

# ***The role of cultural differences in the dynamic of a relationship. The case of Italian and Chinese companies.***

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## **Introduction**

Intercultural differences have been identified as one of the main reasons of failure in business relationships with Chinese companies.

Many international contributions explain these aspects of business relationship (Fang and Ghauri, 2001, Fang, 1999, Ambler et al, 1999, Buttery and Leung, 1998, Foster, 1992). Notwithstanding the authors focus on the existing differences in cultures, a direct comparison between Chinese and Italian business culture has not been analysed yet.

After China's entrance into the WTO, the interest of Italian entrepreneurs towards China has increased. Italy holds 2nd position in Europe as regards exports towards China. It holds a lower position when it comes to direct investments in the Country (ICE, ISTAT, 2003). According to our opinion, the low propensity to invest in China for medium size Italian companies, among other reasons, is related to communication problems and cultural differences among the two cultures. Risk perception, as an example, is also related to cultural differences.

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Objective of this work-in-progress (wip) paper is to deepen the understanding of the business relationship process among Italian and Chinese companies to ultimately define the do's and don'ts Italian companies should follow to establish long lasting relationships with Chinese ones. This understanding is related to communication, interaction and management aspects of the business relationship. This wip paper is made of two parts, a first one related to the theoretical approach, where we explain culture, communication and negotiation. A second part is related to the empirical research.

In the first part, starting from a theoretical analysis, we examine the dynamics of the relationship existing in a negotiation context among Chinese and Italian companies. The main focus of our research is on cultural differences and communication problems between the two cultures. Cultural differences go far beyond the language; language is a major component of culture and is an important part in the negotiation. They need to be analyzed and considered, in order to establish endless and strong relationships with Chinese companies. In the second half of part one, we take as a reference the Ford's relationship phases model - pre-relationship stage, exploratory stage, developing stage and stable stage – (Ford, 1980, 1984) to understand how the practice of business relationship with Chinese companies has been led from the Italian point of view.

The second part of the wip paper is based on the empirical research. In particular it covers the key questions we want to address through the paper, the research method applied and the findings of our study - in terms of results-analysis in the negotiation process, and difference-analysis in the business cultural approach.

The wip paper ends with final consideration and open issues for further research.

## **Cultural differences among Western Countries and China**

The concept of culture has been analysed in depth: Tylor in 1871 (Nagels, 1996) identified culture with the social system; Hofstede (Hofstede, 2001), years later, proposed culture as a software of the mind. This software is actually not definable, it is a system made of way of thinking and habits. A person realizes these characteristics only when, and if, he is facing different cultures. Among the multitude of researches on culture, Hall (Hall, 1976) made probably the first breakthrough changing the point of view among the theories, G Hofstede (Hofstede, 2001) and F. Trompenaars (Trompenaars, 1993) went a step further. We decided to embrace G. Hofstede's theory which identifies some basics differences among the cultures. In his theory, he finds five comparison's levels, called dimensions, which gave us the most important features of every culture. Hierarchy level, collectivism vs individualism, uncertainty avoidance level, masculinity vs femininity, long time vs short time orientation. He gives for each

culture different values to each dimension. The results are that, generally speaking, western cultures tend to be more individualistic than Asian cultures. He highlights also that, in Asia, a boss, in order to be accepted needs to be the only one who takes action, and cannot delegate any function without losing power. On the other side In Europe a manager has more the function of a supervisor.

As stated above a person does not fully understand the software of the mind until he faces the differences. The way to face these differences is through communication, in all it's forms day-by-day, as well as business communication. Communication is a vehicle to exchange values and experiences and allows to understand the context where the parties live (Usunier, 1996). Differences are related to the encoding/decoding activities and to the cultural context of each speaker (Warthun, 1997). "Cross-cultural communication is like trying to follow a route on which someone has turned the signposts around. The familiar signs are there, but when you follow them, they take you in the wrong direction" (Tannen, 1979; Nagels, 1996).

Who wants to do business in China, may succeed only if he realizes the cultural differences and insert these new values in his business code. Beyond the knowledge of the political, as well as economical situation of the region, the businessman needs to be familiar with the socio-cultural structure. Religion has an important role in this structure. Asia and China have shaped their business behaviour on their own religions (Bedi, 1991). In China there isn't a clear distinction between philosophy and religion (Chu, 1991). Among these aspects it is important to understand concepts and roles of "Guanxi" or personal relationship (Seligman 1990), "Danwei" or basic unity-family (Fang, 1999), "Mianzi" which means honour (Gao-Ting-Toomey, 1998) and "Xinren" or trust.

Those cultural differences find their full application in the business domain and in particular in the negotiation process where the parties - belonging to different cultures - interact, communicate and try to establish business relationships.

In this context with intercultural negotiation we refer to a social interaction process in which complementary parties try to solve incompatible or divergent goals through a win-win approach (Battaglia et al 2001, Tan and Lim 2004).

If we take the above mentioned points in a day-by-day negotiation process between an Italian and a Chinese company, we realize that the gap between the two business styles could be a reason of misunderstanding and in many cases of failure (Nguyen et al, 2003).

Another difference between the two cultures is the hierarchy level: Italian society has, generally speaking, a shorter hierarchy level. This means that often, in a company, the bottom and middle level of management have more decisional power than in China. The hierarchy level and the connected decisional power make a

difference also when it comes to critics. Although there is no culture where a someone criticize another person in front of other people, it is true, that in Italian culture, an open discussion between two persons with a different point of view is seen as stimulating and not negatively.

Personal status needs to be respected, and not forgotten, in Chinese culture, such an important point is highlighted through repetition instead of raising the voice or changing the tone as it is in Italian culture. Confucianism teaches that repetition is more important than invention, through repetition a person comes every time closer to perfection. Time has also another value, or, a bigger value is given to situations which for Italians would not request much time.

Although personal knowledge is very important for doing business in Italy too, it is also true that usually this knowledge is established only after having done the business. The Chinese culture sees a great importance in the personal knowledge and this is the mandatory basis for any further step (Kriz and Fang, 2003).

In the Chinese culture, harmony has an important role: people act always trying to keep the harmony and the balance (Kriz et al, 2002) with the counterpart. This is the reason why people express themselves indirectly. Another great difference among the two examined cultures lies in ethic. What is ethic or not, is obviously not the same for everyone and in every culture. To the majority of European people, in the Bin Fa, is full of unethical behaviours. T. Fang (1999) identifies the core of the Chinese business culture in the interaction among "*mianzi*", "*guanxi*", "*guoqing*" and "*ji*" (stratagems),.

### **Ford's model on relationship development**

The evolution path of a business to business relationship has been theorized by many academics belonging to the "relationship management" stream. Ford (1980, 1984) has proposed a five step model which can be applied to a dynamic analysis of a business relationship: pre-relationship phase, exploratory phase, developing phase, stable phase and final stage.

These phases are not simply linked by the time flow but are the consequence of a specific behaviour held by the two or more parties involved in the relationship.

Among many others, this model underlines the central role of the perceived distance between the two parties in the relationship, as a critical factor which can influence (positively or negatively) the evolution, from one phase to the next in a business relationship. Here the distance is not only a physical constraint (as we may think when referring to a Sino-European negotiation) but it is represented also by a social distance, a cultural distance, a technological distance and a time distance, qualified by a different time reaction in stimulus-responses.

- **pre-relationship phase**

One of the two parties (in a buyer-supplier relationship example) decides to look for a new partner. In this circumstance he/she decides to collect most of the information regarding the potential partner and the environment in which he/she operates. Since it is important and fundamental to create a positive image in order to build trust in the mind of the counterpart, the proponent will try also to evaluate every previous experience emerging from other similar relationships and, for instance, will work in order to find a third party able to intermediate in a different cultural context. At this stage, uncertainty, in a positive evolution of the relationship, drives the parties to select very carefully every effort and investment, at least, until the relationship shows a serious space where to build the common business.

- **exploratory phase**

This step is very critical because, the perceived satisfaction will directly influence the continuity and the intensity of the relationship. Notwithstanding, none involved in the relationship, knows clearly the objective and the motivation of the counterpart. The absence of a mutual, or standardised procedure, to solve clashes, force the parties to a psychological bid, to get the satisfaction and improve the relationship. Since the perceived distance among the parties is very significant, the required investment here, is related to the creation of a relationship with the counterparts.

- **developing phase**

The relationship is going to be settled. The fulfilment of the duties gives strength to the relationship and reduce the perceived distance between the operators, and as a consequence this helps to better understand and evaluate the intrinsic uncertainty of the common business.

- **stable phase**

In the stable phase the counterparts have already reduced all the aspect that in the previous phases could have been potential problems (uncertainty, perceived distance, undeclared objectives, unshared knowledge and experience). The big issue at this stage, is represented by the shrinkage of attention and engagement, and not least, the need of creativity in order to renew the stable relationship. This aspect is crucial; this could lead the counterpart to follow opportunistic goals since they already learned how to deal with normal procedures (let's take as an example the imitative attitude of the followers, typical in the far-east countries).

- **final stage**

This happens when the parties are not able to re-launch new challenges and are overwhelmed by static procedures and operations, losing the capabilities to foresee the dynamic opportunity showed by the markets. Notwithstanding, in this

step the interaction among the different organizational levels of the parties are maximum, the essence of the relationship could vanish in absence of new feed.

In our study we will take this model as the backbone for a research over the relationship occurred between 11 Italian companies and as many Chinese counterparts. On the basis of deep personal interviews with Italian companies, who have decided to upfront the Chinese market (as regards supply of goods, production or distribution), we will highlight the essence of the initial issue, explained in the concept of perceived distance.

## **Issues and Research Method**

In accordance with the purpose of the paper, stated in the introduction, detailed objectives of this *wip* paper are: i) to define the importance of intercultural communication in each stage of the relationship; ii) to establish the role of relationship-connection (*guanxi*) and trust (*xinren*) in the negotiation process; iii) to find out whether the companies are aware of these aspects; and iv) to define which are the main cross-cultural factors that drive toward the success or the failure of a business relationship between Chinese and Italian companies.

The explorative research is based on 11 face to face interviews to Italian companies, operating in different industries, that have approached the Chinese market.

In this first approach to the research we decided to explore the relationship by one side only. Reason why is related to the proactive attitude used by the Italian party. Since the Italian companies decided to approach the Chinese market starting a new relationship in a foreign country, we assume that they had to show enough flexibility in order to understand the new country culture and to fit with it. On the opposite, the Chinese counterpart playing an “in-house game”, had to guarantee a good welcome approach level but a limited adaptive style concerning the way to interact in intercultural context.

Starting from the assumption that the main role of cultural mediator is played by the initiator, who has to show capabilities to interact in a different intercultural domain, we focused initially our research to understand the feeling of the Italian companies facing a new intercultural relationship. For this reason, considering the high costs of a double check-interview with the Chinese counterpart should imply, we decided to interview Italian companies only. We aimed to understand the first-mover's level of consciousness of the gap among the two cultures. We interviewed in-depth these companies exploring their experiences in the different steps of the

negotiation process with Chinese companies. The approach followed took its start from the suitably revised relationship life-cycle model: preparation activities, first face-to-face, negotiation development, deal closure, implementation. The interviewee target we decided to contact is or the manager who has initiated the relationship the first time, or the manager who has been in charge to develop it. In general and according to the size of the companies, we referred to the export managers, the sales managers, the operation manager (in the case of purchasing agreements) and the owner of the companies in the small and medium enterprises (SME).

## **Interviews analysis**

### **The analysis of the negotiation process**

The Companies interviewed show the characteristics listed below in Figure 1. The reasons leading Italian companies to invest in Chinese market were: an expectation of market growth, and the needs to reduce costs and to beat forging. Objectives of the investments were rather the production in Joint Venture (JV), the sale of their own products, or the selection of alternative sources of supply. As shown in Figure 1, most of the companies established commercial relations many years ago (15-20) through commercial intermediaries from China, or Hong Kong, or Taiwan and/or through their own commercial offices.

Only two of the interviewed companies have big size (presence in the stock exchange market, world wide reputation, holding of multinational companies, etc.). The remaining companies belong to the Medium level enterprises and have at the best foreign commercial offices in Europe or Mercosur markets. This sub-group, having limited resources addressed to new foreign business development decided to give a strong mandate to intermediaries in order to create a first contact in China. As a consequence they overcome the problem, and the opportunity, to manage directly intercultural relationship.

In these circumstances the intercultural difference perception, revealed during our interviews, are blended by the intermediary filter. Notwithstanding the mediator role done by the agents, many issues arise as regards relationship with different culture.

See Figure 1

The analysis shows major topics in each step of the negotiation process above mentioned:

- **pre-relationship phase**

All the interviewed companies started their commercial experiences with China many years ago and through an intermediary as they normally do when they face a new foreign market; moreover, they used to attend international exhibitions related to their specific market sector. These previous international experiences permitted to create valuable links in the Country and to build a certain level of image according to the size and the position in the specific sector of each company.

Despite the presence for many years in the country we found a “scanty knowledge of Chinese culture” that limits the exploitation of additional opportunities.

Medium size companies indicate a generic cultural diversity, the irrelevance of the “*guanxi*”, the unknown concept of the “harmony” and the different concept of the “family”. These companies manage their business in China, through an intermediary (the Chinese employee just hired, the agent from China or Hong Kong or from another Asian country) who *de facto* manages the deal. He works as a filter, positive or negative, between the two cultures. These companies did not entered in the Chinese culture.

On the other hand, major size companies, who manage the deal directly with interpreters, are more aware of the importance of the culture knowledge and in particular of the relevance of the relation (*guanxi*), the importance of the right person and connection, and the fundamental role of trust (*xinren*) in building any business in China. This last aspect is also relevant for “intermediary-managed companies” even if they do not realised that “trust” is required before starting a relationship.

- **exploratory phase**

This stage measures the interactive step and the distance among the parties, according to the cultural differences. Major findings are: i) Time has a different value, it is used as a psychological lever by Chinese and is also seen as measure of the interest of the Italian company “the more time you spare, the more interest in the counterpart you show”; ii) Comprehension degree shows a different result based on the type of the company. In medium size “intermediary-managed companies” it is high because of the intermediary action, these companies do not feel any problem of comprehension except for the language itself; in “direct managed deals companies” comprehension degree is low because sometimes it is difficult to understand the real wish of Chinese Party. Interpreter, in this case, plays an important role because it helps decreasing the gap between the counterparts, on one side “giving time to think about the answer” and on the other side “providing further information on how to react in that specific context”; iii) Chinese etiquette permits to increase personal knowledge, to build business friendship and trust and

to reduce distances “it is easier to discuss a matter after having shared a good dinner”.

In general, “intermediary-managed companies” solved most of their in-depth knowledge and communication issues with the Chinese counterpart. The trust lays, in this case, in the local intermediary chosen as a partner.

- **developing phase**

Signature of the deal takes from 5-6 months to a year in both direct and intermediary managed deals. Further JV deals requires less time due to the strength of the relationship and the building of the trust (*xinren*). Trust permits to develop, quickly and easily, additional business relationships with the same or with a different counterpart. In order to sign a contract it is necessary to overcome some problems related, once again, to cultural differences, more often than not understood: i) flexible approach towards disagreements: all the companies interviewed show the strong wish to establish win-win relationships. This implies the search of the right solution even if sometimes Italian companies do not understand how the real problem arose; ii) re-negotiation of defined clauses: signature of the contract is a formality, uncertainty in negotiation with China is part of the deal, even after the final signature. It is a common opinion that Chinese companies tend to get advantages at any time, it is not understood that they may send “false signals” to let the counterpart know there is a problem somewhere; iii) indirect style of communication: because of their search of harmony, Chinese negotiators send false messages to let Italian counterpart know they do not agree on some points. It is fundamental to understand the signals and check, with the third party involved (the trustee), to find the right way to go ahead.

- **stable phase**

All the interviewed companies showed satisfaction in the defined deal that is still alive. Companies that reached this stage overcome cross-cultural problems, alone or with a local partner. Success is due to i) the wish of the Italian companies to establish a win-win long lasting relationship. Relevant to notice is that “it took sometimes to convince the Chinese counterpart to reinvest profit in the JV” or that “satisfaction has to be measured in the long run since initial false deals may sort out as excellent deals and vice versa”; ii) the necessity to build the trust over the time both in the direct and intermediary managed deals; iii) re-negotiation is part of the negotiation; iv) keeping the deal alive is fundamental, this means to provide interest to the Chinese counterpart at any time, otherwise he/she looks for other opportunistic alternatives.

- **final stage**

The few cases of death occurred in the limited sample analyzed bring the causes to cultural differences still, in particular to the different concept of business ethics

among the parties. Failures were due to: i) high divergence of objectives in particular when the Chinese counterpart is State-owned and he/she plays different roles according to the people involved in the various meetings the approach to the deal is seen under an opportunistic perspective; ii) dual role played by the Chinese counterpart when he/she was dealing at the same time with the company and its best competitor; iii) lack of honesty and reliability on the Chinese side when they heavily forged the alleged partner.

**The analysis of business cultural approach differences**

In this section we outline the potential differences or analogies existing in the way the two cultures run business.

Starting from the view of the Italian side, we asked to show us the perceived positioning of the two parties on a scale from 1 to 10, with two contrasting attributes at the opposite. This enabled us to understand the typical way to approach a problem (under the Italian perspective only) and how much the two cultures differ in the response.

In order to better understand the method applied, it's easier to see directly the 10 topic results obtained from the interviews.

Here below we show the average result from the 11 interviews done during this exploratory research. Standard deviation of the single answers is given to demonstrate the relevance of the average per every single topic. Ten topic results are classified by rank of differences in cultural approach.

- **Topics with significant approach differences**

In this group we count four topics which score three or more points of distance in the positioning.

***Interaction perception toward communication in each team.***

As shown in figure 2 the contrast is the dichotomy between an egalitarian style (belonging to a team which encourage the participation of each member) or, on the opposite, a hierarchical style (where only one member of the team is enabled to communicate and manage every problem with the counterpart).

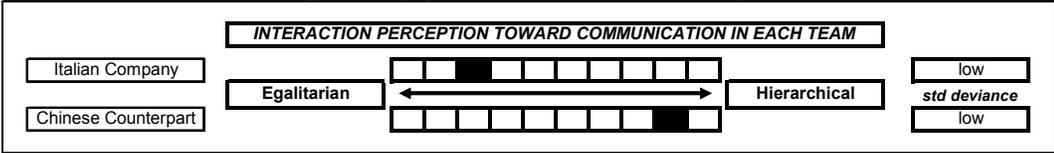


Figure 2 – egalitarian vs. hierarchical participation

The approach distance is very high given that the two positions differs for 6 point over 10 maximum. Italian companies perceive them more egalitarian and, on the opposite, think that Chinese ones are more hierarchical oriented.

If we take in count a further segmentation based on the object of the investment (production joint venture, distribution agreement and buying agreement), the differences are stronger in JV agreement than in distribution or buying agreements. That's because in JV the agreement is very insidious and Chinese don't want to lose control on the deal.

**Style of communication**

Big differences arose also in the way the two counterparts communicate (see figure 3). Chinese adopt a style which is oriented to send indirect messages while Italian try to explain their ideas with clear and unequivocal messages.

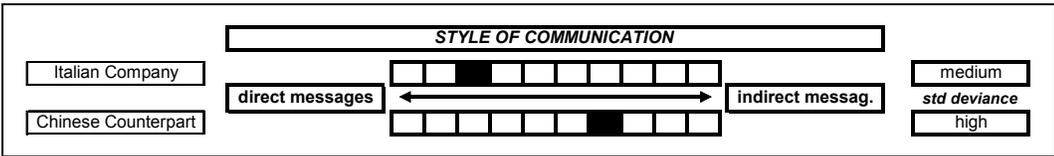


Figure 3 – direct vs indirect messages sent

This must be always kept in mind by the Italian because a positive answer doesn't always mean agreement on a specific topic, but it could be re-read as "I want to keep harmony". While a "no" it doesn't always mean a closure behaviour.

For this reason many companies decide to ask for help to a local trustee intermediary facilitating the flow of indirect messages.

**Problem solving approach**

This can be another field of potential cultural clash. European culture is based on rational and logical scheme while far east approach is generally more circular and intuitive. Notwithstanding business is a domain of quasi rational approach; figure 4 shows that the Chinese is inclined to non linear decision taking approach. The average of perception of the interviewed, as regard the Chinese approach, has a high deviance in each positioning and indicates that there isn't a clear and unique approach.

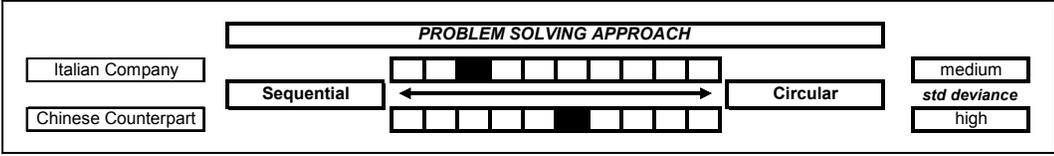


Figure 4 – sequential vs circular problem solving approach.

**Decisional power per each problem.**

This topic is focused on the ability of each team to take decisions (see figure 5). The Chinese counterpart suffers a limited decisional-power over problems occurred in the relationship. The difference in the positioning explains the difficulty,

mentioned by the interviewed, with regard to the timing and the procedures to speed up the negotiation. In order to reduce this gap any European company should correctly understand the decisional power of his counterpart and consequently redefine the timing to reach the target, otherwise its behaviour would seem to be too much compelling and reckless to the eyes of Chinese.

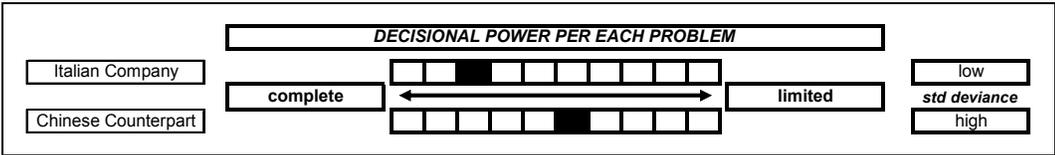


Figure 5 – decision taking: complete autonomy vs limited power.

When the object of the negotiation is a joint venture with common investments, the perception of the positioning of the Chinese to the eyes of Italian, is likely more limited, confirming the general idea of hierarchical organization of the Chinese companies. Where the negotiation is held by SME (Small and Medium Enterprises) the differences tend to disappear, thanks to the powerful decision taking process managed by the entrepreneur. These examples help us to better understand, the high level of deviance registered in the Chinese average.

- **Topics with affordable approach differences**

This section refers to the topics which positioning differences score two points. Notwithstanding there is no significant difference in the approach, it's important to point out the different behaviour in order to improve the complementarities among the potential partners.

**Relationship approach**

The way the parties approach the relationship is influencing the level of trust. Our research shows (see figure 5) that the Italian companies are quite more informal than the Chinese ones.

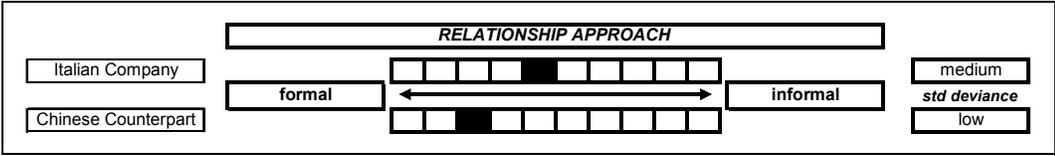


Figure 5 – Formal relationship approach vs informal.

These differences are not so relevant to eventually compromise the success of the relationship. While the behaviour of the Chinese partner has a low deviance from the average, as a symptom of a rooted cultural approach, the Italian one is more

varying in order to fit the circumstances and it is in accordance with a typical Italian attitude.

### **Agreement horizon**

Italian companies have a favourite orientation to long lasting agreement while Chinese ones are more inclined to maximise short term benefit.

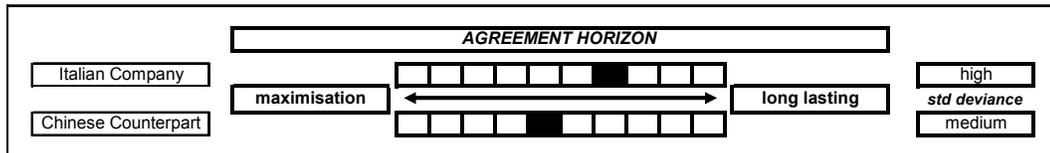


Figure 6 – Agreement horizon: short term maximisation vs long lasting mutual benefit

The interviewed told us that the short term orientation of the Chinese counterpart is due to the lack of expectation and , the evaluation of the uncertainty related to new way of making business.

This is a considerable alert for any European company who decides to do business in China. In order to reduce the cultural differences, they should define intermediate target to pursue the aim of a long lasting relationship.

- **Topics with irrelevant approach differences**

Our research shows that there are many topics where the positioning of the two companies are almost the same.

In particular we count: relational dialectic (comprehension vs. proposal), negotiation attitude (impatient vs. harmonious), persuasion approach (aggressive vs. shared)

For all these three items we found the score given by the interviewees was aligned to the median for both the parties.

### **Final considerations and open issues**

From our explorative research (11 value cases only) it emerges that intercultural communication is very important in each phase of the negotiation process, particularly in the initial phase when companies need to build and develop a common understanding, working together and creating mutual trust.

This is true especially nowadays, a time of high economic changes in China and of higher entrepreneurial of SME in the region.

To create long lasting relationships in China Italian SME need to find the right partner. In order to achieve this, the company need to build a significant level of trust (*xinren*) for both, direct and intermediary managed deals. *Guanxi* is also important to find the right relationship-connection when it is needed.

Despite the satisfaction of Italian companies about clinched deals, companies are not totally aware of the above mentioned aspects. This incomplete tuning, drives the companies to a narrow exploitation of the potential emerging from the Chinese market. Main success factors are: a right partner (culturally complementary), trust building, flexibility and attention to subtle messages, mutual benefit search.

Principal things to avoid: hit and run strategy, to be aggressive to make the deal, to be impatient to get the goal, to show unclear objectives.

These final considerations suggest to enlarge the research at least to validate the results provided.

In our project we did not explore the intermediary role. Nevertheless, due to the fact that many Italian SME enter the Chinese market with the active role of trustee intermediaries - who play a fundamental task in the negotiation (culturally, operatively and linguistically) - we believe that the exploration of this role is recommended.

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Figure 1: Relevant information of selected interviewed companies

**Companies Profile**

<b>Company</b>	<b>Objective of Chinese site</b>	<b>Management of the deal</b>	<b>Industry Sector</b>	<b>in China since/for</b>	<b>how in China</b>	<b>Number of people today</b>
<b>1</b>	Commercial	Intermediary	Industrial Automation	1987	Agency	3
<b>2</b>	Production	Intermediary	Textile Machinery	30 year with agents, JV since 1992	Hong Kong partner, JV	24
<b>3</b>	Commercial	Intermediary	Textile consultancy & engineering	2000	agents, Agency	0
<b>4</b>	Production	Intermediary	Office Furniture Components	2000	Taiwan partner, JV	70
<b>5</b>	Production	Direct	Tools Equipment for Textile	1993	Local partners for 2 JVs	1500
<b>6</b>	Commercial	Intermediary	Yarn production	2000	Agency in Hong Kong	n/a
<b>7</b>	Production	Intermediary	Brown Household Equipment	n/a	Agency	3000 agents
<b>8</b>	Production	Direct	Cables	1984	local partners for 3 JVs + 1 WOFE	Many people
<b>9</b>	Commercial	Direct	Knitting Machinery	2000	Agency + local JV	n/a
<b>10</b>	Production	Direct	knitting Machinery	1998	local partner JV + Agency	n/a
<b>11</b>	Purchasing	Direct	Motorcycles accessories	1994	Agency today, JV years ago	1

Acronym legend

JV: Joint Venture, WOFE: Wholly Owned Foreign Enterprise,

n/a: not applicable