	$\chi^2 = 270.22$ df = 155 RMSEA = 0.066 NNFI = 0.93 CFI = 0.94 IFI = 0.94	X12(AS3), x14 (PD1), x4 (FC4), and x21 (MA4) excluded Chosen model
Model 5	$\chi^2 = 256.66$ df = 153 RMSEA = 0.063 NNFI = 0.94 CFI = 0.96 IFI = 0.96	X12(AS3), x14 (PD1), x4 (FC4), and x21 (MA4) excluded Allowed correlated error terms between x24 and x25 (CAP2 and CAP3), as well as between x3 and x5 (FC3 and FC5)

8.2.1.3 Reliability

As it is possible that the global measures of fit indicate a satisfactory model but the internal structure of the model is unsatisfactory, the internal fit of the model needs to be assured. The assessment criteria suggested by Bagozzi and Yi (1988) were followed. First, the parameter estimates and accompanying test of significance should be inspected; the λ 's should preferably be greater than 0.6 and significant by the t -tests. Second, the individual item reliabilities should be examined. Third, scale reliabilities of the latent constructs should be above 0.6⁴², and fourth, the average variance extracted should be above 0.50.

Table 8.5 presents the information of interest. Overall, the items and scales showed good scores along the dimensions of interest. One item, item $\lambda_{2,2}$, appears to be troublesome; this item has rather low factor loading, high error term and low item reliability. Deleting this item would mean that an important facet of relational contracts, i.e. flexibility, is lost. Hence, the item is retained in the analysis. Comments are also needed on the relational contracts scale. The average variance extracted is low. The composite reliability of the scale, however, indicates satisfactory scale reliability.

⁴² To investigate scale reliability, I used the procedure suggested by Raykov (2003). Check appendix E for information about this procedure.

Table 8-5: The measurement model - reliability measures and factor loadings

<u>Factor loadings^a</u>			<u>Error term^a</u>			Item reliab- ility	Average variance extracted	Scale reliab- ility	Highest shared variance
Estimate	<i>t</i> -values	Estimate	<i>t</i> -values						
Formal contracts									
$\lambda_{1,1}$	0.84	12.56	$\theta_{1,1}$	0.30	6.55	0.60			
$\lambda_{2,1}$	0.87	13.27	$\theta_{2,1}$	0.25	5.85	0.75			
$\lambda_{3,1}$	0.80	11.65	$\theta_{3,1}$	0.37	7.18	0.67	64%	.86	50%
$\lambda_{4,1}$	0.73	10.26	$\theta_{4,1}$	0.47	7.80	0.53			
Relational contracts									
$\lambda_{1,2}$	0.69	8.70	$\theta_{1,2}$	0.52	6.43	0.48			
$\lambda_{2,2}$	0.45	5.23	$\theta_{2,2}$	0.80	8.28	0.20			
$\lambda_{3,2}$	0.65	8.08	$\theta_{3,2}$	0.58	6.97	0.42	41%	.63	23%
$\lambda_{4,2}$	0.73	9.24	$\theta_{4,2}$	0.46	5.85	0.54			
Asset specificity									
$\lambda_{1,3}$	0.81	12.12	$\theta_{1,3}$	0.34	7.05	0.76			
$\lambda_{2,3}$	0.84	12.68	$\theta_{2,3}$	0.29	6.61	0.71	76%	.89	50%
$\lambda_{3,3}$	0.91	14.27	$\theta_{3,3}$	0.18	4.62	0.82			
Product differentiation									
$\lambda_{1,4}$	0.85	12.02	$\theta_{1,4}$	0.28	4.64	0.68			
$\lambda_{2,4}$	0.82	11.46	$\theta_{2,4}$	0.33	5.41	0.67	58%	.78	38%
$\lambda_{3,4}$	0.61	7.98	$\theta_{3,4}$	0.62	7.97	0.38			
Market attractiveness									
$\lambda_{1,5}$	0.75	10.33	$\theta_{1,5}$	0.44	6.85	0.56			
$\lambda_{2,5}$	0.80	11.22	$\theta_{2,5}$	0.36	5.79	0.64	65%	.83	2%
$\lambda_{3,5}$	0.87	12.45	$\theta_{3,5}$	0.24	3.92	0.76			
Relational capability									
$\lambda_{1,6}$	0.93	15.59	$\theta_{1,6}$	0.13	6.64	0.87			
$\lambda_{2,6}$	0.99	17.45	$\theta_{2,6}$	0.01	0.89	0.99	89%	.96	14%
$\lambda_{3,6}$	0.91	14.85	$\theta_{3,6}$	0.18	7.59	0.82			

8.2.1.4 Validity

The next step is to establish the construct validity of the scales, i.e., establish that the meaning of the underlying factor correspond to the construct of interest. We investigated the convergent and discriminant validity of the scales. Convergent validity was assessed by evaluating the statistical significance of each indicator’s estimator pattern coefficient, i.e., whether the τ -values of the λ ’s are significant. These values are reported in table 8.5. All values were significant.

Discriminant validity was established by two procedures. First, I assessed it by using the 95% confidence interval around the correlation estimates for each of the latent constructs, ξ ’s. If none of the 95% confidence intervals include 1.0 (absolute value), then no pairs of constructs are perfectly correlated within the range of random sampling error, and discriminant validity can be claimed. LISREL provides the necessary information in the Φ matrix, when all latent variables are considered to be ξ variables (no structural paths are imposed on the model). The Φ matrix is presented below (table 8.6). As demonstrated by this table, none of the correlations +/- two standard errors include 1 (absolute value), so that the latent construct show satisfactory discriminant validity. Second, I established discriminant validity using Fornell and Larcker’s (1981) test. I calculated the shared variance between all possible pairs of constructs and verified that these variances were lower than the average variance extracted for the individual constructs. Table 8.5 shows that all possible pairs of factors passed this test; none of the squared correlations are higher than the average variance extracted for the particular construct.

Table 8-6: Estimated correlation matrix between latent variables

	FC	RC	AS	PD	MA	CAP
FC	1.00					
RC	.43 (.08)	1.00				
AS	.71 (.05)	.37 (.09)	1.00			
PD	.49 (.07)	.48 (.08)	.62 (.06)	1.00		
MA	.05 (.09)	.06 (.10)	.13 (.09)	.14 (.09)	1.00	
CAP	.24 (.08)	.37 (.08)	.13 (.08)	.24 (.08)	.08 (.09)	1.00

8.2.2 Concluding comments on the measurement model

As is common in studies such as this one, the pre-specified measurement model did not show acceptable fit, and a series of respecifications had to be done in order to reach at a measurement model with good overall fit (Gerbing and Anderson 1988). This measurement model was evaluated to be good in terms of overall fit, the reliabilities for each of the individual observed variables and latent variables are satisfactory, and the construct validities of the constructs have been confirmed through assessing convergent and discriminant validity.

Models are fitted to data in an attempt to understand better the underlying processes that have been operating. Good models should be parsimonious (superfluous parameters should be avoided), and crossloadings or correlated error terms should be avoided to retain interpretability (Browne and Cudeck 1993). The previous sections have demonstrated that this model satisfies these criteria. This observation lends considerable confidence in stage two of the analysis, i.e., in the assessment of the structural paths of the model.

8.3 Structural analysis

In the following, the structural paths in the model are assessed using structural equation modeling (SEM). The advantages of SEM over multiple regression analysis are undisputable. First, SEM has the ability to estimate a complete model incorporating both measurement and structural considerations at the same time. The program enables a simultaneous assessment of both the quality of the measurement and the predictive relationships among the (latent) constructs. This approach “offers the considerable advantage of estimating predictive relationships among “pure” variables that are uncontaminated by measurement error” (Kelloway 1998: 3).

Second, SEM provides an assessment of the overall model fit as well as for each of the free parameters. This is critical, as it may be meaningless to test the structural model unless one has confirmed that the measurement model holds in the population (Jöreskog 1993).

Third, SEM offers an analysis of all structural paths in the model at the same time, whereas in multiple regression analysis the researcher has to regress on each dependent variable. Interdependencies among the endogenous variables are then dealt with in a single estimation, so that a test of the overall model is provided in addition to a test of the individual

hypotheses (Sandvik 1998). In this case, this is important, because asset specificity is posited as a mediator between product differentiation and formal contracts. Judd and Kenny (1981) demonstrated that the presence of measurement error in the mediator tends to produce an underestimate of the effect of the mediator and an overestimate of the effect of the independent variable on the dependent variable when all coefficients are positive (as they are in this case). Using SEM instead of multiple regression, this problem may be dealt with to a much greater extent, as interdependencies among endogenous constructs are dealt with directly and the presence of measurement error are taken into account when the parameters of the structural paths are computed.

Testing the structural paths consists of five steps. First, the direct effects of the theoretical model are tested. Second, it is tested whether asset specificity is a mediator between product differentiation and formal contract. Third, the moderator effect of the model is tested using Latent Variable Scores in LISREL. Fourth, in order to increase the confidence in the theoretical model, the effects of control variables (cf section 7.5.1) are included to test the robustness of the findings. In the fifth part, potential rival predictors (cf section 7.5.2) on varying degrees of governance mechanisms are included; if explanations of formal and relational contracts from rival theories can be ruled out statistically, the confidence in the appropriateness of the model increases (cf Meehl 1990).

8.3.1 Test of hypotheses in the direct effects theoretical model

The direct effect hypotheses of the main model were:

- H₁:** Asset specificity is positively related to formal contracts.
- H₂:** Asset specificity is positively related to relational contracts.
- H₃:** Product differentiation is positively related to asset specificity.
- H₄:** Product differentiation is positively related to relational contracts.
- H₆:** Relational capability is positively related to relational contracts
- H₇:** Relational capability is positively related to formal contracts

The results of the direct effects model are reported in the table below. The fit of the model is satisfactory along all indices reported.

Table 8-7: Structural Model of the Direct Effects

Structural linkages in the model	Hypotheses	Number sign	Parameter	Theoretical model	
				Estimate	t value
Endogenous - endogenous variables					
Asset specificity - Formal contracts	H1	+	β_{21}	0.69	8.11***
Asset specificity - Relational contracts	H2	+	β_{31}	0.14	1.22
Exogenous - endogenous variables					
Product differentiation - asset specificity	H3	+	γ_{11}	0.63	7.09***
Product differentiation - relational contracts	H4	+	γ_{31}	0.32	2.49**
Relational capability - relational contracts	H6	+	γ_{32}	0.28	3.14***
Relational capability - formal contracts	H7	+	γ_{22}	0.15	2.35**
Significance levels: $t > 1.96$: $p < 0.05^*$; $t > 2.33$: $p < 0.01^{**}$; $t > 3.10$: $p < 0.001^{***}$					
	Sq. multiple correlation for structural equation		Sq. multiple correlation for reduced form		
Asset specificity	0.39		0.39		
Formal contracts	0.53		0.24		
Relational contracts	0.31		0.30		
Goodness-of-fit indices:	$\chi^2=270.96$ ($p=0.0$) $df=161$ $RMSEA=0.066$ $CFI=0.94$ $IFI=0.94$ $NNFI=0.93$				

The table reports that all direct effects except one are supported. β_{21} , γ_{11} and γ_{32} (hypothesis 1, 3 and 6) reach support at the level of $p < 0.001$. γ_{31} and γ_{22} (hypothesis 4 and 7) get support at the level of $p < 0.01$. β_{31} (hypothesis 2) is not supported. Also, the explained variances of the endogenous variables range satisfactorily compared to other channel studies (see column “squared multiple correlation for reduced form”). The reported fit indices of the overall model are identical to those of the measurement model. As expected then, information from the modification indices report that more structural paths would not improve model fit. This gives support for the mediating role of asset specificity between product differentiation and formal contracts.

8.3.2 Testing the mediating role of assets specificity.

The theoretical model posits asset specificity as a mediator between product differentiation and formal contracts, i.e., asset specificity represents the generative mechanism through

which product differentiation is able to influence the degree of formal contracts. In the last sub-chapter I demonstrated indirect support for this mediating role, as inclusion of more paths would not improve model fit. However, in order to explicitly demonstrate that asset specificity indeed functions as such a generative mechanism, I followed the procedure described by Baron and Kenny (1986). According to this procedure, if asset specificity has a mediation effects, the following conditions must hold. First, product differentiation must affect asset specificity; second, product differentiation must affect formal contracts; and third, asset specificity must affect formal contracts. Condition one and three correspond to hypotheses 3 and 1 in the direct effects model. These hypotheses were supported, hence, these conditions hold. To check for the second condition, the LISREL model was respecified. The result is reported in the upper part of table 8.8.

Given that these three conditions hold, if there is a mediation effect, then the effect of the independent variable (product differentiation) on the dependent variable (formal contracts) should be considerably less when it is controlled for the effect of the mediator (asset specificity). Also, it is “critical that the investigator examine not only the significance of the coefficients, but also their absolute size” (Baron and Kenny 1986: 1177). The LISREL model was respecified according to these guidelines. The main effects structural model were taken as a basis, and the relation from product differentiation to formal contracts were freed. The relevant results of this run are provided below in table 8.8.

Table 8-8: Testing the Mediating Role of Asset Specificity

Checking for Condition 2:		
	Estimate	t value
Product differentiation - formal contracts	0.56	6.27***
Controlling for the mediator (asset specificity):		
	Estimate	t value
Product differentiation - formal contracts	0.05	0.53
Asset specificity - formal contracts	0.66	6.23***
Significance levels: $t > 1.96$: $p < 0.05^*$; $t > 2.33$: $p < 0.01^{**}$; $t > 3.10$: $p < 0.001^{***}$		
Goodness-of-fit indices:	$\chi^2 = 270.75$ (p=0.0) df=160 RMSEA=0.066 CFI=0.94 IFI=0.94 NNFI=0.93	

As shown, the second condition for a mediation effect holds (product differentiation has a significant effect on formal contracts). Hence, all three conditions hold for testing the

mediating role. Further, as expected, the results give strong support for the mediating role of asset specificity between product differentiation and formal contracts. Both the significance and the size of the effect of product differentiation on formal contracts fell dramatically when I controlled for asset specificity (compare the values of the effect of product differentiation on formal contracts in the upper and lower part of table 8.8).

8.3.3 Testing the moderator effect

The model posits market attractiveness as a moderator variable. What kind of moderator variable is it? Sharma et al. (1981) provided a framework for identifying moderator variables. This framework identifies three types of moderators; homologizers, quasi moderators, and pure moderators. A variable which cannot be classified as any of these three types of moderators is an antecedent, suppressor, exogenous, or intervening variable to the relationship between a predictor and a criterion.

A homologizer influences only the strength between the predictor(s) and the criterion variable(s). The form of the relationship between the predictor and criterion variables is then not modified by the homologizer. The two other types, on the other hand, have such modifying effects. Pure moderators modify the form of the relationship between the predictor and criterion. This modification is achieved through an interaction with the predictor variable. At the same time, the pure moderator is not directly related to the predictor or criterion variables. The quasi-moderator is similar to the pure moderator in that it modifies the form of the relationship between the predictor and the criterion, but it also has an interaction relationship with the predictor and a direct relationship with either of the predictor or criterion variable. The market attractiveness variable fits nicely within the pure moderator category of this framework. It does not have any direct relationship to the predictor or the criterion, it is hypothesized to have only a modifying effect (cf hypothesis 5).

Product term regression analysis is generally the recommended method for estimating interaction and moderator effects with continuous variables in multiple regression (Aiken and West 1991; Cohen and Cohen 1983; Jaccard et al 1990), and especially when sample sizes are small and the scales have good reliability (Jaccard and Wan 1996). Hence, product term analysis rather than sub-group analysis (splitting samples) was applied to test moderator effects in SEM. When applying sub-group analysis, one divides the sample into two or more groups based on some level of the moderator, and then subjects the difference in slope of the effects in each group to a test of statistical significance. When it is not theoretically

meaningful to reduce the moderator to two (or three) categories, this approach is not satisfactory (Jaccard et al. 1990).

In contrast, product term regression analysis retains the moderator in its original form and yields a more powerful test of statistical significance than does sub-group analysis. However, testing product terms in LISREL is not straightforward. Even though several procedures have been developed (e.g., Hayduk 1987, Jöreskog and Yang 1996, Bollen and Paxton 1998; Klein and Moosbrugger 2000, Algina and Moulder 2001), all of them are rather complicated to implement, and there is no consensus among researchers that any of them is optimal (Marsh et al. 2004). All these latent variable approaches require an understanding of how to specify complicated non-linear constraints (Jöreskog 1998), and are difficult to implement for the applied researcher. Furthermore, these approaches typically involve the additional difficulty of selecting which multiple indicators to form the latent constructs⁴³.

Recently, Jöreskog (2000) suggested a procedure called Latent Variable Scores (LVS). This procedure provides a vastly simplified alternative to the traditional approach to testing product terms in LISREL. In the same paper, Jöreskog provides a formal proof of the method, and Schumacker (2002) subjected the method to a preliminary test. The method has also been applied in a recent empirical study, which compared the results of three different methods of testing a product term in LISREL (Yang-Wallentin et al. 2004). The methods they applied were called the Maximum Likelihood Method (ML), the Robust Maximum Likelihood Method (RML), and the Latent Variable Scores (LVS). The methods all produced the same results in regards to the effect of the product term. Albeit simulation studies evaluating the appropriateness of this method are still missing (Yang-Wallentin et al. 2004), these considerations lends confidence in using the LVS method. Also, the LVS provides the additional benefit of circumventing the difficulty of selecting which of the many product terms to include because the relevant product term is computed directly on the basis of the latent variable scores (all possible product terms are “taken into account”). Hence, this dissertation will use this method in the testing of the moderator effect in LISREL.

The procedure suggested by Jöreskog (2000) was followed. First, the latent variable scores were computed and appended to the PRELIS file containing the data. These scores are unbiased estimates of the latent variables, and satisfy the same relationships as the latent variables themselves; the covariance matrix of these scores is equal to the estimated

⁴³ If a latent variable product term is to be formed on the basis of two 4-item constructs, the researcher has $4*4=16$ different product terms among which to choose. Alternatively, all product terms may be included, but, of course, doing so makes the specification of the syntax a very complicated matter.

covariance matrix of the reference variable scores. On the basis of these latent scores, a product term was computed between the latent scores of product differentiation and market attractiveness. Finally, a LISREL model was estimated using the latent variables scores directly, in order to assess the effect of the product term on asset specificity. As an additional check of the appropriateness of the method, the significance levels and sizes of the direct effects model computed by the two different methods ('normal' approach and LVS approach) were compared. The results of this test along with the test of the moderator effect using LVS are provided in the table below⁴⁴.

Table 8-9: Comparing values using different methods and testing the moderator effect

Structural linkages in the model	Hypotheses	Normal method		LVS method	
		Estimate	t value	Estimate	t value
Endogenous - endogenous variables					
Asset specificity - Formal contracts	H1	0.69	8.11***	0.68	12.26***
Asset specificity - Relational contracts	H2	0.14	1.22	0.10	1.24
Exogenous - endogenous variables					
Product differentiation - asset specificity	H3	0.63	7.09***	0.60	9.18***
Product differentiation - relational contracts	H4	0.32	2.49**	0.37	4.39***
Relational capability - relational contracts	H6	0.28	3.14***	0.28	4.16***
Relational capability - formal contracts	H7	0.15	2.35**	0.16	2.81**
Significance levels: $\triangleright 1.96$: $p < 0.05^*$; $\triangleright 2.33$: $p < 0.01^{**}$; $\triangleright 3.10$: $p < 0.001^{***}$					
The moderator effect		<u>Jöreskog-Yang 1996</u>		<u>LVS method</u>	
		Estimate	t value	Estimate	t value
Prod Diff * Market Attractiveness - Asset specificity	H5	0.10	0.86	0.05	0.66

As a further additional check, the product term was also estimated using the Jöreskog and Yang (1996) single-indicator method. To simplify, only three of the model variables were taken into account in the estimation; product differentiation, market attractiveness, and asset specificity. The product term was formed by the first item of both product differentiation and

⁴⁴ Fit measures are not included in the table as such considerations are not relevant when using the Latent Variable Scores (LVS) method; normal multiple regression (as in SPSS) is conducted in stage two of this method. The difference to the normal approach taken in SPSS is that (i) scores of the latent variables have been computed taking into account the issue of measurement error and heterogeneous factor loadings, and that (ii) regressions on all three dependent variables are conducted at the same time.

asset specificity. Note that the difficulty of choosing which of the observed variables to form the latent construct remains. The procedure laid out by Jaccard and Wan (1996) was followed.

In regards to the appropriateness of the LVS method, the beta values of the three methods are almost the same, whereas the significance levels changes somewhat more. All methods lead to the same conclusions in regards to the direct effects of the model. These considerations lend confidence in regards to the viability of the LVS method. Both the LVS method and the Jöreskog-Yang (1996) single-indicator method conclude that the product term does not have any effect on asset specificity. Hence, hypothesis 5 is not supported. The LISREL syntaxes for the LVS and Jöreskog-Yang (1996) methods are provided in appendix C.

8.3.4 Including control variables

The confidence in the theoretical model will increase if one takes into account the effects of some control variables that might have impact. The variables of customer asset specificity (CAS), environmental uncertainty (EU), and opportunism (OPP) are included as control variables.

Prior to controlling for the effects, a measurement model was established⁴⁵. On the basis of the final measurement model, a structural model was tested holding all paths from control variables fixed. In this test, the modification indices revealed that environmental uncertainty was significantly related to formal contracts, opportunism was significantly related to relational contracts, and customer asset specificity was significantly related to asset specificity. The paths reported to have significant impact on the dependent variables were then freed to be estimated in a subsequent run. The results of this run are provided in the table below, along with the fit indices.

⁴⁵ OPP2, OPP6, and CAS1 were eliminated, as they showed very high crossloadings to other variables. These eliminations were considered acceptable, as the spirit of the constructs was still retained. See sub-chapter 7.5.1 for the wordings of the items deleted.

Table 8-10: Including control variables

Structural linkages in the model	Hypotheses	<u>Structural model</u>		<u>Including control variables</u>	
		Estimate	t value	Estimate	t value
Endogenous - endogenous variables					
Asset specificity - Formal contracts	H1	0.69	8.11***	0.70	8.48***
Asset specificity - Relational contracts	H2	0.14	1.22	0.17	1.44
Exogenous - endogenous variables					
Product differentiation - asset specificity	H3	0.63	7.09***	0.50	5.81***
Product different - relational contracts	H4	0.32	2.49**	0.29	2.33**
Relational capability - relational contracts	H6	0.28	3.14***	0.24	2.82**
Relational capability - formal contracts	H7	0.15	2.35**	0.13	1.99*
Significant effects of control variables					
Customer asset spec - (supplier) asset specificity				0.32	3.94***
Opportunism - relational contracts				-0.30	-3.45***
Environmental uncertainty - formal contracts				-0.13	-1.92
Significance levels: $t > 1.96$: $p < 0.05^*$; $t > 2.33$: $p < 0.01^{**}$; $t > 3.10$: $p < 0.001^{***}$					
Goodness-of-fit indices: $\chi^2=542.35$ (p=0.0) df=305 RMSEA= 0.070 CFI=0.91 IFI=0.90 NNFI=0.89					

Looking at the table, we see that environmental uncertainty has a partially significant negative effect on formal contracts, opportunism has a significant negative effect on relational contracts, and customer asset specificity is positively related to (manufacturer) asset specificity.

Comparing the sizes and significance levels of the original structural paths, we see only trivial changes. All effects remain significant. This provides additional support to the model.

8.3.5 Rival predictors

Below, some potential rival predictors were included in the direct effects model. These potential predictors have been identified by taking perspective of competing theories on

channel governance. In total, three additional constructs were included; local market ethnocentricity, local state influences, and customer dependence.

Prior to evaluating the effects of these constructs, a measurement model was established. None of the a priori items of the rival predictors were eliminated. On the basis of the final measurement model, a structural model was tested, holding all paths from rival predictors fixed. In this test, the modification indices revealed that state influences was significantly related to formal and relational contracts, customer dependence was significantly related to relational contracts and asset specificity. Ethnocentricity was not reported to be related to any of the dependent variables. The model was rerun with these significant paths freed. The results of this run are reported in the table below, along with the fit indices.

Table 8-11: Including rival predictors

Structural linkages in the model	Hypotheses	<u>Structural model</u>		<u>Including control variables</u>	
		Estimate	t value	Estimate	t value
Endogenous - endogenous variables					
Asset specificity - Formal contracts	H1	0.69	8.11***	0.70	8.39***
Asset specificity - Relational contracts	H2	0.14	1.22	0.00	0.01
Exogenous - endogenous variables					
Product differentiation - asset specificity	H3	0.63	7.09***	0.58	6.89***
Product different - relational contracts	H4	0.32	2.49**	0.38	3.13**
Relational capability - relational contracts	H6	0.28	3.14***	0.26	3.22***
Relational capability - formal contracts	H7	0.15	2.35**	0.13	1.98*
Significant effects of rival predictors					
Customer dependence - asset specificity				0.30	3.84***
Customer dependence - relational contracts				0.33	3.47***
State influences - formal contracts				-0.19	-2.85**
State influences - relational contracts				-0.32	-3.84***
Significance levels: $t > 1.96$: $p < 0.05^*$; $t > 2.33$: $p < 0.01^{**}$; $t > 3.10$: $p < 0.001^{***}$					
Goodness-of-fit indices: $\chi^2=577.40$ (p=0.0) df=279 RMSEA= 0.082 CFI=0.90 IFI=0.90 NNFI=0.88					

State influences has a significant negative effect on both formal and relational contracts, and customer dependence is significantly positively related to relational contracts and asset specificity. The sizes and significance values of the original structural paths showed only trivial changes, and all of them remained significant. These results further increase our confidence in the adequacy of the theoretical model.

8.4 Conclusion

Chapter 6 presented the theoretical model that was to be subjected to empirical test. The model contained six direct effects and one moderator effect. Further, one variable was posited as a mediator between two variables. The table below presents a summary of the analysis.

Table 8-12: Summary of hypotheses

Constructs	Sign	Found	Sign. level ^a	Conclusion
H ₁ : Asset specificity - formal contracts	+	0.69 ^b	(p<0.001)	Supported
H ₂ : Asset specificity - relational contracts	+	0.14 ^b	Not support	Not supported
H ₃ : Product differentiation – asset specificity	+	0.63 ^b	(p<0.001)	Supported
H ₄ : Product differentiation - relational contracts	+	0.32 ^b	(p<0.001)	Supported
H ₅ : Market attractiveness * product diff - asset specificity	+	0.05 ^b	Not support	Not supported
H ₆ : Relational capability - relational contracts	+	0.28 ^b	(p<0.01)	Supported
H ₇ : Relational capability - formal contracts	+	0.15 ^b	(p<0.01)	Supported
Mediation role of AS between PD and FC				Confirmed

^a One tailed test

^b Standardized regression coefficients

Part V

9 DISCUSSION AND IMPLICATIONS

This chapter has four sections, of which the first provides a summary of the study. The second chapter addresses theoretical and managerial implications. The third section draws up some guidelines for future research in this area. Finally, the chapter finishes with some concluding remarks.

9.1 Summary of the study

This dissertation started with acknowledging the findings of earlier research on what makes firms form closer customer relationships. In doing so, it became clear that some important matters were left largely unanswered. Amongst others, Ghosh and John (1999) found the current TCE literature unable to answer why firms in the same industry choose very different approaches to bringing their products to market. Following TCE, all firms would choose the same approach because they all face the same exogenous attributes (Hunt and Morgan 1995). Ghosh and John (1999) posited that this theoretical problem could be solved by bringing into the TCE model elements related to the firm's heterogeneous resources and strategic positioning considerations. More specifically, they posited that differences related to positioning, customer brand equity, technology, and channel resources have impact on the extent to which the firm relies on formal and relational governance in its business relationships. Their arguments were of conceptual and anecdotal character.

This dissertation has attempted to provide statistically founded answers to a subset of Ghosh and John's (1999) original propositions, as well as what effect the perceived attractiveness of a market has. In particular I have attempted to answer the following questions;

1. Why do firms in the same industry use so different approaches in bringing their products to market?
2. How does the positioning strategy of a firm influence the design of their supply chain governance form?
3. How do the channel capabilities of a firm influence their supply chain governance form?
4. How does the attractiveness of a market influence the firms' supply chain governance form?

In so doing, I established a relationship governance *base model*, of which the robustness had been demonstrated across different settings. Such a model could serve as a theoretical anchor on which to deduce additional effects of variables from the perspectives of organizational capabilities and strategic positioning. This governance base model was constructed by reviewing the literature on inter-firm governance mechanisms. Basically, this model said that when considerable investments were made in a specific customer relationship, the design of their supply chain governance form would change considerably; instead of letting the exchange relationship be dominated by the price mechanism, the firm would put more emphasis on contractual agreements, as well as try to establish cooperative norms to govern the exchange relationship. Such contractual agreements and cooperative norms were called formal and relational contracts respectively.

Having established a robust base model of channel governance form, one could focus on how positioning differences (cf question 2), channel resources differences (cf question 3) between firms, and different levels of market attractiveness (cf. question 4) would relate to this model. Together, the answers to these matters would constitute an answer to the first research question. However, answering these questions is out of the confines of the synthesized model of TCE and RET, so that elements were extracted from some other paradigms - that of the strategic positioning and organizational capabilities respectively - and brought into the base model. In regards to the influence of positioning differences (question 2), it was hypothesized that product differentiation would impact the level of relational exchange norms, as well as the level of investments made in a customer interface. The latter relation would also be positively moderated by the perceived attractiveness of the market in which the customer was operating (question 4). In regards to channel resource differences (question 3), focus was set on the firm's experiential base related to the initiating, developing, and maintaining close customer relationships. This experience, termed relational capability, was hypothesized to positively impact the degree to which both relational and formal

contracts were established. Together, the answers to these questions (question 2, 3, and 4) have the potential to explain why firms in the same industry demonstrate starkly different approaches to bringing their products to market (question 1), obviously a question of great importance, but also a question for which scant empirical material of quantitative character exists.

9.1.1 Support of hypotheses, control variables, and rival predictors

Five out of seven hypotheses were supported. Further, the posited mediating role of asset specificity in transmitting the effect of product differentiation on formal contracts was confirmed; product differentiation was found to strongly affect the degree of formal contracts, but when this effect was controlled for asset specificity, the effect's size and level of significance fell from a $p < 0.001$ level of significance to well below the 0.05 cut-off level.

The control tests indicated no spurious or masked effects from all supported hypotheses. Customer asset specificity had no impact on formal contracts and a positive impact on (supplier) asset specificity. Opportunistic behavior from the counterpart had, as expected, a negative influence on relational contracts. The rationale behind this is straightforward; opportunistic behavior from the counterpart destroys the relational climate and undermines the building of relational norms.

Environmental uncertainty was negatively related to formal contracts. This contradicts the logic of TCE, which maintains that, given that the parties made investments in the relationship, larger degrees of uncertainty make it more imperative that the parties develop a stronger contractual arrangement to work things out. The results here indicate the opposite; in the face of higher uncertainty, the parties refrain from increasing contractual specificity, maybe because external changes may quickly render them irrelevant.

A number of potential rival predictors were included to increase the confidence in the hypothesized model. The rationales behind the possible effect of these predictors were somewhat exploratory in nature, so that hypotheses were not deduced. However, based on a broad review of the literature, there were some indications that the variables might have an effect.

Customer dependence was positively related to both relational norms and asset specificity. Ethnocentricity did not have any effect on neither of the dependent variables. State

influences was negatively related to both formal and relational contracts; higher degrees of official bureaucracy and governmental interference in the host country impede the establishment of relational norms and formal contracts. The *Beta* and *T* values of the originally hypothesized effects showed only trivial changes and were declared stable.

To sum up, the tests conducted give broad support to the model. Five out of seven hypotheses were supported, of which none was subjected with masked effects. Further, some rival predictors had explanatory power, but did not affect any of the modeled effects, as the *Beta* and *T* values showed only trivial changes.

9.2 Theoretical and managerial implications

First, the theoretical implications of the study will be discussed. Second, the managerial implications will be discussed.

9.2.1 Theoretical implications

Transaction cost economics has been repeatedly up for scrutiny and heavily criticized for neglecting the relevance of a number of issues such as trust, social embeddedness, firm heterogeneity, narrow focus etc. A common response has been to complement the theoretical framework with other theories to make the constructed model better fit the real world. This paper follows this same approach. This approach was chosen in order to answer some very basic, yet largely unexplored, questions originally identified by Ghosh and John (1999).

An integratory approach to the study of inter-firm governance is certainly not new. Elements from one or more of the perspective of the resource-dependence, political economy, relational exchange, and the export literature have all been frequently combined into a model where TCE is normally one of the most important elements. Constructs from the organizational capabilities and strategic positioning paradigms have however been far less frequent when studying inter-firm governance. When studying related subjects such as vertical integration and foreign market entry, on the other hand, such constructs have often been parts of the toolbox. For example, in a number of studies on the vertical integration of the firm, one has found that capability-based along with TCE-based variables are significant drivers behind firm scope (see, e.g. Argyres 1996; Poppo and Zenger 1998; Steensma and Corley 2001; White 2001; Schilling and Steensma 2002; Leiblein et al. 2003; Leiblein and

Miller 2003). Similarly, there have been a large number of studies focusing on how capability- and/or positioning-based variables relate to the mode of entry into foreign markets (see, e.g., Gatignon and Anderson 1988; Agarwal and Ramaswamy 1992; Kim and Hwang 1992; Erramilli and Rao 1993; Contractor and Kundu 1998). These studies have produced similar results; by supplementing TCE with elements from one or both of the resource-based and IO frameworks, the explanatory power of the model increases.

Accordingly, one has found that both capability-based and positioning-based variables have impact on what operating mode is used. Unfortunately, however, as the variation of the governance mechanisms across governance forms is not well established in the literature (Heide 1994), one cannot extrapolate these findings onto the domain of (inter-firm) governance mechanisms and make conclusions about how the capability-based and positioning-based variables affect governance mechanisms in inter-organizational exchanges. Therefore, it is strange that one has not yet systematically extended this ‘integratory’ work to the domain of formal and relational contracting in B2B relationships. This lack of empirical research is illustrated by the way Ghosh and John (1999) presented their arguments; after having theoretically demonstrated that firms in the same industry differed in their market approach due to differences in their inherent resources/capabilities and market positioning strategies, they illustrated their “conceptual arguments largely through anecdotal examples because of the lack of systematic empirical work on these issues” (p. 142).

This study follows the spirit of Ghosh and John’s (1999) governance value analysis (GVA) framework in three ways. First, emphasis was put on the development of a base model of channel governance. When having made asset specific investments, the firm would increase the degree of both formal and relational contracts. Findings partially support this base model. Having established such a base model facilitated the development of arguments in regards to how constructs from other perspectives were related to relationship governance.

Second, building on Day and Klein (1987) and Ghosh and John (1999), it was shown theoretically how different positioning choices impact the degree to which a more advanced governance apparatus was developed. As TCE represents the theoretical backbone of the study, emphasis was placed on how product differentiation affects asset specificity, which in turn impacts the degree of formal contracting. In this case, asset specificity is posited as a mediator, transmitting the effect of product differentiation on formal contracts. This cross-paradigmatic link represents one theoretical contribution which has been hitherto left unexplored by the larger number of studies. Capitalizing on the aforementioned works, a

number of conceptual arguments were developed in regards to how asset specificity followed from a product differentiation strategy. These arguments were largely of strategic and competitive character, as the characteristics of the transaction “reflect strategic choices made partially outside the confines of the [TCE] model” (Day and Klein 1987: 55). Hence, the underlying rationale for making such investments was dominated by a different type of logic. TCE’s narrow efficiency rationale was not appealing as an explanation mechanism for this purpose. Instead, some strategic considerations were adopted. For example, investments in the customer interface needed to be made in order to support crucial features of the supposedly higher value differentiated product, thus building up under its product strategy. Also, such investments had the potential to keep potential entrants out of the market, as they observed that larger investments needed to be made if they wanted to capture customers in this market. Obviously, such investments are also crucial if the products are to be distributed further down the value chain, attempting to make the distributor commit to the product strategy. This hypothesis received strong support by the data.

It was also hypothesized that firms would be more inclined to make such relationship specific investments if the market in which the customer was operating, was perceived to be attractive. Such reasoning represents the backbone of standard investment models; if the prospect is considered attractive, the probability of making the investment increases because the potential future payoffs are likely to be higher, thus justifying to a larger degree the risks of such investments. The hypothesis did not receive support by the data. However, the logic behind this idea intriguingly simple, and represents a possible link between the characteristics of the industry, the firm’s positioning considerations, and its investments made in a customer interface. As such, I assert that, instead of trying to speculate on any potential direct effects of such industry characteristics on the design of governance form, as has been done by some studies (e.g., Genturck and Aulakh 1995; Joshi and Stump 1999a; Morgan et al. 2004), it might be more productive to take one step back and consider such industry characteristics in regards to investments made in this market, i.e., in the customer interface. The point is that the underlying logic of the way by which industry characteristics is related to some relationship governance model should be dominated by strategic rather than efficiency considerations. As the degree of asset specificity reflect strategic choices rather than efficiency considerations and must be explained outside the confines of the TCE model (Day and Klein 1987), this approach of incorporating industry characteristics to relationship governance appears more promising than relating industry characteristics directly to the governance of the relationship.

It should be noted in passing that these considerations clearly have a value-maximizing spirit, thus meeting the (mistaken) critiques of TCE's apparently obsessive cost minimizing focus (e.g., Zajac and Olsen 1993). As pointed out by Ghosh and John (1999), this confusion stems from the way by which the TCE model usually is tested; as only the reduced-form of the model is tested, focus is guided away from the value creation aspect of the theory. In this dissertation, on the other hand, it is emphasized that investments will only be made if the resulting increase in the (net present) joint value exceeds the investments costs made. Not making such investments means inefficiency, because opportunities to realize value are not pursued. I claim that the treating asset specificity as a decision variable has the potential to eliminate this confusion in the literature. Parenthetically, as efficiency considerations are not appealing, or not as obvious, when trying to explain the level of investments made in the relationship, one may apply strategic considerations for this purpose.

The third way in which this study follows the spirit of Ghosh and John (1999) is the recognition that the firm's supply chain resources have impact on the extent to which firms rely on formal and relational governance. A broad experiential base seemed to be an important element in the raising of relational contracts. The rationale is that such experience (i) helps the firm choose partners who will abide by relational norms, (ii) better understand themselves the value following relational norms (Weitz and Jap 1995), and (iii) helps the firm get a better understanding of the counterpart, facilitating the reciprocative process by which relational norms are developed. Earlier research has found largely corroborative results that such resources have a positive impact on relational sentiments. This study corroborates earlier research on this matter.

Less literature exist in regards to how such experience is related to the degree to which formal contracts are relied on. A starting point of argumentation was taken in TCE's asymmetrical appliance of the bounded rationality theorem. Williamson (1975; 1985) assumed away the existence of perception and interpretation difficulties. Hodgson (2004), in contrast, pointed out that such matters are of great importance, and that the scope and effect of them must be minimized by providing a more complete set of instructions. In brief, such reasoning makes matters of perception and interpretation, alongside with opportunism, reasons for differences in governance structures.

How does such reasoning relate to formal contracting? To answer this question, one must first recognize that the writing of contracts must be considered a costly activity. Increasing the specificity of contracts is then assumed to be undertaken only if there is an incentive to do so. In this dissertation I argue that such incentives may come from at least two

sources. First, given nontrivial degrees of asset specificity, the firm is more motivated to increase contractual specificity because of the risk of being exposed to opportunism (Williamson 1975). This is standard TCE reasoning. Second, inspired by Hodgson (2004), provision of a more complete set of instructions is desirable per se, because it reduces the possibility for confusion, misinterpretations, and misunderstandings. A broad experiential base would (i) facilitate the writing of more clear-cut instructions, (ii) make the company more aware of the benefits of doing so, and (iii) make it less costly for them to do so. This hypothesis received support by the data.

By adopting a construct that represents a firm's relevant accumulated contracting experience, one is at least partially able to address matters related to misunderstanding and misinterpretation resulting from differences in perception, interpretation, and cognitive framing of information. Excluding this aspect implies making some implausible assumptions in the construction of a relationship governance model. Whereas bounded rationality is claimed to be assumed in regards to relationship governance, this assumption is actually only related to the parties self-interest behavior; matters of interpretation, understanding, and cognitive framing of information are assumed to be non-existing or negligible. Hodgson (2004) convincingly demonstrated that this assumption is implausible, at best. This dissertation has shown how to incorporate such matters in a relationship governance context.

As shown throughout this sub-chapter, having taken perspective in each of the paradigms of strategic positioning and organizational capabilities, a number of arguments have been developed in regards to how such considerations relate to relationship governance, the base model of which is a synthesis of TCE and RET. Hence, this dissertation is cross-disciplinary in the uttermost sense. Nevertheless, I claim that clarity and precision of the original relationship governance baseline model are at least partially retained, because great emphasis has been paid to how the elements from the different models are related to each other, and respecifications of the original assumptions have been clarified. Also, I claim that this potential loss in clarity and precision is justified to the extent that (i) the originally stated questions were answered, and (ii) that the explanatory power of the model has increased.

9.2.2 Managerial implications

The trend towards forming closer customer relationships has been repeatedly highlighted in both academic and practical journals. Emphasis has been put on the criticality of forming such

relationships for surviving in the ever-more competitive market place (Houston and Johnson 2000). Such relationships are even considered a source of competitive advantage (Dyer and Singh 1998; Day 2000).

Given the potential benefits in forming closer customer relationships, there is less knowledge about under what conditions firms are likely to form such relationships. General rationales, such as improving the efficiency and effectiveness of sales and procurement efforts and more intense competition have been attributed to this trend. But such rationales are far too general and then also unsatisfactory. This study provides four important insights for managers in this regard.

First, the literature on distribution channel relationships has over and over again reminded us about the importance of safeguarding one's investments in customer interfaces. The implications of such investments for organizing their relationships seem to be well established; such safeguarding can be achieved either by increasing the degree of formal contracting, and/or nurturing relational sentiments in the relationships. This study partially corroborates this finding.

Second, it has been shown what governance implications are likely to follow from a firm's strategic positioning within an industry. A successful implementation of a product differentiation strategy is often dependent on support from investments in the customer interface. Also, such investments have deterring effect on potential entrants to the same market niche. Finally, in cases where the product is to be distributed further downstream, such investments can build the customer's commitment to the strategy. In turn, such investments imply that the level of contractual specificity must be raised. Also, as a successful differentiation strategy depends on deep information about customer preferences, and frequent updates on the changes in such preferences, this necessitates a nurturing of the information channels to that market.

Third, firm's accumulated experiential knowledge with close customer relationships is crucial for the raising and implementation of more formal and relational contracts. Recent studies have found that more detailed contracts and relational governance complement each other, and the combined use of these mechanisms enhances performance (Cannon et al. 2000; Poppo and Zenger 2002). A broad experiential base makes the firm better able to develop a cooperative climate with its exchange partner through the raising of such governance mechanisms.

9.3 Limitations and future research

If knowledge about how resource/capability- and positioning-based variables relate to inter-firm governance mechanisms can be built, one can substitute the popularized Strength, Weakness, Opportunity, and Threat (SWOT) model with a more sophisticated model that may answer questions such as how the focal firm's strengths, weaknesses, opportunities, and threats disable, enable, discourage, or encourage different ways of organizing and governing customer relationships (Ghosh and John 1999). This model may also be more practical, as formal and relational governance mechanisms are the actual management tools with which sales managers meet their markets. Further, by integrating these frameworks one may be able to bridge the knowledge having been built from the huge number of 'traditional' SWOT studies with the accumulated knowledge from the studies having focused on firm's reliance of different governance mechanisms. Establishing such a knowledge base may also facilitate an extrapolation of the findings of the cross-disciplinary studies on vertical integration and foreign market entry strategies onto the area of inter-firm relationship governance.

Overall, such an approach bears the promise of developing a set of guidelines for sales managers that take into account a broader set of concerns. These guidelines may not only consider obvious inter-organizationally related concerns, such as the degree of adaptation to the partner, the difficulty with which contractual compliance can be ensured, the perceived level of conflict between the parties, difficulties of building relational norms due to cultural and geographical distance etc. Instead, they may also consider the implications of a firm's positioning considerations, industry characteristics, and channel resource differences on the formation of close customer relationships. This study has provided one step in this direction. Future studies along this avenue are encouraged.

The results of the study must be interpreted in light of its limitations. There are a number of such limitations. First, due to theory testing purposes, the context of the study was quite homogenous (two industries with several similarities). This made it easier to control for extraneous sources and develop grounded measures. However, caution must be shown when generalizing the results of this study to other contexts.

Second, in the pursuit of presenting a parsimonious model that took into account elements from a broader set of perspectives, only one construct was chosen in regards to each of these questions; product differentiation was chosen to reflect positioning considerations, perceived market attractiveness was chosen to reflect industry characteristics, and relational capability was chosen to reflect channel resources. The results of the study largely support

this idea of incorporating fundamentally different concerns in the same model to explain the formation of close customer relationships. However, choosing only one element to reflect positioning considerations, industry characteristics, and channel resource differences respectively is a rather blunt approach. Ideally, several constructs should have represented each of the different concerns. For example, in regards to positioning considerations one could also include cost leadership strategy and niche strategy (Porter 1980), a strategy to create especially desirable advantages such as monopoly rents (see Aulakh and Kotabe 1997), or the impact of competitor's strategy. Likewise, in regards to channel resource differences, one could also include constructs as customer brand equity and access to technology (as suggested by Ghosh and John 1999), as well as 'a number of different capabilities' (see, e.g., Jap 2001). Finally, in regards to industry characteristics, one could also include constructs such as customer bargaining power, threats from competitors, technology intensiveness, market volatility, and the degree of price competition.

Third, in regards to matters of cognition and interpretation, it was admitted in the theory section that the 'relational capability' construct did not fully capture such matters. Rather, it was argued that broad experience with customer relationship management would make the firm more aware of matters related to cognition and interpretation, more able to specify a more complete and clear-cut set of instructions, and less costs would be entailed in doing so. Hence, the 'distance' between the theoretical argumentation and operationalization of the construct is considerable, and it could be questioned whether the observed correlation is in fact attributable to other explanations than what was emphasized herein. For example, a possible explanation might be that experience has accumulated within the organization about how to organize transactions, and that such experience is manifested in organizational routines. In turn, a broader experience with similar transactions may make it more likely that a firm has established routines in writing more detailed contracts. These routines display substantial rigidity (Hannan and Freeman 1984), and cannot be readily altered. Hence, if the firm has relied on formal contracting in the past, it is more likely to do so again in the future. This line of arguing provides an explanation of the correlation between relational capability and formal contracting which does not rely on any profitability or incentive-based calculus (as does the explanation provided in chapter 6.2.2). A better approach to accommodate matters of misinterpretation and cognition may be to measure directly the degree to which there is potential for misunderstandings and the degree to which confusion in regards to roles, procedures, and responsibilities may arise. If such measures can be obtained, one will have a more direct test of the relevance of such matters for relationship governance.

Fourth, this study sought to examine what makes firms form closer customer relationships, i.e. antecedents to governance mechanisms in their distribution channels. In doing so, it was only concentrated on formal and relational contracting. The choice of formal contracting was grounded in earlier research of what seemed to be the most viable approach when studying indicators of hierarchical governance in inter-firm relationships. Hence, there are a number of other governance mechanisms among which to choose, which might serve the same purposes in a different manner. Dimensions such as participation and centralization have also been studied in an interfirm setting, albeit less frequent. Moreover, “centralization ... does not appear to apply very well in an interfirm setting (Frazier 1999: 233). Given that this construct reflect decision making authority, which is an important dimension of the hierarchy (cf. Weber 1947), including this dimension may be important. Considering the difficulties involved with making the construct ‘work’ in an interfirm setting, more research is needed in this regard. Related to this matter, when studying governance mechanisms one might also include market governance, i.e. the degree to which the price mechanism governs the relationship. The market governance would then constitute the logical opposite of (any of the dimensions of) hierarchical governance, cf. Williamson’s continuum. This construct is almost never included in empirical studies, but promising results were provided by Haugland et al. (2004).

Fifth, this study has placed an exclusive emphasis on economic explanations for governance mechanisms in distribution channels. Certainly, there exist other explanations for governance mechanisms. For example, as shown above, one can give sociological explanations for the effect of a broad experiential base on formal contracting. Also, the sociologically based power and resource dependence theory have been frequently included as explanations for formal and relational contracting (see, e.g., Bello and Gilliland 1997; Bello et al. 2003; Buvik and Reve 2002; Joshi and Stump 1999c; Jap and Ganesan 2000; Lusch and Brown 1996). The disregard of these explanations may be questioned; “ultimately, the question of which paradigm or alternative explanation is capable of explaining the most variance in governance structures [and mechanisms] is an empirical one” (Chiles and McMackin 1996: 95). Hence, future studies may examine sociological explanations for governance mechanisms and then compare the explanatory power of these explanations with the explanatory power of those provided herein.

Sixth, the desirability of forming close customer relationships under some conditions is not actually tested, but inferred based on theory and earlier findings. A better approach is to explicitly test this assumption by including some aspect(s) of performance in

the research model, and test under which conditions the formation of closer customer relationships improve performance.

The chosen research design has five obvious limitations. First, the static nature of the cross-sectional design disables the studying of the dynamic processes underlying the nature of elements in the model. Researchers have repeatedly raised awareness of the evolutionary nature of interfirm relationships. Obviously, transaction costs, formal contracts, and relational norms vary with the frequency, type, and history of exchanges between the parties (Williamson 1975). Second, the cross-sectional design makes one incapable of statistically investigating the directionality of the influence, which is actually one of the fundamental underpinnings of the whole model (the relations of the model are of a causal nature). Despite the cause-and-effect language in the hypotheses, the directionality of these influences could not be established statistically. For these two purposes, a longitudinal research design is needed.

The third limitation is that data was only collected on one side of the dyad. This does not allow an assessment of the impact of the counterpart's characteristics on the interfirm relation. Such an assessment would be especially relevant when measuring the impact of relevant experience with channel relationships. For example, what would happen if the customer had a broad experiential base, whereas the manufacturer had very little experience with similar exchanges? Would the customer's experiential base compensate for the manufacturer's experience? Such questions must be answered by dyadic data (Lambe et al. 2002).

Fourth, only one informant reported on each dyad. Even though using only one informant per dyad is generally accepted, the accuracy of the data might be questioned. Using several informants for each dyad would facilitate an inter-informant comparison of the data provided, and the accuracy might have been improved. Of course, doing so would impose a severe logistical challenge on behalf of the researcher, which needs to be balanced against the resources available and the value added by doing so.

Finally, it was only relied on the managers' retrospective perceptions to operationalize the variables. Even though this is the common approach, and has been demonstrated reliable and valid (e.g., Schwenk 1985), the findings can be strengthened if complemented with more objective data.

9.4 Concluding remarks

This dissertation has investigated what makes firms form closer customer relationships. In particular, it has been shown how the study of formal and relational contracts in an interfirm setting benefit from bringing in elements from structural and resource-based analysis, and how a synthesis of these theories provides a more holistic understanding. The proposed hypotheses received support to a great extent. However, these findings must be interpreted in light of its limitations. In turn, these limitations provide promising avenues for future research.

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11 APPENDICES

11.1 Appendix A: Questionnaire (Norwegian version)

RELASJONER I INTERNASJONALE DISTRIBUSJONSKANALER

Dette spørreskjemaet består av fire deler. I del I går vi nærmere inn på relasjonen til en av deres viktigste eksportkunder, mens del II setter fokus på et produkt som selges til denne kunden, samt ulike forhold vedrørende markedet der produktet selges. Del III tar for seg bedriftens tidligere erfaring med eksportvirksomhet og kunnskaper relatert til eksportmarkedet, mens del IV spør om noen få fakta om bedriften. Som svar på spørsmål der vi ber om tallstørrelser, er det nok å oppgi **omtrentlige verdier**. Dersom dere ikke umiddelbart vet dette, kan dere hoppe over punktet. Dere skal derfor **ikke lete frem opplysninger** for å besvare skjemaet. De fleste spørsmål er formulert som påstander på en svarskala fra 1 til 7. Du svarer ved å sette en ring rundt ett av tallene. Tallet du velger skal gjenspeile i hvilken grad påstanden er beskrivende for deres bedrift.

Eksempel:

I svært
liten grad

I svært
stor grad

Vi er internasjonalt konkurransedyktige 1 2 3 4 5 **6** 7

Alle opplysninger som blir gitt i dette skjemaet vil bli behandlet **strengt konfidensielt**. I rapporter og andre publikasjoner som utgis i forbindelse med prosjektet, vil dataene som samles inn kun benyttes i aggregert form, slik at det er umulig å tilbakeføre opplysninger til den enkelte bedrift.

Ett av formålene med undersøkelsen er å gi statistisk begrunnede anbefalinger til næringen. For at man skal kunne trekke slike konklusjoner, er det viktig at bildet blir mest mulig komplett. Vi vil derfor presisere at det er viktig at dere tar dere tid til å besvare skjemaet. **Som takk for hjelpen vil dere få tilsendt en konfidensiell, spesiallaget rapport om dere ønsker det.** I denne vil det være beskrevet både resultatene av studiet som helhet, samt en spesifikk fremstilling av dataene til deres bedrift sammenlignet med resten av bedriftene.

Spørreskjemaet bes returnert i den **frankerte svarkonvolutt** innen to uker.

Bedriftens navn: _____

Kontaktperson: _____

DEL I - RELASJONEN TIL EN AV BEDRIFTENS VIKTIGSTE EKSPORTKUNDER

Vennligst velg nå ut **en kunde** i den internasjonale distribusjonsskjeden som bedriften samarbeider med. Bedriften du velger bør være **en av deres viktigste aktører på eksportmarkedet**, og helst en av deres større internasjonale kunder. Videre bør det være en kunde du **har god kjennskap til**, og som bedriften har solgt til over tid - helst tre år eller mer.

Kundens nasjonalitet: _____

Hvor mange år har bedriften solgt til denne kunden? _____ år

Hvor stor andel av total omsetning representerer kunden? _____%

Hva slags type bedrift er kunden? Kryss av for hva som er mest riktig

- Utenlandsk distributør
- Agent
- Industribedrift
- Annet (spesifiser) _____

1.1 Hvor sikre var dere på at dette var den beste løsningen?

	I svært liten grad						I svært stor grad	
Vi kunne like gjerne ha valgt en annen distribusjonskanal i dette markedet	1	2	3	4	5	6	7	
Da vi valgte distribusjonskanal i dette markedet, var det usikkerhet forbundet med hvilken løsning som ville være best for oss	1	2	3	4	5	6	7	

1.2 Benytter dere i tillegg andre distribusjonskanaler til å nå markedet der denne kunden opererer? (f.eks. selger dere både via en agent og direkte til en industribedrift i dette markedet)

JA / NEI (sett ring rundt det som passer)

Nå rettes oppmerksomheten mot ulike forhold vedrørende relasjonen mellom deres bedrift og denne kunden. Alle spørsmålene i denne delen besvares kun i forhold til akkurat dette kundeforholdet.

1.3 Først settes fokus på hvordan dette kundeforholdet styres eller administreres.

	I svært liten grad						I svært stor grad	
Det eksisterer en skriftlig avtale som spesifiserer hva slags oppgaver og ansvar partene har	1	2	3	4	5	6	7	
Hvordan den daglige styringen av kundeforholdet skal foregå, er uttrykt i en skriftlig avtale	1	2	3	4	5	6	7	
Det er utviklet regler (avtaler) og retningslinjer for de fleste ting i dette kundeforholdet	1	2	3	4	5	6	7	

Det forventes at begge parter følger de regler og retningslinjer som beskrevet i avtalen	1	2	3	4	5	6	7
Vi legger vekt på å opptre formelt riktig i henhold til avtalen	1	2	3	4	5	6	7
En skriftlig avtale spesifiserer hvordan uenigheter og konflikter skal løses	1	2	3	4	5	6	7
Vi har stor innflytelse over kundens salgs- og markedsføringsaktiviteter for vårt produkt	1	2	3	4	5	6	7
Vi tar alle avgjørelser relatert til transport og levering	1	2	3	4	5	6	7
Vi krever at produktet skal ha et bestemt symbol eller logo ved videre salg/distribusjon	1	2	3	4	5	6	7
Vi har stor innflytelse over kundens lagerhold av vårt produkt	1	2	3	4	5	6	7
For å få oss til å arbeide mer effektivt henviser kunden til hva andre leverandører tilbyr	1	2	3	4	5	6	7
Utvikling i pris og markedsforhold er avgjørende for om vi får fremtidige leveranser til kunden	1	2	3	4	5	6	7
Kunden overvåker markedet for å være sikker på at våre priser ikke er vesentlig høyere enn hos andre leverandører	1	2	3	4	5	6	7

1.4 De utsagn som følger dreier seg om hvordan deres bedrift og den valgte kunden **forholder seg til hverandre.**

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Partene betrakter løsning av problemer som oppstår partene imellom som felles ansvar							
Begge parter ser det som viktig at det gjøres forbedringer som gagnar forholdet som helhet	1	2	3	4	5	6	7
Både vi og kunden tar ansvar for at dette forholdet fungerer for begge to	1	2	3	4	5	6	7
Fleksibilitet når motparten ønsker endringer om ulike ting, er typisk for dette forholdet	1	2	3	4	5	6	7
Vi forventer å gjøre tilpasninger i dette kundeforholdet for å håndtere endrede betingelser	1	2	3	4	5	6	7
Når en uventet situasjon oppstår, utarbeider vi heller en ny avtale enn å tvinge hverandre til å overholde betingelsene i den gamle avtalen	1	2	3	4	5	6	7
I dette forholdet forventes det at informasjon som kan gagne motparten, vil bli formidlet	1	2	3	4	5	6	7
Det forventes at man holder hverandre informert om hendelser eller endringer som kan være viktig for motparten	1	2	3	4	5	6	7

Det forventes at man vil gi motparten informasjon, hvis den kan være av betydning	1	2	3	4	5	6	7
I dette forholdet utveksles ofte informasjon	1	2	3	4	5	6	7
Vi forventer at dette forholdet vil vare lenge	1	2	3	4	5	6	7
Vi antar at avtalen med kunden vil fornyes	1	2	3	4	5	6	7
Vi gjør planer for fortsettelsen av kundeforholdet, og ikke bare for enkeltstående ordre	1	2	3	4	5	6	7

1.5 Denne delen rettes oppmerksomheten mot **samarbeidstiltak** mellom deres bedrift og den kunden du har valgt. Merk at spørsmålene kun fokuserer på **akkurat dette kundeforholdet**.

	I svært liten grad							I svært stor grad	
	1	2	3	4	5	6	7		
For å kunne levere til denne kunden har det vært nødvendig å gjøre spesielle investeringer eller tilpasninger i utstyr og/eller anlegg	1	2	3	4	5	6	7		
Det har vært nødvendig å gi ansatte som arbeider med denne kunden spesiell opplæring	1	2	3	4	5	6	7		
Det har vært nødvendig å tilpasse vårt produksjonsutstyr til kunden	1	2	3	4	5	6	7		
For å kunne levere til denne kunden har vi gjennomført spesielle investeringer eller tilpasninger i distribusjonssystem	1	2	3	4	5	6	7		
Denne kunden har gjort investeringer eller tilpasninger i utstyr/anlegg mot vår bedrift	1	2	3	4	5	6	7		
Denne kunden har gitt ansatte som jobber mot vår bedrift, spesiell opplæring	1	2	3	4	5	6	7		
Denne kunden har gjort tilpasninger i interne prosesser av hensyn til forholdet til vår bedrift	1	2	3	4	5	6	7		
Denne kunden har tilpasset sine distribusjonssystemer mot vår bedrift	1	2	3	4	5	6	7		
Vi har opparbeidet en grundig forståelse for denne kundens virksomhet	1	2	3	4	5	6	7		
Dette kundeforholdet betrakter vi som en investering som vil gi fremtidige gevinster	1	2	3	4	5	6	7		
Vi har brukt mye tid og ressurser på å bygge opp dette kundeforholdet	1	2	3	4	5	6	7		
I dette kundeforholdet har det vært nødvendig å tilpasse vår egen organisasjon til kunden	1	2	3	4	5	6	7		
For å levere til denne kunden har vi skaffet oss kompetanse som har begrenset verdi for oss dersom kunden slutter å kjøpe fra oss	1	2	3	4	5	6	7		
Hvis denne kunden slutter å kjøpe fra oss, vil tidligere investeringer være av begrenset verdi	1	2	3	4	5	6	7		

1.6 Hvordan opplever dere ulike **problemer** som kan oppstå i denne kunderelasjonen?

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Til tider feilinformerer denne kunden oss om ting for å beskytte eller fremme egne interesser							
Denne kunden lover noen ganger å gjøre ting uten faktisk å følge dette opp senere	1	2	3	4	5	6	7
Denne kunden handler ikke alltid i tråd med kontrakten eller avtalene oss imellom	1	2	3	4	5	6	7
Denne kunden prøver noen ganger å bryte uformelle avtaler for å fremme egne interesser	1	2	3	4	5	6	7
Denne kunden vil prøve å dra fordel av "hull" i kontrakten for å fremme egne interesser	1	2	3	4	5	6	7
Denne kunden utnytter noen ganger uventede hendelser for å oppnå bedre betingelser fra oss	1	2	3	4	5	6	7

1.7 Hvor **avhengige** er deres bedrift av denne kunden?

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Hvis salget til denne kunden skulle opphøre, ville det være vanskelig å finne en god erstatning for denne kunden							
Hvis salget til denne kunden skulle opphøre, ville vi fått økonomiske problemer	1	2	3	4	5	6	7
Vi er avhengige av denne kunden	1	2	3	4	5	6	7
Det finnes andre tilsvarende bedrifter som kan erstatte denne kunden	1	2	3	4	5	6	7

1.8 Til slutt i del I fokuseres det på ulike forhold relatert til denne kundens **videre salg/distribusjon** av produktene deres. Dersom dette ikke er relevant for deres bedrift, hopp over dette punktet.

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Det er forbundet med betydelige kostnader å finne ut hvem denne kunden videreselger produktene våre til	1	2	3	4	5	6	7
Vi må bare anta at denne kunden yter god kundeservice, fordi det er ingen annen måte vi kan finne det ut på	1	2	3	4	5	6	7
Det er forbundet med betydelige kostnader å forsikre oss om at aktivitetene til denne kunden er i overensstemmelse med avtalen oss imellom	1	2	3	4	5	6	7
Hvis kunden ikke lenger handler i tråd med intensjonen med avtalen, får vi raskt greie på det	1	2	3	4	5	6	7
Å evaluere denne kunden kun på bakgrunn av salgshallene gir ikke et riktig bilde av om kunden handler i tråd med våre interesser	1	2	3	4	5	6	7
Vår evaluering av denne kundens aktiviteter er basert på tvetydig informasjon	1	2	3	4	5	6	7

DEL II - ET AV DE VIKTIGSTE PRODUKTENE FOR DEN VALGTE UTENLANDSKE KUNDEN

Ved besvarelse av de påfølgende spørsmålene ber vi deg ta utgangspunkt i det dere anser som **det viktigste produktet dere selger til den valgte kunden** (jf Del I) (målt etter f.eks. fjorårets omsetning). Produktet kan være en komponent, et enkeltstående produkt, en eller flere tjenester, en pakke av produkter og tjenester eller en totalløsning. Det er viktig at du velger ett produkt hvor du har god kjennskap både til produktet og det respektive eksportmarkedet der kunden opererer. Merk at spørsmålene **kun besvares i forhold til akkurat dette produktet**.

Velg produkt: _____
(produktbetegnelse)

2.1 Først ber vi deg besvare enkelte forhold ved det valgte produktet.

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Når kunden kjøper dette produktet, er pris den eneste faktoren av reell betydning	1	2	3	4	5	6	7
Vårt produkt er forskjellig fra produkter som tilbys av konkurrentene i dette markedet	1	2	3	4	5	6	7
Strategien vår kan best beskrives som det å skape en "høystandardprofil" for produktet	1	2	3	4	5	6	7
Produktet vi selger til denne kunden, er tilpasset denne kundens behov	1	2	3	4	5	6	7
Når kunden kjøper dette produktet, er det flere faktorer enn kun pris som er av reell betydning	1	2	3	4	5	6	7
Uautorisert import av produktet til dette markedet er et problem	1	2	3	4	5	6	7

2.2 Hvor attraktivt og konkurranseintensivt er dette eksportmarkedet for akkurat dette produktet?

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Det er stor sannsynlighet for store fremtidige overskudd i dette markedet	1	2	3	4	5	6	7
Dette markedet har stort etterspørselspotensial	1	2	3	4	5	6	7
Dette markedet vil ha en sterk vekst fremover	1	2	3	4	5	6	7
Gjennomsnittlige marginer i markedet er høye	1	2	3	4	5	6	7
Konkurransen i dette eksportmarkedet er hard	1	2	3	4	5	6	7
Alt vi tilbyr, kan våre konkurrenter også tilby	1	2	3	4	5	6	7
Priskonkurranse er typisk for dette markedet	1	2	3	4	5	6	7
En hører ofte om nye konkurransemanøver i dette markedet	1	2	3	4	5	6	7

2.3 Her rettes oppmerksomheten mot **kulturelle aspekter** samt **offentlige lover og reguleringer** i det geografiske markedet der den valgte kunden opererer.

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Utlendinger behandles ofte annerledes enn de lokale i dette markedet	1	2	3	4	5	6	7
I dette markedet er den nasjonale kulturen lite åpen for andre kulturer	1	2	3	4	5	6	7
Offentlig byråkrati gjør det mer vanskelig å eksportere til dette landet	1	2	3	4	5	6	7
'Proteksjonistiske' regler gjør det mer vanskelig for oss å eksportere til dette landet	1	2	3	4	5	6	7
Statlig innblanding gjør det mer vanskelig for oss å eksportere til dette landet	1	2	3	4	5	6	7

2.4 Så fokuseres det på de **resultater** bedriften har oppnådd i dette markedet.

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Vi har nådd våre strategiske mål i forbindelse med eksport til dette markedet	1	2	3	4	5	6	7
Eksporten til markedet har vært suksessfull	1	2	3	4	5	6	7
Vi har nådd våre salgsmål for dette markedet	1	2	3	4	5	6	7
Vi har nådd våre vekstmål for dette markedet	1	2	3	4	5	6	7

2.5 Her fokuseres det på **usikkerhet** i markedet for det valgte produktet.

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Våre viktigste konkurrenter i dette markedet gjør ofte endringer i forhold til dette produktet og/eller utvikler nye relaterte produkter	1	2	3	4	5	6	7
Salget av produktet i dette markedet er vanskelig å forutsi	1	2	3	4	5	6	7
Etterspørselen etter produktet i dette markedet er vanskelig å forutsi	1	2	3	4	5	6	7
Konkurransen i markedet er vanskelig å forutsi	1	2	3	4	5	6	7

DEL III INTERNASJONAL FORRETNINGSVIRKSOMHET

3.1 Først belyses bedriftens erfaring med internasjonal forretningsvirksomhet.

	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
Vi har lang erfaring med å operere i dette eksportmarkedet							
Vi har lang erfaring med gjeldende forretningspraksis i dette markedet							
Vi har lang erfaring med relevante eksportprosedyrer for dette markedet							
Vi har bred erfaring med å etablere og vedlikeholde utenlandske kundeforhold							
Vi har bred erfaring med forhandlinger med utenlandske kunder							
Vår bedrift har bred internasjonal erfaring							
Hvor mange år har bedriften drevet med eksport? _____ år							

3.2 Hvordan er bedriftens kunnskaper om eksportmarkedet?

I dette markedet har vi bra kunnskaper om:	I svært liten grad					I svært stor grad	
	1	2	3	4	5	6	7
o aktuelle kunder							
o konkurrenter							
o aktuelle agenter og distributører							
Vi har god tilgang til relevant markedsinformasjon i dette markedet							
Vi har god forståelse for kundepreferansene i dette markedet							

DEL IV BEDRIFTEN OG DENS EKSPORTVIRKSOMHET

	2004	2003
Eksport i NOK (i mill. kroner)	_____	_____
Eksportandel (av total oms.)	_____	_____
Antall ansatte som hovedsakelig driver med eksport	_____ (2004)	
Total omsetning	NOK _____ (2004)	
Årsresultat før skatt	NOK _____ (2004)	
Antall ansatte	_____ (2004)	

11.2 Appendix B: Measures

This appendix presents the wordings of all observed variables in the structural analyses. Observed variables that were deleted due to high cross-loadings or correlated error terms are then not included in this appendix.

11.2.1 Measures of the variables in the theoretical model

Formal contracts (Scale Reliability = 0.86)

1. There is a written agreement that specifies the tasks and responsibilities of each party.
2. How to handle the day-to-day management of the relationship is expressed in a written agreement.
3. There are rules and procedures for most issues in this relationship.
4. It is important for us to behave formally accurate as according to the agreement.

Relational contracts (Scale Reliability = 0.63)

1. The parties are committed to improvements that may benefit the relationship as a whole and not only the individual parties.
2. Flexibility in response to requests for changes is a characteristic of this relationship.
3. In this relationship, it is expected that any information that might help the other party will be provided to them.
4. We assume that renewal of agreements with this supplier will generally occur.

Asset specificity (Scale Reliability = 0.89)

1. In order to deliver to this customer it has been necessary to make special investments or adaptations in equipment.
2. It has been necessary to give employees who are working with this customer special training
3. In order to deliver to this customer we have made specific investments or adaptations in our distribution systems.

Product differentiation (Scale Reliability = 0.78)

1. Our product is different from products offered by our competitors in this foreign market.
2. Our strategy can be best described as maintaining higher quality standards for our products.
3. When buying this product, there are more factors than price of real importance.

Relational capability (Scale Reliability = 0.96)

1. We have broad experience with establishing and maintaining foreign customer relationships.
2. We have broad experience with negotiating with foreign customers.
3. Our firm has broad international experience.

Market attractiveness (Scale Reliability = 0.83)

1. There are prospects for great future profits in this market.
2. This market has a great demand potential.
3. This market will have a strong growth in the future.

11.2.2 Measures of control and rival variables**Customer asset specificity (Scale Reliability = 0.87)**

1. This customer has given special training to employees that work towards our firm
2. This customer has done special adaptations in internal process in concern for the relationship to our firm
3. This customer has made adaptations in their distribution systems towards our firm

Environmental uncertainty (Scale Reliability = 0.88)

1. Market demand is hard to predict
2. The sales for this market is hard to predict
3. The competition in this market is hard to predict

Opportunism (Scale Reliability = 0.90)

1. On occasion, the customer lies about certain things in order to protect their interests.
2. The customer does not always act in accordance with our contract or agreement.
3. The customer sometimes tries to breach informal agreements between our companies to maximize their own benefit.
4. The customer will try to take advantage of “holes” in our contract to further their own interests.

Ethnocentricity (Scale Reliability = 0.67)

1. Foreigners are often treated differently than local citizens in this market
2. In this market the national culture is closed towards other culture

State influences (Scale Reliability = 0.88)

1. Official bureaucracy makes it more difficult to export to this country
2. National protectionism makes it more difficult for us to export to this country
3. Governmental interference make it more difficult for us to export to this country

Customer dependence (Scale Reliability = 0.70)

1. Should the sales to this customer cease, it would be difficult for us to find alternative purchasers
2. Should the sales to this customer cease, we would face economic problems
3. We are dependent on this customer
4. There are other similar firms that may replace this customer (R)

11.3 Appendix C: Syntax of methods for estimating moderator effect

11.3.1.1 Method 1: Latent Variable Scores (LVS)

As previously mentioned, the LVS method is new, and systematic evaluations of it await future research. Comparing the results of the two methods seems to support the viability of the method. As the method is relatively unknown outside the LISREL community, the syntax of the LISREL input file(s) is presented below.

Step 1: Latent Variable Scores - creating LVS for all variables

LISREL input file:

```
DA NI=20 NO=160
RA = 160_LVS.psf
MO NX=20 NK=6 LX=FU,FR
LK
Formal_contracts relational_contracts asset_specificity
prod_differentiation market_attractiveness relational_capability

PA LX
0 0 0 0 0 0
1 0 0 0 0 0
1 0 0 0 0 0
1 0 0 0 0 0
0 0 0 0 0 0
0 1 0 0 0 0
0 1 0 0 0 0
0 1 0 0 0 0
0 0 0 0 0 0
0 0 1 0 0 0
0 0 1 0 0 0
0 0 0 0 0 0
0 0 0 1 0 0
0 0 0 1 0 0
0 0 0 0 0 0
0 0 0 0 1 0
0 0 0 0 1 0
0 0 0 0 0 0
0 0 0 0 0 1
0 0 0 0 0 1

VA 1 LX 1 1 LX 5 2 LX 9 3 LX 12 4 LX 15 5 LX 18 6

PS=160_LVS.psf

PD
OU
```

Step 2: Estimating the structural model

First, the relevant product term was estimated in PRELIS using the latent variables of product differentiation and market attractiveness respectively. Then, LISREL was used to estimate the structural model using the previously estimated latent variable scores.

LISREL input file:

```
DA NI=27 NO=160 MA=CM
RA=160_LVS.psf

SE
21 22 23 24 26 27/ !selection of variables

MO NY=3 NX=3 GA=FU,FI BE=FU,FI PS=DI,FR !model specification

LE
Formal_contracts relational_contracts asset_specificity ! Labelling
endogenous variables

LK
prod_differentiation relational_capability PRODUCT_TERM ! Labelling
exogenous variables

FR BE 1 3 BE 2 3 ! Structural relationships among endogenous variables

FR GA 2 2 GA 3 1 GA 2 1 GA 3 3 GA 1 2 ! Structural relationships among
endogenous var.

PD
OU ML TO SS TV EF
```

11.3.1.2 Method 2: Single product indicator (cf. Jöreskog-Yang)

LISREL input file:

```
TEST of product term model
DA NI=25 NO=160

CM FI=160_product.cov
ME FI=160_mean.me

SE
9 10 11 13 14 15 16 17 18 22/ !selection of variables

MO NY=3 NE=1 NK=3 NX=7 LX=FU LY=FU TD=SY TE=SY PH=SY PS=SY GA=FU,FR C
BE=FU GA=FU KA=FU TX=FU TY=FU AL=FU

LK
proddiff attr PDMA

LE
assetspec
```



```

PA LY
1
1
1

PA LX
1 0 0
1 0 0
1 0 0
0 1 0
0 1 0
0 1 0
1 1 1 ! see Jaccard and Wan (1996:56-59) for explanation

PA TE
1
0 1
0 0 1

PA GA
1 0 1 ! specifying the structural relations

PA BE
0 ! no relations among endogenous variables

PA PS
1

PA KA ! Kappa specifies the latent variable means for the predictor
!variables
0 0 1 ! mean centering the latent predictors
CO KA(3)=PH(2,1)

PA PH
1
1 1
0 0 1 ! fixing the variances with the product to be zero
CO PH(3,3)=PH(1,1)*PH(2,2)+PH(2,1)*PH(2,1)
PA AL ! ALpha matrix specifies the intercept of the regression equation
to be zero
0
PA TD
1
0 1
0 0 1
0 0 0 1
0 0 0 0 1
0 0 0 0 0 1
1 0 0 1 0 0 1

CO TD(7,7)=TX(1)*TX(1)*TD(4,4) + TX(4)*TX(4)*TD(1,1) + PH(1,1)*TD(4,4) +
PH(2,2)*TD(1,1) + TD(1,1)*TD(4,4) !see Jaccard and Wan (1996:56-59) for
!explanation

CO TD(7,1)=TX(4)*TD(1,1) !see Jaccard and Wan (1996:56-59) for explanation
CO TD(7,4)=TX(1)*TD(4,4) !see Jaccard and Wan (1996:56-59) for explanation

PA TY
1 1 1

```

```
PA TX
1 1 1 1 1 1 1

CO TX(7)=TX(1)*TX(4) !see Jaccard and Wan (1996:56-59) for explanation
CO LX(7,1) = TX(4) !see Jaccard and Wan (1996:56-59) for explanation
CO LX(7,2) = TX(1) !see Jaccard and Wan (1996:56-59) for explanation

FI LX(1,1) LX(4,2) LX(7,3) LY(1,1) !set reference indicators
VA 1.0 LX(1,1) LX(4,2) LX(7,3) LY(1,1) !set reference indicators

OU SC RS AD=OFF IT=200
PD
```

11.4 Appendix D: Fit indices selection and justification

Following the recommendations of Tanaka (1993) and Hoyle and Panter (1995), a justification for the fit criteria chosen, a definition of them, and a specification of the “critical value” of each index are provided below.

Traditionally, overall model fit has been based on the chi-square statistic. Given the known sensitivity of chi-square to variations of sample size, a number of other fit indexes have been proposed and evaluated (for reviews, see Hu and Bentler 1995; Gerbing and Anderson 1993; Marsh, Balla, & McDonald 1988; Tanaka 1993). Given the variety of fit indexes, it has become common to discriminate between them in terms of absolute and incremental type of fit indexes (Gerbing and Anderson 1993; Tanaka 1993). An absolute fit index assesses the degree to which an a priori model reproduces the sample data. Reference is made to a saturated model that exactly reproduces the observed covariance matrix (Hu and Bentler 1995). An optimal fit is typically indicated by a value of zero, with increasing values indicating that the covariance matrix implied by the a priori model departs from the observed covariance matrix. An incremental fit index, also called a comparative fit index, measures the proportionate improvement in fit by comparing a target model with a more restricted baseline model (typically a null model in which all observed variables are uncorrelated). In contrast to absolute fit indexes which gauge “badness of fit”, incremental fit indices gauge “goodness of fit”; higher values indicate improved model fit (Hoyle and Panter 1995). This latter group can be further divided into three groups of indexes, types 1, 2, and 3 (Hu and Bentler 1995). In total, then, there are four different categories of fit measures.

There is little consensus among researchers concerning the best index of overall fit for evaluating structured equation models. Hence, most investigators who have evaluated and compared extant indexes encourage reporting multiple indexes of overall fit (Bollen 1989; Marsh, Balla & McDonald 1988; Tanaka 1993). In doing so, the most persuading approach would be to pick indices that emphasize different aspects of model fit, so that the model is evaluated from different perspectives. Below, a set of indices are chosen to meet this appeal.

The first category of fit indices is the type-1 incremental fit index. These indices use information from the optimized statistics T that is used to fit baseline and target models, and assess the adequacy of a target model in relation to a baseline model. Examples of fit indices from this category are NFI and BL86. Both of these indices are positively associated with

sample size and tend to overreject true models at small sample sizes (Hu and Bentler 1995). Following the recommendations of Hu and Bentler (1995) and Hoyle and Panter (1995), no indices are selected from this category.

The second category of fit indices is the type-2 incremental fit index. These indices are based on an assumed distribution of variables, and use information from the expected values of a target model and a baseline model. NNFI (or TLI) and IFI (or BL89) are examples from this category. Both these indices perform well with ML estimation, and are not related to sample size. NNFI are significantly downwardly biased with GLS estimation. As this study uses ML estimation, this is not a problem. Both these indices will therefore be reported.

The third category of fit indices is the type-3 incremental fit index. Like type-1 incremental fit index, these indices use information from the optimized statistics T that is used to fit baseline and target models, but also use information from the expected values of T_T and/or T_B under the relevant noncentral χ^2 distribution (Hu and Bentler 1995). Among the ones available, CFI is the most preferred (Hoyle and Panter 1995), and will therefore be reported in this study.

An absolute fit index assesses the degree to which an a priori model reproduces the sample data. A number of such indices have been developed (GFI, AGFI, CAK, CK, MCI) (Hu and Bentler 1995). Among these, despite the numerous troubles associated with it (e.g., effect of sample size and latent variable dependence), the χ^2 should be reported (Hoyle and Panter 1995). The χ^2 test is a test of perfect fit. As perfect fit is known a priori to be false in social sciences (it is, at best, an approximation to reality), a test of close fit is more realistic (Browne and Cudeck 1993). For this purpose, they recommended RMSEA. In contrast to the incremental fit indices, this test statistic has a known sampling distribution and can therefore be applied as a test statistic.

The table below summarizes the selection and definition of the indices, as well as specify their critical values

Table: 11-1: Chosen fit measures

<i>Name</i>		<i>Definition</i>	<i>Critical value</i>
Incremental fit indices			
Type-2	NNFI	Compares the lack of fit of a target model to the lack of fit of a baseline model	Good fit: NNFI > 0.90
	IFI	Same as NNFI	Good fit: IFI > 0.90
Type-3	CFI	Compares the lack of fit of a target model to the lack of fit of a baseline model, using the noncentral χ^2	Good fit: CFI > 0.90
Absolute fit indices			

	χ^2	Measures the degree to which a priori model accounts for observed correlations among indicators	
	RMSEA	Measures the degree of close fit of the model in terms of discrepancy per df.	Very good fit: RMSEA < 0.05 Acceptable fit: RMSEA < 0.08 Mediocre fit: RMSEA < 0.10

11.5 Appendix E - Scale reliability evaluation in LISREL 8.50

Scale reliability reflects the precision or consistency of the measurement of the construct, and is defined as the overall percentage of true variance in observed variance on a given measure. Cronbach's α has been the most commonly used estimator of scale reliability in the social sciences. The problems with Cronbach's α are well known; it only equals scale reliability when all observed variables are tau-equivalent, i.e. equal error variances. Needless to say, this requirement is not met very often.

Raykov (2003) designed a procedure to test scale reliability in LISREL, taking into account that observed variables are not necessarily tau-equivalent. Following earlier research, he defined the reliability coefficient ρ_y of the total score $Y = Y_1 + Y_2 + \dots + Y_k$ (assuming that errors are uncorrelated) as;

$$\rho_y = [(\sum b_i)^2] / [(\sum b_i)^2 + (\sum \theta_{ii})],$$

where $\sum \theta_{ii} = \text{Var}(E_i)$ are the error variances. The LISREL syntax is shown below. Note that the syntax is for a four-item scale. If the scale has a different number of items, the syntax needs to be adapted a little bit.

```
DA NI=50 NO=160 MA=CM
CM FI= inputfile.cov
MO NY=4 NE=4 PS=SY,FI ! PS(2,2) through PS(4,4) are dummy var's
FR LY 1 1 LY 2 1 LY 3 1 LY 4 1
VA 1 PS 1 1 ! the first dummy are preset to 1

FR PS 2 2 PS 3 3 PS 4 4

CO PS(2,2) = LY(1,1)**2 + LY(2,1)**2 + LY(3,1)**2 + LY(4,1)**2 + C
2*LY(1,1)*LY(2,1) + 2*LY(1,1)*LY(3,1) + 2*LY(1,1)*LY(4,1) +
2*LY(2,1)*LY(3,1) + C
2*LY(2,1)*LY(4,1) + 2*LY(3,1)*LY(4,1) ! The numerator

CO PS(3,3) = LY(1,1)**2 + LY(2,1)**2 + LY(3,1)**2 + LY(4,1)**2 + C
2*LY(1,1)*LY(2,1) + 2*LY(1,1)*LY(3,1) + 2*LY(1,1)*LY(4,1) +
2*LY(2,1)*LY(3,1) + C
2*LY(2,1)*LY(4,1) + 2*LY(3,1)*LY(4,1) + C
TE(1,1) + TE(2,2) + TE(3,3) + TE(4,4) ! The denominator

CO PS(4,4) = PS(2,2)*PS(3,3)**-1 ! this is the scale reliability
coefficient (the equation)

ST .5 ALL ! start values
OU NS
```