

## Analysing inter-organizational relationships in the context of their business systems: a conceptual framework for comparative research

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**Analysing Inter-Organizational  
Relationships in the Context of  
Their Business Systems –**  
A Conceptual Framework for  
Comparative Research

Reinhard Bachmann  
Arjen van Witteloostuijn



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# **Analysing Inter-Organizational Relationships in the Context of Their Business Systems –**

A Conceptual Framework for  
Comparative Research

Reinhard Bachmann  
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July 2006

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Founded in 1963 by two prominent Austrians living in exile – the sociologist Paul F. Lazarsfeld and the economist Oskar Morgenstern – with the financial support from the Ford Foundation, the Austrian Federal Ministry of Education, and the City of Vienna, the Institute for Advanced Studies (IHS) is the first institution for postgraduate education and research in economics and the social sciences in Austria. The **Sociological Series** presents research done at the Department of Sociology and aims to share “work in progress” in a timely way before formal publication. As usual, authors bear full responsibility for the content of their contributions.

Das Institut für Höhere Studien (IHS) wurde im Jahr 1963 von zwei prominenten Exilösterreichern – dem Soziologen Paul F. Lazarsfeld und dem Ökonomen Oskar Morgenstern – mit Hilfe der Ford-Stiftung, des Österreichischen Bundesministeriums für Unterricht und der Stadt Wien gegründet und ist somit die erste nachuniversitäre Lehr- und Forschungsstätte für die Sozial- und Wirtschaftswissenschaften in Österreich. Die **Reihe Soziologie** bietet Einblick in die Forschungsarbeit der Abteilung für Soziologie und verfolgt das Ziel, abteilungsinterne Diskussionsbeiträge einer breiteren fachinternen Öffentlichkeit zugänglich zu machen. Die inhaltliche Verantwortung für die veröffentlichten Beiträge liegt bei den Autoren und Autorinnen.

## Abstract

This paper suggests a cross-country comparative framework of inter-organizational relationships and organizational performance. It connects three different bodies of literature, dealing with three different issues: the role of (a) socio-organizational factors in relationships across organizational boundaries; (b) legal contractual arrangements, human capital features, and information and communication technologies as control and coordination mechanisms; and (c) convergence *versus* divergence of cultural and institutional patterns of national business systems. The argument is illustrated by reference to Germany, Great Britain, Ireland and the Netherlands. In so doing, the effects of population size (large for Germany and Great Britain *vis-à-vis* small for Ireland and the Netherlands) and governance regime (Anglo-Saxon in Great Britain and Ireland *vis-à-vis* continental-European in Germany and the Netherlands) are argued to play a central role in determining the nature of inter-organizational relationships.

## Zusammenfassung

Diese Arbeit präsentiert einen theoretischen Bezugsrahmen für die vergleichende Analyse der Qualität von inter-organisationalen Beziehungen. Dabei werden 3 verschiedene Literaturen, die sich mit verschiedenen Fragen beschäftigen, miteinander verknüpft: (a) die Arbeiten, welche die sozio-organisationalen Faktoren untersuchen, die insbesondere für Organisationsgrenzen überschreitende Beziehungen wichtig sind; (b) der Themenkomplex in der Literatur, der die rechtlichen und vertraglichen Vorkehrungen, das verfügbare Humankapital und den Gebrauch von Informations- und Kommunikationstechnologien im Hinblick auf deren Koordinations- und Steuerungsfunktionen in den Blick nimmt; und (c) die Diskussion über die Tendenzen zur Konvergenz und Divergenz von kulturellen und institutionellen Ordnungsmustern in nationalen Wirtschaftssystemen. Der theoretische Bezugsrahmen, den dieser Beitrag entwickelt, wird am Beispiel von Deutschland, Großbritannien, Irland und den Niederlanden illustriert. Dabei wird davon ausgegangen, daß die Größe der Volkswirtschaft und das Regulationsregime (angel-sächsisches *versus* kontinental-europäisches Modell) eine zentrale Rolle in Bezug auf die Qualität der Beziehungen zwischen Unternehmen spielt.

## Keywords

Keywords: national business systems; interorganizational relations; theoretical framework; comparative research

## Schlagwörter

Schlagwörter: nationale Wirtschaftssysteme; interorganisationale Beziehungen; theoretischer Bezugsrahmen; vergleichende Forschung

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# 1 Introduction

More than ever in history, inter-organizational forms of cooperation are characteristic of today's business world. Relationships cut across organizational and industry boundaries, as well as national borders. They form complicated and permanently changing networks with moving centers and peripheries. Not very surprisingly, contemporary management literature mimics this development by increasing the number of concepts and publications devoted to issues of inter-organizational relationships, varying from partner selection and alliance control to network structure and supply chain management (e.g. Jarillo 1988; Ebers 1997; Child and Faulkner 1998; Gulati et al. 2000; Grabher and Powell 2004; Kotabe and Mol 2006).

With regard to the quality of inter-organizational relationships, in terms of such features as their friendliness or trustworthiness, much has been said about the attractiveness of close forms of cooperation between legally independent organizations, providing an alternative possibility to the 'traditional' transaction modes of hierarchical internalization and the market-oriented externalization of business activities (Williamson 1975; 1985). Depending upon the opportunities and threats involved, as well as the costs and benefits of these different options, a firm is supposed to select strategically the 'optimal' transaction mode, which under current conditions of capitalist developments often means that 'hybrid' forms of cooperation are preferred. However, this transaction cost logic does not say much about the characteristics of inter-organizational relationships as such.

Despite the enormous attention that these issues have received, and still do so, in the current debate within organization theory and strategic management, the bulk of existing literature in these fields seems to be too narrowly focused to get a firm grip on the central questions related to the social constitution of business relationships. Studies tend to either look at the micro level of relationships where the role of inter-personally developed forms of trust, risk and power are analyzed (e.g., Mintzberg 1985; Lyons and Mehta 1997; Knights and McCabe 2003), largely bypassing the influence of macro-institutions, or indeed focus on the macro level where national business systems are compared, more or less ignoring the underlying micro-mechanisms on which these systems build (e.g., Hofstede, 1991; Fukuyama 1995; Whitley 1999). In contrast, this paper will present a comprehensive multi-level theoretical framework for analyzing the control, coordination and performance potential of inter-organizational relationships. It will include a variety of factors at the micro, meso and macro levels of business relationships, and it will look at how these might be inter-linked in an integrated framework.

In so doing, the present paper makes an attempt to connect three different literatures in the context of a cross-country comparative framework of inter-organizational relationships and organizational performance: the role of (a) socio-organizational factors in inter-organizational

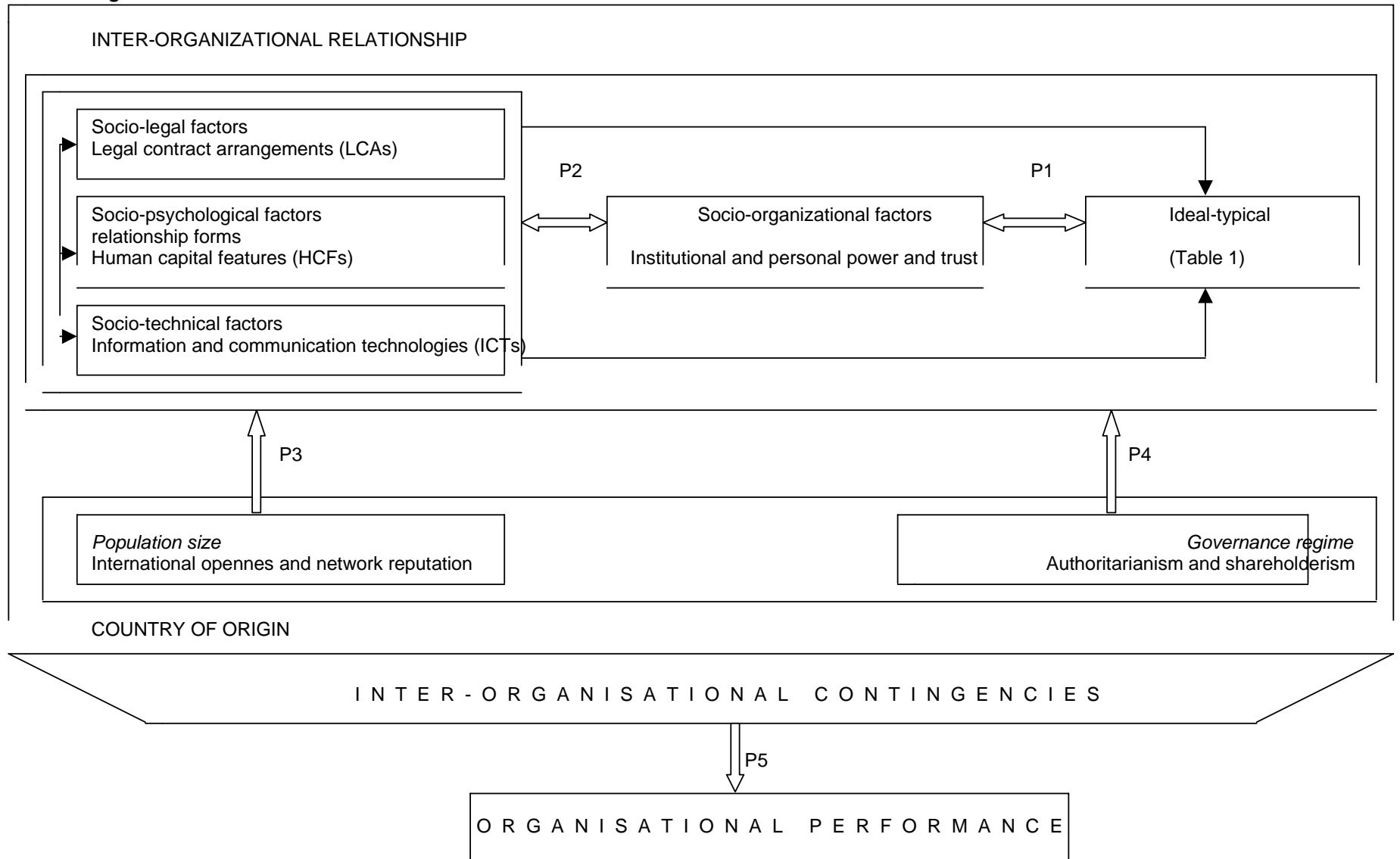
relationships; (b) legal contractual arrangements (LCAs), human capital features (HCFs), and information and communication technologies (ICTs); and (c) convergence *versus* divergence of national business systems (NBSs). These issues will be discussed in the context of a multi-level framework. Moreover, the argument is illustrated by reference to the cases of Germany, Great Britain, Ireland and the Netherlands. The potential effects of population size (large for Germany and Great Britain *vis-à-vis* small for Ireland and the Netherlands) and governance regime (Anglo-Saxon in Great Britain and Ireland *vis-à-vis* continental-European in Germany and the Netherlands) are argued to be crucial factors with regard to the control, coordination and performance of inter-organizational relationships.

The argument is organized as follows. Section 2 will define key elements of our conceptual framework, using a graphical overview of the latter's basic structure. Section 3 will suggest four different 'ideal-typical' inter-organizational relationship types that can be reconstructed against the background of the general framework presented in Section 2. Then, in Section 4, five propositions will be formulated to illustrate the theoretical framework's implications, as well as the underlying premises. Before reaching our conclusions, the theoretical assumptions developed in Sections 2, 3 and 4 will be tentatively illustrated by elaborating upon the cases of the above-named four European NBSs, suggesting hypotheses that may be tested more rigorously in future work. This, together with other issues, is discussed in the concluding Section 5. In advance, we would like to underline the conceptual and exploratory nature of our argument. Given the high complexity of a comparative and multi-level theory of inter-organizational relationships, our propositions are tentative only, whilst our cases serve merely as illustrations. As a first step, though, we believe that this paper's framework offers a promising steppingstone for a comprehensive analysis of the nature of inter-organizational relationships and the NBSs in which they originate.

## 2 An Overarching Framework

An all-encompassing conceptual framework of the control, coordination and performance of inter-organizational relationships must deal with different levels of analysis and with a variety of issues. To organize the argument, our theoretical framework is visualized in Figure 1.

**Figure 1: The theoretical framework**



Below, all key elements of our theoretical multi-level framework are defined and discussed subsequently.

### **Inter-organizational relationships**

As mentioned already, formal and informal inter-organizational linkages have gained increasing prominence across countries and industries in recent decades. Today, vertical cooperation and horizontal alliances of all sorts are more than commonplace in the business world. Here, we define inter-organizational relationships by placing emphasis on three features: inter-organizational relationships are formal arrangements that bring together assets (of whatever kind, tangible and intangible) of two or more legally independent organizations with the aim to produce joint value added (of whatever kind, tangible or intangible). That is, both input and output are formally shared by the independent organizations that are involved in the relationship.

### **Socio-organizational factors**

Different forms of inter-organizational relationships can be distinguished according to the relative dominance of two channels of control and coordination (power and trust), on the one hand, and two sources of power and trust (institutional arrangements and inter-personal contact: see below), on the other hand (Bachmann 2001). Power is the chance that other actors will do what the powerful entity or person wants them to do, even if this is against their free will. Trust is the expectation that other actors will voluntarily reciprocate one-sidedly offered favors, even if this is not done immediately and directly. Both power and trust function as social mechanisms that reduce uncertainty in the external relationships of organizations (Luhmann 1979; Giddens 1990; Bachmann 2001). In so doing, power and trust facilitate transactions between vertically and horizontally cooperating organizations.

### **Socio-legal factors**

In many ways, the contract (explicit or implicit) can be seen as the cornerstone of a relationship between two independent organizations (Deakin and Michie 1997). Contracts differ in what they specify as the duties, responsibilities and expectations of each party in a relationship, and in how detailed the clauses are that are spelled out explicitly or implicitly. Generally, they are necessarily incomplete as they are unable to foresee all possible events that may affect the relationship in the future. Particularly when sophisticated products or services are subject to the transaction, it is not feasible to take provision for all possible developments in the relationship. Thus, the actual practice of using contracts, as well as the relevant country-specific legal codes which a contract inevitably has to refer to, are essential parts of the socio-legal context in which inter-organizational parts of the socio-legal context

in which inter-organizational relationships are embedded (Arrighetti *et al.* 1997; Burchell and Wilkinson 1997).

### **Socio-psychological factors**

Inter-organizational alliances exist because of human beings, and are run by human beings. Thus, we cannot fully understand the control, coordination and performance of a inter-organizational relationship without taking account of so-called human capital features. From the upper echelon or top management literature, we know that the features of those in charge are crucial determinants of an organization's behavior and performance (Boone *et al.* 1996 & 2004). This, *mutatis mutandis*, holds equally true for inter-organizational relationships. The large upper echelon literature has revealed a wide variety of relevant human capital features, including person-based social network assets (Pennings *et al.* 1998). Here, we may distinguish objective characteristics (such as education and tenure) from subjective features (such as personality traits and risk perceptions), which may both be measured at the level of an individual (e.g., an alliance's 'CEO') or a team (e.g., an alliance's top management team). What is particularly interesting in the context of this paper, is that there is abundant evidence that such human capital features are associated with the development of inter-personal (dis)trust (Boone *et al.* 1999; van Witteloostuijn 2003).

### **Socio-technical factors**

Clearly, the distribution of knowledge is crucial in inter-organizational networks. Both the functional features of the technical artifacts that are available for information and communication purposes, and – particularly – the ways of using these systems in the context of the cultural, economic and social environment are elements of the socio-technical arrangements of a given NBS. As we know from the literature on computer-supported cooperative work (CSCW) (e.g., Bannon *et al.* 1996), access to large databases, for example, can be either restricted to a limited number of powerful experts or shared freely within the community of individuals who – in one way or the other – may be affected by decisions that build on the utilization of these data (Schneider and Wagner 1993). Since communication and information are largely technology-based today, the use of ICT plays an essential role with regard to the control, coordination and performance of modern inter-organizational relationships.

### **Organizational performance**

'Good', value-adding, organizational performance is the raison d'être of business organizations. Measuring organizational performance, however, can be difficult when indicators are not defined precisely enough (Buijink and Jegers 1989). After the collapse of

the stock exchange's Internet bubble, example after example emerged in the business press, the record-breaking figureheads being the bankruptcy of the 'virtual' energy trading giant Enron and the creative bookkeeping practice of Worldcom in the US. To avoid too much confusion, we suggest an important distinction between two types of organizational performance measures according to the time horizon of expected returns on (capital) investments. First, there are many accounting-based performance yardsticks that target the short run, such as all kinds of profitability measures (from operating income and shareholder value to ROI and ROS) and size proxies (e.g., aggregate turnover and market share). Second, there are measures that try to capture performance in the long run, popular ones focusing on survival chances and sustainability proxies. For sure, short-term profitability can be high whilst long-run sustainability is low, and *vice versa*.

### Country-specific influences

Country features are likely to influence the control, coordination and performance of inter-organizational relationships. By way of illustration, we focus on two influential country characteristics only. First, the governance regime that prevails in a given NBS (e.g., the continental-European *versus* the Anglo-Saxon business model) is an important element when the social constitution of inter-organizational relationships is to be revealed (e.g., Whitley 1999; Hall and Soskice 2001). While the continental-European approach is based on strong institutions and collectively binding rules of behavior, the Anglo-Saxon system is much more oriented to individualism and situational decision-making. Second, the size of the business system – *i.e.*, its population size – is likely to have a considerable impact upon how these business models are modified. Generally, we assume to find stronger modifications of the ideal-types of the two models in the smaller NBSs, as those are necessarily more open to foreign influences and less inward looking than their large NBS-counterparts.

Referring to our summarising Figure 1, again, our central framework is associated with five propositions (P1 to P5, to be discussed in Section 4). The double-lined arrows in Figure 1 indicate the theoretical propositions that are central to this paper's argument, where a one-way arrow suggests a unidirectional causality and a two-way arrow indicates a reciprocal association. This is not to say that other linkages, such as the single-lined ones in Figure 1, are unimportant. Rather, we focus on a limited set of five propositions that can be backed by current evidence and theory. In an empirical study, linkages such as those reflected in Figure 1's single-line arrows can be investigated in an explorative manner by including an assessment of these associations without adding any *a priori* prediction. Below, the five propositions are introduced explicitly. However, before going into our five propositions, we will first introduce four simplified, ideal-typical inter-organizational relationship forms.

### 3 Inter-Organizational Relationship Forms

Power and trust are two channels of socio-organizational control and coordination in the context of inter-organizational relationships. Depending on the (informal) cultural and – specifically – (formal) institutional environment, there are two distinct sources of power and trust in inter-organizational relationships, where power and trust are inter-related in different ways. First, the source of power and/or trust is located at the inter-personal level, where either power or trust dominates the relationship between two actors. Second, power and/or trust originates with constitutive reference to the formal institutional environment in which relationships are placed. Power, in these circumstances – *i.e.*, impersonal power –, is highly conducive to developing trust in business relations, while the use of personal power makes it less likely that trust will also flourish (Bachmann 2001). Combining both dimensions produces the four potential power-trust patterns, associated with four ideal-typical forms of inter-organizational relationships that are depicted in Table 1.

**Table 1: Four inter-organizational relationship types**

	<b>Institutional power dominance</b>	<b>Personal power dominance</b>
<b>Institutional trust dominance</b>	<i>Pure Form 1</i> Fully institutionalised form (FI-form)	<i>Hybrid Form 1</i> Institutional trust / Personal power (IT/PP-form)
<b>Personal trust dominance</b>	<i>Hybrid Form 2</i> Institutional power / Personal trust (IP/PT-form)	<i>Pure Form 2</i> Fully personalised form (FP-form)

To start with, we can distinguish two ‘pure’ inter-organizational relationship types, where the sources of power and trust are both either predominantly institution-based or person-based.

#### **Fully institutionalised form (FI-form)**

The fully institutionalised form of shaping inter-organizational relationships presupposes a tight and coherent system of institutional arrangements that govern the behavior of social actors (*i.e.*, individual managers and organizations). Here, power and trust arise in inter-organizational relationships because the institutional arrangements of the NBS provide collectively generated and monitored rules of business behavior. In such a system, power is largely anonymous and actors have little chance to opportunistically utilise their individually



available resources of power against the existing powerful order. Power, in other words, is embodied in hierarchical decision-making processes and collectively accepted rules of social inclusion and exclusion. This form of power produces a high level of predictability in individual relationships. Thus, trusting a business partner implies low risk and will, therefore, occur frequently under these circumstances. In many situations, institutional power and institutional trust will be difficult to disentangle. Both of these social coordination mechanisms tend to be amalgamated in a strong form of institutional control of individual actors' business behavior.

### **Fully personalised form (FP-form)**

Alternatively, power and trust can emerge at the inter-personal level – *i.e.*, without constitutive reference to the institutional framework of the NBS. Especially where strong and reliable institutions and generalised rules of behavior do not exist, individual managers and organizations need to base their decisions on individually mobilizable resources of power and/or trust. In these circumstances, power and trust remain two different channels of social control. Also in this case, both mechanisms can occur in combinations, but here it makes a very important difference whether power or trust dominates the relationship. Each option implies specific chances of saving on transaction costs, increasing flexibility and fostering the innovativeness of the involved parties. Generally, the inherent risk of trust is high under these conditions, implying that the powerful party will tend to draw on his or her individual resources of power in many situations.

In addition to both 'pure' ideal-typical forms, hybrid types of inter-organizational relationships may perhaps theoretically not seem very likely to emerge, but do occur where the macro-institutional inventory of a given NBS is not (fully) congruent with the micro-cultural traditions. Two different forms of incongruence are important to discern.

### **Institutional trust / Personal power form (IT/PP-form)**

The first hybrid form occurs where a relatively strong institutional trust-promoting NBS-framework is in place, but where at the same time the micro-cultural foundations of business behavior encourage individualistic strategies and risk-taking conduct. In such a context, institution-based trust goes hand in hand with person-based power. This implies, on the one hand, that trust development is backed by institutional arrangements, both formal (*e.g.*, contract law) and informal (*e.g.*, high-trust societal culture) in nature, so that inter-organizational relationships can be based upon common trust-promoting knowledge. Power, on the other hand, must be developed and sustained with reference to personal authority, whilst collective ('non-personal') rules of conduct are absent. How the mixture of institutional trust and personal power works out in practice is largely an empirical question.

### **Institutional power / Personal trust form (IP/PT-form)**

The second hybrid form emerges where strong forms of power-promoting institutions are characteristic of the NBS, whilst the micro-cultural order builds strongly on an ethics of cooperation and collective problem-solving. Then, institutional power operates next to personal trust. Thus, on the one hand, inter-organizational relationships cannot benefit from trust-generating institutions, implying a lack of macro-level safeguards against opportunistic behavior, which implies that actors largely have to develop trust at the micro inter-personal level. On the other hand, power is embedded in an institutionalised context of hierarchy-supporting cultures and rules, so that people do have the chance to fall back on generalised codes of power-related behavior. Again, the empirical consequences of this power-trust pattern can imply tensions or beneficial conditions for inter-organizational relations.

All four ideal-typical forms may involve specific advantages and disadvantages. In terms of power and trust, these forms can either have a tendency towards the high-trust system or the low-trust system. This also depends on whether the overall coordination of the whole NBS is more strongly based on micro-cultural routines or on macro-institutional arrangements in the context of developing power and trust in inter-organizational relationships, and how the different forces balance out.

## **4 Five Propositions**

Our general framework for analysing inter-organizational relationships generates opportunities to explore systematically the theoretical predictions that emerge when the different conceptual building blocks are combined. In this paper, by way of illustration, we suggest and discuss five propositions, along the arrows depicted in Figure 1 (P1 to P5). The first proposition simply summarises the argument outlined above as to the four ideal-typical forms of inter-organizational relationships.

### **Proposition 1 (power and trust in inter-organizational relationships)**

Two channels of socio-organizational control and coordination – power and trust (dimension 1) –, as well as the two different sources of power and trust – institution-based or person-based (dimension 2) –, work together to produce four different power-trust combinations that are associated with four different ideal-typical forms of inter-organizational relationships.

**Table 2: Ideal-typical forms, and LCAs, HCFs and ICTs**

<b>Ideal-typical forms</b>	<b>LCAs</b> Legal contract arrangements	<b>HCFs</b> Human capital features	<b>ICTs</b> Information and communication technologies
FI-form Fully institutionalised 'pure' form	Detailed contracts, following standardised guidelines, signal macro-level high trust <i>ex ante</i>	Top managers make much use of formal hierarchical power	Strict macro-level privacy rules dictate what can and what cannot be communicated electronically
FP-form Fully personalised 'pure' form	Detailed tailor-made contracts offer devices to punish opportunistic behavior in court <i>ex post</i>	Top managers must develop person-based authority	What is and what is not communicated electronically is established in micro-level inter-personal relationships
IT/PP-form Institutional trust / Personal power hybrid form	Detailed contracts, following standardised guidelines, signal macro-level high trust <i>ex ante</i>	Top managers must develop person-based authority	Strict macro-level privacy rules dictate what can and what cannot be communicated electronically
IP/PT-form Institutional power / Personal trust hybrid form	Detailed tailor-made contracts offer devices to punish opportunistic behavior in court <i>ex post</i>	Top managers make much use of formal hierarchical power	What is and what is not communicated electronically is established in micro-level inter-personal relationships

**Proposition 2 (socio-legal, socio-psychological and socio-technical factors)**

The socio-legal (*i.e.*, the practice of using LCAs), socio-psychological (*i.e.*, the psychological HCFs of top managers) and socio-technical (*i.e.*, the ways in which ICTs are used in inter-organizational relationships) factors are key variables in determining the role and relative importance of power and trust in controlling and coordinating activities in inter-organizational relationships. Their role and relative importance depends upon the specifics of the relevant cultural and institutional contexts. Table 2 links, tentatively, our four ideal-typical forms with illustrative examples of the influences that LCAs, HCFs and ICTs may have on inter-organizational relationships.

The way in which these variables are reflected in concrete individual relationships among organizations, is both a result and a condition of how power and trust do their jobs as social mechanisms of controlling and coordinating expectations and interactions across individuals and organizations.

**Proposition 3 (influence of population size)**

Larger countries are associated with culturally-embedded rules of conduct and institutionalised NBSs that offer path-dependent routines as to how to use power and trust (and LCAs, HCFs and ICTs) in controlling and coordinating inter-organizational relationships. Hybrid forms of power and trust, though, are easier to establish and further developed in smaller countries. Smaller countries, in contrast to their larger counterparts, are an ideal seedbed for medium-range forms of power and trust in the context of inter-organizational relationships. On the one hand, the relative importance of networking activities and social reputation, which are a consequence of these countries' small size, offer ample opportunities to develop tailor-made arrangements. On the other hand, hybrid forms of social control result from the greater openness to foreign influences that is characteristic for smaller countries, implying that elements from foreign 'pure' systems are mixed to create new forms of inter-organizational relations.

**Proposition 4 (influence of governance regime)**

Countries may be associated with institutionalised governance systems that suggest how power and trust (and LCAs, HCFs and ICTs) are supposed to be shaped and worked out in inter-organizational relationships. For the purpose of the current paper, we concentrate on the likely impact of two features: high *versus* low 'hierarchical rigidity' and high *versus* low 'shareholderism'. First, as Hofstede (1991) has pointed out time and again, countries differ widely with respect to 'power distance'. That is, societal cultures may or may not imprint people with a clear sense of hierarchy. Clearly, countries that score high on hierarchical

rigidity (e.g., France) are characterised by institutionalised power, whereas their counterparts (e.g., the US) feature personalised power. Second, we distinguish Anglo-Saxon shareholder governance regimes (high shareholderism) from continental-European stakeholder systems (low shareholderism), as widely discussed in the literature (Gordon 1996). Here, we expect that low shareholderism goes hand in hand with high-trust institutions, whereas the opposite holds true for high shareholderism. That is, in Anglo-Saxon countries, such as the Great Britain, the relationship between different parties in the business system, particularly ‘capital’ (i.e., employers) and ‘labour’ (i.e., employees), is based upon conflict, rather than cooperation, whereas the reverse holds true in continental-European countries, such as Germany. This is reflected, for instance, in the ways in which labour law and decision-making participation are shaped (Hall and Soskice 2001).

Finally, Proposition 5 brings together the four Propositions 1 to 4 above in an overall contingency-type of performance argument (cf. Figure 1), along the lines of contingency theory’s multi-fit concept (Heijltjes and van Witteloostuijn 2003).

#### **Proposition 5 (contingencies for organizational performance)**

The short and long-run performance of a inter-organizational relationship is enhanced if the different pieces of the contingency puzzle (i.e., ideal-typical form, LCAs, HCFs, ICTs, population size and governance regime) complement one another and produce a perfect fit, so that the inter-organizational relationship’s internal features (cf. Propositions 1 and 2) are aligned with the environmental characteristics (cf. Propositions 3 and 4).

Proposition 5 implies that we can expect that specific ideal-typical forms of inter-organizational relationships (a) perform better and (b) are found more in country environments with ‘fitting’ features, either as a result of adaptation by local organizations or as a consequence of domestic selection processes. This idea is explored in greater detail in Section 5.

## **5 Countries**

By way of illustration, we apply the above argument to four countries that differ markedly along the two country features that we have explored in the theoretical part of this paper: population size (Proposition 3) and governance regime (Proposition 4). The central difference between the smaller countries of Ireland and the Netherlands builds on their orientations towards two divergent business models, which are more purely represented in the larger business systems of Germany (continental-European model) and Great Britain (Anglo-Saxon model). In the Netherlands, network-based relationships are a means to make rigid institutional arrangements more flexible than this is the case in Germany, while in

Ireland hybrid relationships are a means to produce more stability within the business system as compared to Great Britain. Given these broad differences, the question is how inter-organizational relationships are likely to be shaped in this set of four countries. Here, the underlying idea is that high-performance types of inter-organizational relationships, and the associated LCAs, HCFs and ICTs, are adopted and selected as a result of organization-level learning and environment-level selection processes, respectively, as extensively argued in ecological (Hannan & Freeman 1977) and institutional (DiMaggio and Powell 1983) theories of organizational fields or populations. Our overall predictions are summarised in Table 3.

**Table 3: Governance regime and inter-organizational form**

	<b>Low authoritarianism</b> (low power)	<b>High authoritarianism</b> (high power)
<b>Low shareholderism</b> (high trust)	Hybrid IT/PP-form (The Netherlands)	Fully institutionalised form (Germany)
<b>High shareholderism</b> (low trust)	Fully personalised form (Great Britain)	Hybrid IP/PT-form (Ireland)

### **Germany: The Institutionalised System**

The German business system is characterised by a strong and coherent institutional framework (Lane 1995). In these circumstances, power as well as trust will predominantly appear in their institutional forms. Power and trust, in other words, are mechanisms which emerge in business relations because highly generalised rules of behavior and abstract patterns of social regulation effectively govern organizational relations. At the level of individual interaction that means, for instance, that the power that a purchasing manager of a buyer firm may have over a sales manager of a supplier firm, has very little to do with her or his individual skills of communication or personal obligations that might result from previous interactions between the two parties. Rather, the power he or she may be able to exert on a business partner depends on impersonal factors such as market position, size and reputation of her or his organization, technical standards or legal and social norms of business behavior which he or she refers to in his or her business behavior.

The latter sources of power, by the same token, are prime sources of trust in inter-organizational relationships in this system (Lane and Bachmann 1996). This means that the sales manager of the supplier firm can also develop trust to the purchasing manager of a

large and powerful firm because he or she can rely on the fact that the rules of the interaction are not based on the other party's opportunistic and idiosyncratic motives. Both parties' behavior is controlled by generalised and abstract rules embodied in anonymous social structures that channel their mutual expectations and provide stable patterns of inter-organizational interaction. The use of legal contracts and the ways in which information flows between business partners are organised by means of ICT, for instance, produce highly predictable patterns of behavior. Standardised contracts and the reliable routines of ICT-based exchanges of knowledge reduce risk and can be taken as good reasons to invest trust in a business relationship and to acknowledge power (*i.e.*, institution-based power), which an individual can hardly utilise in order to simply maximise her or his own individual profit. As far as the recruitment of top managers is concerned, much depends upon the formal criteria (*i.e.*, documented educational background) whilst idiosyncratic talents seem to be less important (Stewart *et al.* 1994).

### **Great Britain: The Atomised System**

In Great Britain, generalised rules of business behavior exist only in rudimentary form. The institutional framework of this business system is patchy, and can neither be deemed a reliable source of trust nor can it be described as powerful or influential with regard to the behavior of individual managers. Thus, the coordination of expectations and interactions between, for instance, a purchasing manager of a buyer firm and a sales manager of a supplier firm has to draw on sources of power and trust that are rooted in inter-personal contact rather than in institutional arrangements (Lane and Bachmann 1996). This means that the predominant form of trust is personal trust, while the power that may become relevant for individual relationships between managers is primarily based on individually attributable resources such as communication skills and personal obligations.

This implies that individuals – at least the powerful ones – have a choice between whether they want to base their relationships more on power or more on trust. Here, personal power and personal trust tend to appear as alternative ways of coordinating expectations and interactions between business partners. The use of legal contracts and the organization of information flows across organizational boundaries is often dominated by opportunistic motives, rather than controlled by generalised and collectively binding rules. The relative absence of collectively accepted norms and standards of business behavior is mirrored in legal practice, and in the way in which ICT is used. In this business system, powerful actors lead a comfortable life, whilst less powerful managers and organizations are often forced to 'trust' their business partner and thus to accept very high risk in their external relationships. Who does and who does not emerge as a powerful organization or *ditto* manager, largely depends upon the subjective leadership-related set of characteristics of individuals.

## **The Netherlands: The Top-Down Network**

In general, the Dutch business system is historically oriented to the fully institutionalised model (Hartog 1999; den Butter and Mosch 2001; Spithoven 2002). The fact that the country is much smaller than Germany, however, allows for considerably more flexibility in business relationships. Institutions may play an important role and provide an overall framework of business behavior. At the same time, however, many informal arrangements are possible because managers often know each other personally and frequent face-to-face contacts are easy to arrange where geographical distances are short. Under these conditions, power and trust are not solely channelled through generalised rules of business behavior and abstract structures, as this tends to be the case in the German system. The institutional framework of the Dutch system may well be seen as a prime source of power and trust, but it is characteristic of this system that both mechanisms of coordinating expectations and interactions are substantially supplemented by forms of power and trust that are based on networking and reputation. It is not so much personal power and personal trust – which is typical for the atomised system (Great Britain) –, but a medium-range form of power and trust production that plays an important role in the Dutch system.

Within the framework of institutional arrangements, in other words, social networking and social reputation are very important mechanisms with regard to the nature, quality and dynamics of business relations. Legal contracts are not used opportunistically, but as such they are no guarantee for efficient relations. The social embeddedness of the contractual arrangements plays a crucial role in the interpretation and application of standardised contract clauses. In a similar vein, there are standard norms of using ICT on which individuals can fall back. An adequate understanding of the practice of using these systems, however, requires an analysis that makes them visible as means to control information flows within networks in which social reputation works as an effective entry barrier and ‘third-party guarantors’ act as boundary spanners with regard to the external relations of the network. Similarly, the selection of top managers is the result of a betwixt-and-between mixture of formal characteristics screening and informal networking processes.

## **Ireland: The Bottom-Up Network**

The Irish system, at first glance, seems a little bit difficult to assess because a huge proportion of this countries’ economy is in the hands of foreign-owned enterprises. In the late 1990s, for example, more than two thirds of the manufacturing net output is accounted for by non-Irish investments (Ruane and Gorg 1997). This, clearly, brings a number of unusually heavy foreign influences into the Irish business system. However, looking at the Irish system as a whole, with special emphasis on its historical traditions, there cannot be much doubt that Ireland clearly follows the model of the ‘liberal market economy’ (Hall and Soskice 2001). This system can hardly be understood without major references to the British

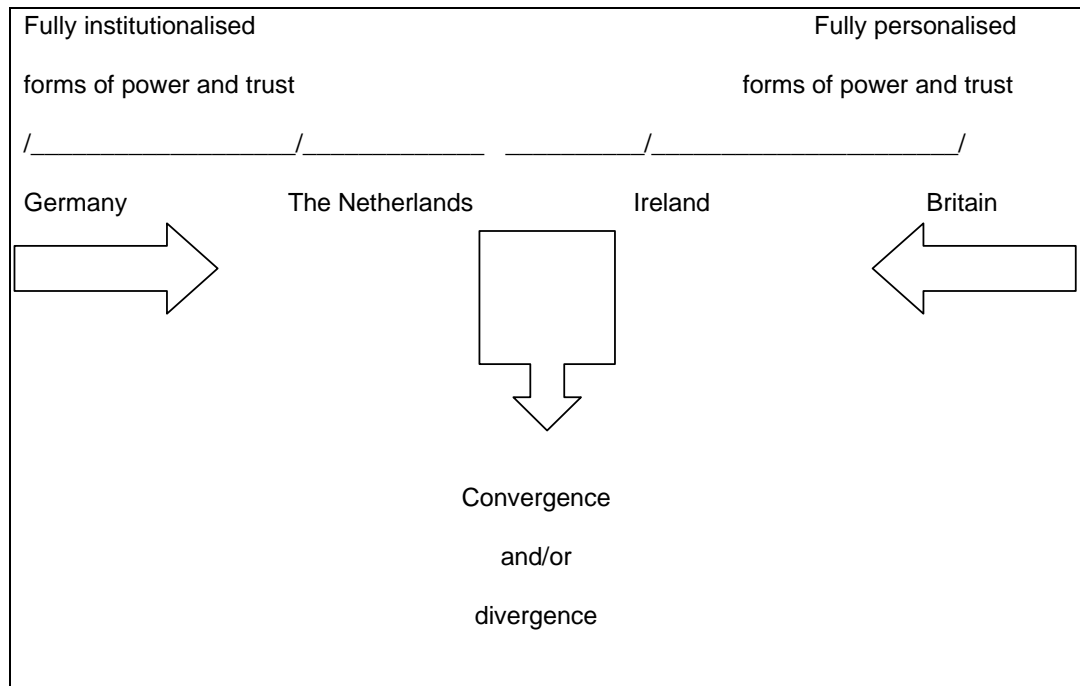


business system, although the desire to distance itself from the British heritage has been strong in Ireland after the country's partition in 1921 (Roper 2000). Irish business relationships do, generally, not build on strong institutional arrangements and collectively binding rules of behavior as this is the case, for example, in Germany. At the same time, especially the size of the country also produces important differences compared to the British business system. Similar to the Netherlands, social reputation is crucial. But the Irish system generates these medium-range forms of power and trust not within a given system of institutional regulation. Rather, inter-organizational networks are built on the basis of and as an important supplement to personal forms of power and trust. Networking is not a means to make the rigid patterns of the institutional order more flexible. Rather, it is a means to produce more stability within the system.

When the use of legal contracts and the practices of using ICT are under review, it appears that there exists room for the opportunistic use of individual resources of power. Due to the size of the system, however, there is very little chance that this could pay off. In a small business community like Ireland, this would have immediate and disastrous effects on the reputation of the individual manager who considers such behavior, as well as on the reputation of the organization he or she represents. Social networking, similar to the Netherlands, is an important feature of the Irish system. But, contrary to the Dutch system, inter-organizational networks are based on routinization effects in inter-personal relationships rather than on the idea of making a highly institutionalised system more flexible. This implies that, by the end of the day, both 'objective' leadership and 'subjective' networking enter into the selection procedure of top managers.

By way of summary, Figure 2 locates the four countries discussed above on a continuum that runs from fully institutionalised forms of power and trust to their fully personalised counterparts.

From the arguments above, we can formulate concrete predictions as to how inter-organizational relationships are shaped in these four countries, depending upon their location on this continuum (Propositions 1 and 4). As far as performance is concerned (Proposition 5), we hypothesise that those inter-organizational relationship types that fit nicely with the macro-environment in which they operate, outperform their counterparts that have adopted 'mis-fitting' elements. For example, we think that it is unlikely that the FP-form alliance is very viable in Germany, whilst the FI-form relationship is probably ineffective in Great Britain.

**Figure 2: A country continuum of inter-organizational relationship types**

## 6 Conclusion

The specific forms of power and trust (as well as their specific combinations) that prevail in different institutional environments will, according to the argument outlined in this paper, produce very specific performance consequences, suggesting cross-country divergence. Not only are inter-organizational relationships likely to be shaped according to the rules that dominate the environment in which they occur, but also are non-fitting inter-organizational relationship types selected out on the basis of country-specific path dependencies (Sorge 2005). However, there are also arguments that suggest a tendency toward international convergence. For one, the neo-liberal 'revolution' is spreading across the world, particularly after the breakdown of the Berlin Wall, implying a convergence of NBSs toward the Anglo-Saxon model (Gordon 1996). Under these conditions, it may be argued, inter-organizational relationships across the globe reveal a tendency to develop towards the FP-form. Additionally, however, inter-national networks of firms are becoming more and more important in a globalising business world, prominent examples being the impressive network formation in many knowledge-intensive industries. Against this background, new network forms of power and trust emerge that must mix the cultural and institutional flavours of partners from different countries. This is likely to produce hybrid inter-organizational

relationship forms such as the IP/PT and IT/PP-types that include elements of both inter-personal arrangements and institutional regulation. In other words, the hybrid 'third-party guarantor', who acts as a broker/mediator of information, power and trust in a given network, plays an increasingly important role under conditions of internationalised business (van Ees and Bachmann 2006).

If this argument holds true, then hybrid forms of power and trust are associated with a competitive advantage against the background of the current dialectic processes of globalisation and regionalisation of markets and strategies (Sorge 2005). In particular in the knowledge-intensive services sector, for instance, the German system will thus have incentives to move towards the Dutch example and British managers will find the Irish benchmark attractive. This would imply that the perfectly 'fitting' hybrid forms of power and trust as developed in such countries as Ireland and the Netherlands, being associated with specific *betwixt-and-between* socio-legal, socio-psychological and socio-technical features (reflected in the ways in which legal contracts and technical artefacts are used, as well as in the processes of selecting top managers), produce superior performance and greater innovativeness in the medium-term future of business in Europe, compared to their 'pure' counterparts from such countries as Germany and Great Britain. Of course, whether we are in the middle of processes of convergence or divergence (and what is the direction of this development), is still an open question. What is high on our research agenda, therefore, is to study these and related issues thoroughly from the comparative and multi-level perspective introduced above, taking the propositions developed here as our point of departure.

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