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Trust and Performance in Cross-Border Marketing Partnerships: A Behavioral Approach

Preet S. Aulakh, Masaaki Kotabe and Arvind Sahay

The globalization of the business environment and the need for competing simultaneously in multiple markets have led to the proliferation of inter-firm marketing partnerships across national borders. For instance, manufacturing firms are using distribution or licensing partnerships with foreign companies to access complementary marketing skills, make quick entry into foreign markets, reduce risks and costs of doing business in foreign markets, and circumvent tariff and non-tariff barriers, among others [Contractor and Lorange 1988; Kotabe and Swan 1995]. In these partnerships, the manufacturing firm (hereon referred to as the focal firm) depends upon the foreign distributor or licensee to penetrate the market and achieve adequate sales growth and market share for its products. Given that the focal firm's success in a given foreign market is intertwined with the performance of the partnership, a major challenge for its management is to ensure that the partner firm conforms to its contractual obligations to optimize partnership performance.

The importance of managing cross-border interorganizational partnerships is reflected in the extensive literature on this topic which has focused primarily on the *ex ante* structuring of cross-border partnerships (see Parkhe [1993a] for a review). For instance, a number of studies have examined the rationale for international partnerships, including joint ventures (e.g.,

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Contractor and Lorange [1988]; Hagedoorn [1993]), partner selection and characteristics (e.g., Geringer [1991]; Parkhe [1993c]), and performance effects of ownership control in such partnerships (e.g., Beamish [1985]; Geringer and Hebert [1989]). The underlying premise of these studies is that choosing the appropriate partner, aligning strategic and economic incentives of the partner firms, and using ownership control are critical determinants of partnership success, and mitigate the risk of opportunistic behavior inherent in interorganizational relationships. While this research stream provides important insights into the structuring of cross-border partnerships, it sheds little light on the appropriate maintenance of existing relationships. It is assumed that a firm has a choice among many foreign firms to make a partner selection, and that it has the scanning capability to make the optimal choice. However, there is evidence that the choice of foreign partner is often mandated by the host government, or that firms do not choose optimal partner firms due to the information asymmetries about long-term partner objectives during the initiation stage. In these cases, the critical determinant of partnership success becomes the ex post maintenance of the partnership.

A second stream of research on cross-border partnerships complements the structural approach described above by explicitly considering the behavioral dimensions that are relevant to the maintenance of interorganizational partnerships (e.g., Beamish and Banks [1987]; Bradach and Eccles [1989]; Casson [1992]; Hill [1990]; Madhok [1995]). The behavioral element of importance in these studies is the role of trust, for according to Casson [1992, p. 11], "in a high-trust environment the true nature of economic relations cannot be inferred from the ownership structure because the relations that really matter exist in the social fabric beneath." Thus, trust has the potential of enhancing our understanding of the dynamics and performance of interorganizational relationships.

The purpose of this paper is to extend this behavioral approach by identifying the antecedents of trust in cross-border marketing partnerships and examining the relationship between trust and performance. The choices for a manufacturing firm in organizing its marketing activities in foreign markets can be viewed along the markets and hierarchies continuum [Heide and John 1992; Webster 1992]. In between the extremes of one-time spot transactions and vertically integrated hierarchies, there exist various intermediate forms including repeated transactions, strategic alliances/joint ventures, and networks. The fundamental property shared by these intermediate forms is that they involve long term relationships with one or more foreign firms [Thorelli 1986; Webster 1992]. We define partnership in this study to mean any long term relationship that exists between two firms. In particular, the focus is on two specific types of marketing partnerships: manufacturer-foreign distributor and licensor-foreign licensee.

This study builds on previous research on four aspects. First, the study explicitly examines the behavioral determinants of inter-firm trust, which has been identified as an important alternative to hierarchical exchanges (i.e., ownership-based control). Second, it explores the different types of monitoring mechanisms available to the focal firm that are functional substitutes of control and enforcement, normally considered to be achieved through ownership in vertically integrated hierarchies [Grossman and Hart 1986; Noordewier, John and Nevin 1990]. Third, the study examines the effects of trust on partnership performance. Fourth, the conceptual model is empirically tested on a sample of U.S. firms' partnerships with foreign firms in Asia, Europe, and Central/South America.

The rest of the paper is organized as follows. In the next section, the conceptual model is introduced through a survey of the relevant literature. This is followed by the development of specific research hypotheses to be empirically tested. Next, after reviewing the research method used in the study, we report the results of the empirical tests. The last section discusses the implications of the findings along with the study's limitations and directions for future research.

Conceptual Model and Research Hypotheses

Role of Trust in Interorganizational Partnerships

The concept of trust has been examined in a wide variety of organizational and social settings, and accordingly conceptualized in different ways [see Hosmer 1995 for a review]. For instance, trust in interpersonal relations is defined as the willingness of one person to increase his/her vulnerability to the actions of another person [e.g., Zand 1972]; in economic exchanges as the expectation that parties will make a good faith effort to behave in accordance with any commitments, be honest in negotiations, and not take advantage of the other, even when the opportunity is available [Hosmer 1995]; and in society as a collective attribute based upon the relationships in a social system [Lewis and Weigert 1985]. A review of the literature examining trust points towards two issues relevant to this study. First, although trust, with its property of bilateral expectations of behavior, exists between individuals, it can be extended to exchanges between organizations because interorganizational relationships are managed by individuals in each organization (e.g., Bradach and Eccles [1989]; Hosmer 1995]). Thus, as suggested by Madhok [1995] and Thorelli [1986], trust in inter-firm relationships includes a set of expectations between the partners regarding each other's behavior and each partner's fulfillment of its perceived obligations in light of such anticipation. Second, the literature suggests that the "expectations of behavior" between exchange partners has two components: structural and behavioral [Hosmer 1995; Madhok 1995]. The structural component refers to the form of trust fostered by mutual hostages and complementarity of resources contributed by the partners [Madhok 1995]. As suggested by Madhok [1995], the structural dimension may be essential for the creation of the relationship but not sufficient for its continuation, because one partner may become more vulnerable in the relationship because of unequal dependence.

The behavioral component of trust refers to the confidence aspect in exchange relationships. For instance, Moorman, Deshpande and Zaltman [1993: 82] define trust as "a willingness to rely on an exchange partner in whom one has confidence." Similarly Anderson and Narus [1990: 45] focus on this confidence aspect of trust by defining it as a "firm's belief that another company will perform actions that will result in positive outcomes for the firm as well as not take unexpected actions that result in negative outcomes." This behavioral element of trust becomes particularly useful in the maintenance of ongoing relationships, since cooperation is not achieved with structural vulnerability but due to the confidence in the integrity of the exchange partners. Thus, following Morgan and Hunt [1994], we focus on the behavioral dimension by conceptualizing trust in a partnership as the degree of confidence the individual partners have on the reliability and integrity of each other.

Existing literature identifies three interrelated roles of trust in interorganizational exchanges. First, trust in organizational exchanges is an important deterrent to opportunistic behavior [Bradach and Eccles 1989]. Since interorganizational partnerships involve two or more firms which try to balance individual gains with joint partnership performance, there is a strong probability that partnership goals are sacrificed for individual benefits, especially when such behavior is not transparent to the partner firm. However, if trust is embedded in the partnership, opportunistic behavior is unlikely to occur because partner firms will pass short term individual gains in favor of the long-term interests of the partnership [Axelrod 1986; Beamish and Banks 1987; Stinchcombe 1986]. It should be noted that the structure of interorganizational relationships also reduces opportunistic behavior by the partner firms due to forbearance accomplished through a mutual hostage situation [Buckley and Casson 1988] or "tit for tat" possibility in a game theoretic sense [Parkhe 1993b]. However, unlike the structural approach where the *ability* of partner firms to behave opportunistically is curbed, in a trust-based approach, the *motivation* for opportunistic behavior is minimized, because "behavioral repertoires are biased toward cooperation, rather than opportunism" [Hill 1990: 511].

Second, trust is considered to be a substitute for hierarchical governance, thus accomplishing organizational objectives in inter-firm partnerships when ownership-based control is not strategically viable or economically feasible. Unlike hierarchical exchanges, where formal authority structures based on ownership are used to enforce contractual obligations, trust-based interorganizational exchanges rely on mutuality of interests between partner firms

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[Bradach and Eccles 1989; Dwyer, Schurr and Oh 1987]. Trust allows for bilateral governance which accomplishes individual goals for independent organizations through joint accomplishments, shared beliefs, and mutual concern for long term benefits [Heide 1994; Ouchi 1980].

Third, besides the role of trust as a behavioral deterrent of opportunistic behavior and as an alternative to ownership control, there is also evidence that building trust in interorganizational partnerships has important market performance and efficiency implications [Bleeke and Ernst 1991; Parkhe 1993b; Wilkins and Ouchi 1983].

The literature discussed above strongly points to the importance of trust in achieving behavioral and market performance objectives in interorganizational partnerships, especially in cross-border relationships where hierarchical control may not be a viable alternative. However, little systematic research attention has been given to identifying the determinants of interorganizational trust. The purpose of this study is to fill this important gap in the literature by simultaneously identifying the antecedents of trust in cross-border marketing partnerships and formally examining the trust-performance relationship that has been implicit in previous research. The proposed conceptual model is provided in Figure 1.

Research Hypotheses

Building trust in cross-border partnerships can generally be accomplished over time. Since trust involves expectations about future behavior, it is necessarily guided by the past behavior of exchange partners. Partner firms have to learn about each other's ways of doing business and to interpret each other's acts [Håkansson and Johanson 1988]. It is proposed that bilateral relational norms between partner firms as well as the unilateral monitoring mechanisms used by the focal firm are both representations of past interactions and therefore would be important determinants of trust and performance of cross-border partnerships.[1]

Relational norms are defined as expectations about behavior that are shared by a group of decision makers [Thibaut and Kelley 1959; Heide and John 1992] and "provide guidelines for the initial probes that potential exchange partners may make towards each other" [Scanzoni 1979: 68]. According to Dwyer et al. [1987: 17], "by adopting norms and establishing standards of conduct, emerging exchange partners start setting the ground rules for future exchange." Thus relational norms prescribe acceptable behavior at the onset of interorganizational partnerships, which, if considered equitable by the partner firms, eventually lead to future expectations of trust [Ring and Van de Ven 1992]. Although a number of different overlapping relational norms have been identified in various disciplines, the three norms of continuity expectations, flexibility, and information exchange are particularly

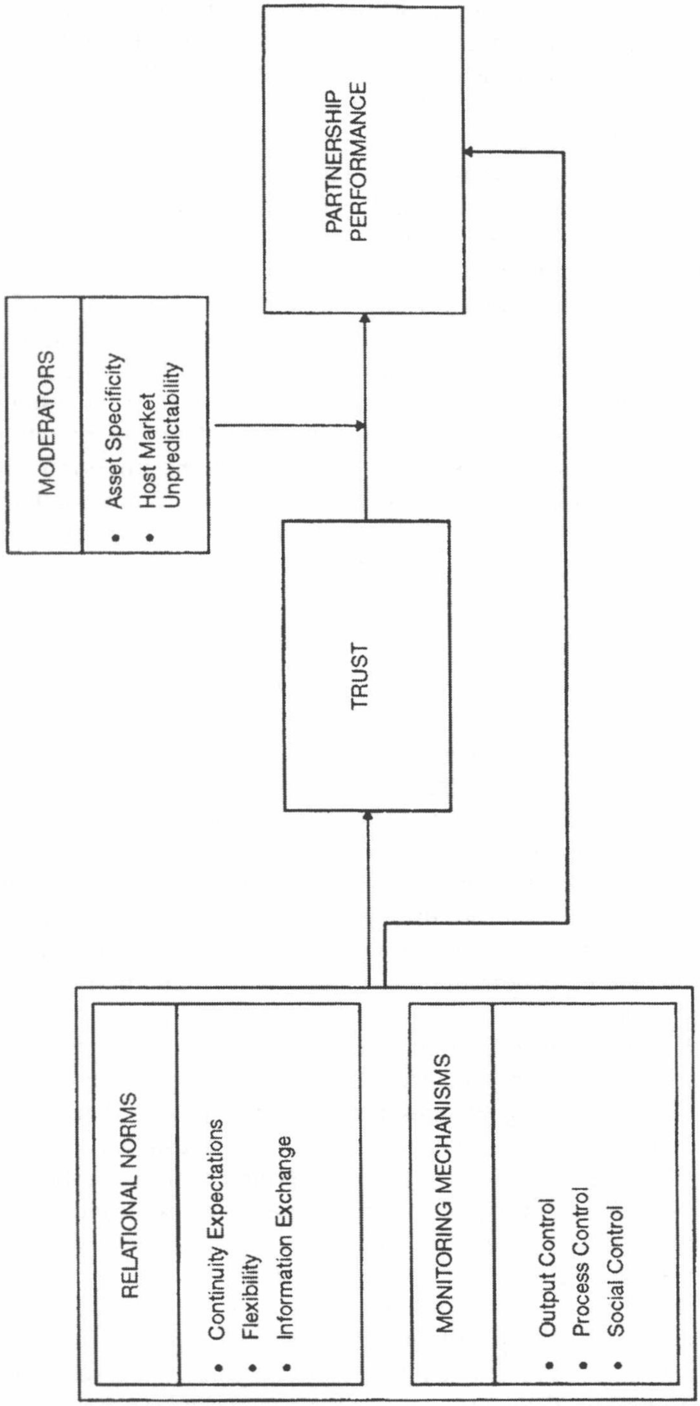

Figure 1: Conceptual model

important in marketing partnerships [Heide and John 1992; Kumar, Scheer and Steenkamp 1995], and are therefore considered in this study.

The norm of continuity expectations is the mutual recognition that the relationship will continue in the future. As a relational norm of continuity expectations is developed, exchange partners achieve a level of satisfaction with the relationship and thus do not look for alternative partners [Anderson and Weitz 1989; Dwyer et al. 1987]. Continuity expectation is analogous to the behavioral commitment in cross-border partnerships suggested by Cullen, Johnson, and Sakano [1995]. The norm of continuity expectations has the effect of encouraging partner firms to "perceive cooperation not as a means but an end in itself" [Buckley and Casson 1988: 39]. A norm of continuity expectations is hypothesized to be positively related to trust because the time horizon for mutual benefits is extended, thus making partner firms pass short term gains in the interest of the long term viability of the relationship. Furthermore, commitment in the relationship allows for long-term scenario planning by both partners. Thus, as suggested by Buckley and Casson [1988], commitment in the relationship leads to higher market performance of the partnership.[2] Based on the above arguments, the following hypotheses are proposed:

H1a: A bilateral norm of continuity expectations is positively related to the trust in the partnership.

H1b: A bilateral norm of continuity expectations is positively related to the market performance of the partnership.

The norm of flexibility in a partnership is defined as the willingness to make adjustments as circumstances change [Heide and John 1992]. Flexibility is particularly important in cross-border relationships because partner firms often operate in diverse political, cultural, and economic environments, thus making relationship adjustments imperative to deal with different and changing environmental conditions. Furthermore, partner firms are often called upon to react to unforeseen changes. Bleeke and Ernst [1991], in their study of forty-nine cross-border partnerships, found that alliances characterized by high degree of flexibility evolved better in the face of unexpected contingencies arising from changes in strategies, skills, and resources of partner firms. Thus, it is proposed that a norm of flexibility will be positively related to trust by creating a stock of goodwill [Madhok 1995], as well as enhance market performance because the firms can better respond to changing operating conditions. Accordingly,

H2a: A bilateral norm of flexibility is positively related to the trust in the partnership.

H2b: A bilateral norm of flexibility is positively related to market performance of the partnership.

The norm of information exchange in interorganizational partnerships is defined as the "formal and informal sharing of meaningful and timely information between firms" [Anderson and Narus 1990: 44]. Timely information exchange between partner firms fosters trust [Morgan and Hunt 1994; Moorman et al. 1993] because communications help in resolving disputes and aligning perceptions and expectations. Furthermore, the expectation of getting all information on an ongoing basis enables the partner firms to cope better with internal processes and external market conditions [Heide and John 1992]. Based on these arguments, the following two hypotheses are proposed:

H3a: A bilateral norm of information exchange is positively related to the trust in the partnership.

H3b: A bilateral norm of information exchange is positively related to the market performance of the partnership.

Monitoring Mechanisms

Besides developing bilateral relational norms to build trust and enhance market performance in cross-border partnerships, the focal firm can also use appropriate unilateral monitoring mechanisms to achieve the same objectives.[3] Conceptually, monitoring of the foreign partner involves establishing the extent to which contractual compliance has taken place [Heide 1994]. While most of the research based on transaction cost economics assumed that the ability to monitor and control in interorganizational relationships is dependent on the degree of ownership of the focal firm, there is a growing evidence that various types of monitoring mechanisms with fundamentally different properties, which are independent of ownership, can be put into place in interorganizational partnerships (e.g., Gencturk and Aulakh [1995]; Heide [1994]). These monitoring mechanisms provide the enforcement function normally thought to be achieved in hierarchical exchanges [Noordewier et al. 1990] and have both behavioral and performance consequences in interorganizational partnerships [Anderson and Oliver 1987; Jaworski 1988].

Organizational theory research suggests that monitoring in interorganizational partnerships from the perspective of the focal firm can be accomplished externally by explicitly measuring outputs or behavior of the partner firm [Heide 1994], or internally, by aligning the incentives of decision makers to reduce the performance measurement altogether [Heide 1994]. In particular three types of monitoring mechanisms are identified: output control, process control, and social control. Output and process controls are considered different types of formal controls since they represent focal firm initiated mechanisms which are generally linked to specific economic and behavioral outcomes respectively [Anderson and Oliver 1987]. Output control is defined as the degree to which the focal firm monitors the results or outcomes produced by the foreign partners, while process control refers to the extent to which the focal firm monitors the partner's behavior or the means used to achieve the desired ends. Social control is defined as establishing an organizational context that encourages self-control by the partner firm. Thus, instead of prescribing specific outcomes, social control involves building common organizational culture [Ouchi 1979], and performance is viewed as a social obligation maintained via mechanisms of social pressure [Jaeger 1983].

When using an output based monitoring mechanism, the focal firm is shifting the risk to the foreign partner, because specific performance goals are prescribed for the latter [Bergen et al. 1992; Eisenhardt 1989]. Since the foreign partner assumes most of the risk, output control encourages a loner attitude on the part of the foreign partner, because such control does not offer protection for the foreign partner against downside risk [Anderson and Oliver 1987]. Hopwood [1972] suggests that heavy reliance by the focal firm on quantitative measures of performance tends to increase the tension for the agent which leads to poorer behavioral relations with the focal firm. Output controls may encourage foreign partners to seek immediate payoffs at the expense of the partnership's long term goals. Thus, it is hypothesized that:

H4a: The use of output control by the focal firm to monitor the foreign partner is negatively related to the trust in the partnership.

H4b: The use of output control by the focal firm to monitor the foreign partner is negatively related to the market performance of the partnership.

Process-controlled relationships require active involvement by the focal firm management whereby it provides the inputs which the foreign partner needs to achieve partnership goals. Since the focal firm prescribes specific behaviors, it assumes all the risk. Such acceptance of risk sends a positive signal to the foreign partner and the motivation for opportunistic behavior is diminished. Furthermore, process control tends to result in supportive, yet more bureaucratic and formalized, relationships than output controls, thus reducing the uncertainty faced by the partner firm. Process control is also expected to enhance the market performance of the partnership since such behavioral monitoring mechanisms reward long term outlook by removing pressures and incentives to sacrifice long term for immediate results [Anderson and Oliver 1987]. Accordingly, the following hypotheses are proposed:

H5a: The use of process control by the focal firm to monitor the foreign partner is positively related to the trust in the partnership.

H5b: The use of process control by the focal firm to monitor the foreign partner is positively related to the market performance of the partnership.

Social control refers to an informal control that creates organizational context or culture whereby the need for formal measurement of either outcomes or behaviors is greatly reduced [Ouchi 1979]. Dalton [1971] suggests that informal controls can provide both the implicit rules and supportive structures to facilitate role understanding in organizational exchanges. The social identity theory further posits that social control in interorganizational exchanges is conducive to shared beliefs and mutual identification by the partner firms [Ashforth and Miles 1989]. Accordingly, in socially controlled partnerships, monitoring occurs through interpersonal interactions, and these repeated interactions over time lead to systematized and shared organizational values which help in building trust between the partners. The achievement of long term economic performance is also enhanced through social control. Through the process of socialization and indoctrination, the focal firm allows wide latitude to the partner firm thus enabling the latter to respond to conditions quickly and in a manner consistent with the goals and objectives of the partnership. Therefore, it is hypothesized that:

H6a: The use of social control by the focal firm to monitor the foreign partner is positively related to the trust in the partnership.

H6b: The use of social control by the focal firm to monitor the foreign partner is positively related to the market performance of the partnership.

Relationship between Trust and Performance

As discussed earlier, trust in interorganizational partnerships is likely to be positively related to the market performance of the partnership. This positive relationship between trust and performance has been empirically supported in a variety of intra- and interorganizational contexts (e.g., Crosby, Evans and Cowles [1990]; Robicheaux and Coleman [1994]) and also suggested in cross-border partnerships (e.g., Madhok [1995]; Parkhe [1993a]). Similar to these studies, we propose that:

H7: Trust is positively related to the partnership's market performance.

Since trust has generally been conceptualized as being the opposite of opportunistic behavior [Morgan and Hunt 1994; Parkhe 1993b], Bradach and Eccles [1989] propose that the risk of opportunistic behavior must be present for trust to have meaningful consequences. This suggests that trust becomes important only when there is risk of opportunistic behavior by the partners [Bradach and Eccles 1989]. In particular, from the focal firm's perspective, its investment in idiosyncratic assets specific to its relationship with the foreign partner creates a dependence situation which can be

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