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# THE ROLE OF MANAGERS' POLITICAL NETWORKING AND FUNCTIONAL EXPERIENCE IN NEW VENTURE PERFORMANCE: EVIDENCE FROM CHINA'S TRANSITION ECONOMY

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*Drawing upon the resource-based view and transaction cost economics, this study aims to examine how various types of managerial resources (i.e., political networking and functional experience) can be beneficial to new ventures in a transition economy. Using survey data from a sample of new ventures in China's high-technology industries, we demonstrate that managers' political networking and functional experience are positively related to new venture performance. We also find that the positive relationship between functional experience and new venture performance is moderated by the type of ownership of the ventures and the level of dysfunctional competition in their environments. Theoretical and managerial implications are discussed.* Copyright © 2007 John Wiley & Sons, Ltd.

It has long been argued that new ventures experience liabilities from their newness and have a high failure rate, because they often have limited resources and their stable links to clients, supporters, and customers have not yet been established (Stinchcombe, 1965). The literature suggests that top managers play an important role in new venture success (e.g., Eisenhardt and Schoonhoven, 1990; Keeley and Roure, 1990; McGee, Dowling, and Megginson, 1995). Managers can generally offer two types of resources: human capital as indicated by their experience (Eisenhardt and Schoonhoven, 1990; McGee *et al*., 1995) and social capital as indicated by their external ties (Granovetter, 1985; Shane and Cable, 2002). These managerial resources can enable new ventures to leverage and exploit other types of resources, to develop competitive advantage, and to achieve better performance (Barney, 1991).

Previous studies in this area are mainly limited to new ventures operating in Western developed markets with relatively stable institutional environments. Yet little is known about how managerial resources are related to new venture performance in transition economies that are experiencing significant institutional changes in moving from central planning to market competition. While several scholars have demonstrated the importance of managerial ties in transition economies (e.g., Peng and Luo, 2000; Xin and Pearce, 1996), this line of research has mainly focused on firms in general rather than specifically examined new ventures. In addition, no study has examined the roles of managerial ties and experience simultaneously. This narrow focus limits theoretical completeness and is a significant gap in the literature. Since the market mechanism (i.e., the allocation of resources mainly by market forces) and the redistributive mechanism (i.e., allocation mainly by governmental agencies) coexist in transition economies (Nee, 1989; Zhou,

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2000), new ventures need to have different types of managerial resources to deal with the redistributive power and the market forces, respectively, for better performance.

More importantly, the link between managerial resources and new venture performance is not universal but rather could be context specific. Prior research has noted that transition economies represent an institutional context characterized by a lack of well-established legal frameworks to define property rights (Choi, Lee, and Kim, 1999; Hoskisson *et al*., 2000; Li and Atuahene-Gima, 2002). The lack of strong legal frameworks has allowed widespread opportunistic behaviors and has affected the ability to enforce property rights even where legislation has been enacted (Hoskisson *et al*., 2000). Thus the institutional characteristics of transition economies can influence the roles of managerial resources in new venture performance. So far, however, little theoretical or empirical work has addressed this issue.

In this study, we aim to address the above gaps in the literature by examining the roles of managers' political networking (as their social capital) and functional experience (as their human capital) in new ventures in China's high-technology industries. We define political networking as the extent to which managers cultivate relationships with government officials (cf. Li and Atuahene-Gima, 2001). Previous studies have suggested that such ties can substitute for the insufficient formal infrastructure in a transition economy (Xin and Pearce, 1996) and thus may help new ventures to deal with the redistributive power. We define functional experience as managers' working experience in various functional areas, including sales/marketing, R&D/engineering, manufacturing, finance, and administration. We focus on functional experience because prior new venture research has argued that 'management's functional expertise often dictates an organization's primary distinctive competence' (McGee *et al*., 1995: 567). Because of increasing privatization and liberalization in a transition economy, managers' functional experience can enable new ventures to build their competitive advantages in market competition. Specifically, we will address two research questions: (1) How are managerial resources related to new venture performance in China's transition economy? (2) How do institutional contexts (i.e., the ownership of the ventures and the level of dysfunctional competition in their environments) moderate the links between managerial resources and new venture performance? Based upon the transaction cost economics (Williamson, 1985), we argue that managers' political networking will have a stronger relationship with new venture performance when the institutional support is weak than when it is strong. This is consistent with the argument that managerial ties can substitute for insufficient institutional infrastructure (Xin and Pearce, 1996). Based upon Teece's (1986) argument of the appropriability of rents, we argue that managers' functional experience will have a stronger relationship with new venture performance if the institutional contexts allow the ventures to retain the rents generated by their managers' functional experience.

Our study will have significant practical and theoretical importance. Practically, findings of this research will allow us to better understand how different types of managerial resources are beneficial to new ventures in transition economies. Theoretically, our study can provide evidence on how institutional contexts influence the values of resources and thus contribute to our knowledge of the boundary of the well-established resource-based view (Priem and Butler, 2001). Also, this study responds to the recent notion by several scholars that international entrepreneurship literature has not yet paid much attention to how institutional factors influence entrepreneurship processes (Baker, Gedajlovic, and Lubatkin, 2005; Oviatt and McDougall, 1994). The remainder of this paper is organized as follows: First, we develop our theory and research hypotheses; next, we describe our methods to test these hypotheses; finally, we present the results of the study and discuss their implications.

## THEORY AND HYPOTHESES

### Managerial resources and new venture performance

*Managers' political networking*

Previous studies on firms in transition economies have emphasized the importance of managerial ties (*guanxi* in Chinese) in firm success. In transition economies in which the formal institutional framework has not been well developed, it appears that who you know is all that counts. For example, Xin and Pearce (1996) argued that in China *guanxi* can



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substitute for the insufficient formal infrastructure. Luo (2003) noted that ties provide flexible resource allocation in an environment where factor mobility is severely constrained and governmental interference remains a factor. In addition, institutional underdevelopment in a transition economy creates an uncertain and risky business environment that lowers trust among people (Atuahene-Gima and Li, 2002: 65). As a result, information passed through external ties 'may be more trustworthy, richer, and more useful than information gained by other means' (Luo, 2003: 1317). This is particularly the case when we consider China's unique culture, which emphasizes collectivism rather than individualism. Individuals are evaluated on the basis not only of their own competence and contributions but also those of other people who are related to them. Ties or *guanxi* based on family, relatives, hometown connections, schoolmates, or even colleagues are all-important in Chinese society (Chen, Chen, and Xin, 2004). Indeed, close *guanxi* can be classified as family-like in China (Hwang, 1987).

Managers' ties with government officials—i.e., their political networking—represent a unique type of managerial resource in China's transition economy (Li and Atuahene-Gima, 2001). Because the government still controls significant portions of strategic factor resources and has considerable power to approve projects and allocate resources, managers tend to maintain a 'disproportionately greater contact' with government officials (Child, 1994: 154). Empirically, Nee (1992) found that managers' networking with local officials leads to better performance of new ventures in China. Peng and Luo (2000) showed that managerial ties with government officials are positively related to firm performance in China. High-technology industries as examined in this study are taken as strategically important industries in China. The government has provided strong support in terms of financing, information, and technology for firms in these industries through institutional devices and regulatory regimes (Li and Atuahene-Gima, 2002; Lu, 2000). Given the government's important role in developing and supporting these industries, new ventures with extensive networking with government officials can rely on such networking to obtain information and funding, which can contribute to their performance (Li and Atuahene-Gima, 2001). Therefore, we propose the following hypothesis:

*Hypothesis 1: Managers' political networking will be positively related to new venture performance in a transition economy.*

### *Managers' functional experience*

It should be recognized that economic transition introduces fundamental changes in 'the formal and informal rules of the game that affect organizations as players' (Peng, 2003: 275). With the development and institutionalization of markets, factors other than managerial ties or *guanxi*, such as managers' expertise, also become crucial. Indeed, new venture research in market economies has long highlighted the importance of managers' expertise as reflected in their experience (e.g., Eisenhardt and Schoonhoven, 1990; Keeley and Roure, 1990). Since experience is a prime source of learning (i.e., learning by doing), managers' experience in various functional areas leads to expertise and skills in these areas. In addition, managers' experience in certain areas can further facilitate their learning and development of related expertise and skills in the future. In the context of new ventures, managers' functional experience enables the ventures to more efficiently and effectively develop, produce, and market new technologies and products. Their functional experience can also be used by investors and other actors, on whom the success of new ventures depends, to evaluate the potential of the ventures. For example, Keeley and Roure (1990) found that managers' functional experience is positively associated with new venture growth.

Firms in transition economies, such as China, have long been constrained by the legacy of Marxist ideology implemented through central economic planning. With this legacy, managers historically were selected for their positions primarily because of their political loyalty rather than for their experience. As Peng and Heath (1996: 509) noted, 'decades of operations under the rigid central planning system have made managers at these firms become agents of the government, whose primary function was to take orders from the top ... they are simply not equipped to work in the context of markets because of their lack of knowledge, skills, and experience in such an environment....' However, privatization and enhanced market competition resulting from economic transition have created the need for managerial expertise (Child and Markoczy, 1993). Indeed,



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successfully managing new ventures in a transition economy requires managers to have experience in many areas. For example, as their ventures explore new market opportunities, they need marketing experience to be able to understand the markets and satisfy customer needs. Also, managers need financial experience in order to fund their entrepreneurial activities from sources other than the government. Therefore, we propose the following hypothesis:

*Hypothesis 2: Managers' functional experience will be positively related to new venture performance in a transition economy.*

## The contingency values of managerial resources

It should be noted that managers' political networking and functional experience are embedded in institutional contexts and may not have the same values for all new ventures. A hallmark of transition economies is the coexistence of state-owned and non-state-owned firms, which differ in their behaviors and performance (Peng and Luo, 2000). In addition, dysfunctional competition represents an important environmental dimension in a transition economy. It specifically refers to the extent to which the competition in a firm's environment is opportunistic, unfair, or even unlawful (cf. Li and Atuahene-Gima, 2001). In the following sections, we will examine how these institutional contexts moderate the roles of political networking and functional experience in new venture performance, respectively.

### *The contingency value of political networking*

As noted earlier, managers' political networking is important to new venture performance in a transition economy because it can substitute for the insufficient formal infrastructure (Xin and Pearce, 1996). Accordingly, we would expect that managers' political networking should be more important when the institutional support for a new venture is weak than when it is strong. This argument is consistent with transaction cost economics (Williamson, 1985), which suggests that an important feature of hierarchical controls is their ability to manage potential moral hazards. Thus, hierarchical controls will become more important when firms are concerned about the problem of moral hazards.

Because ties such as political networking can be very close in China (Hwang, 1987), political networking can transform the relations between new venture managers and their networked government officials into semi-hierarchical relations. Thus, according to transaction cost economics, managers' political networking should be particularly important to new venture performance when the institutional support is weak and moral hazards (e.g., violation of property rights and contract breaking) are a major concern. Under such conditions, extensive political networking can represent a substitute for the legal system and law enforcement. In contrast, when the institutional support is strong, moral hazards become less of a concern, and accordingly political networking may be less important. Based upon these arguments, we will examine below how ownership and dysfunctional competition can moderate the relationship between managers' political networking and new venture performance.

*Ownership.* Compared with non-state-owned ventures, state-owned ventures are founded by the government or its agencies, and their top managers are typically appointed by the government. As a result, these ventures naturally have legitimacy and receive support or even protection from the government agencies that have founded them. In contrast, non-state-owned ventures receive little support from the government and lack market legitimacy, thus they are in a relatively weak position in the institutional environment (Nee, 1992). For example, it has been reported that of the U.S. $38 billion in loans to firms granted by state banks in China in 1998, only 5 percent were to non-governmental firms (*China Economic News*, 2000).

Because of the weak institutional position of non-state-owned ventures in a transition economy, moral hazards become a major concern to them. For example, if their property rights are violated and/or their business partners break contacts with them, they may not get sufficient protection from the existing institutional framework. As a result, political networking is crucial for non-state-owned ventures as a substitute for insufficient formal institutional support. These firms can influence government officials to bring the officials' interests in line with their own (Peng, 2003). Hence, their ties with government officials may protect them



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from moral hazards even if the existing legal system cannot.

In comparison, because state-owned ventures already have relatively strong institutional support in a transition economy, political networking becomes less important to protect them from moral hazards. It is possible, of course, that managers in state-owned ventures may spend more time and money in networking with government officials than those in non-state-owned ventures because they are beholden to government officials and need to spend a great deal of effort trying to influence these officials. However, we argue that while political networking may help secure the careers of managers in state-owned ventures, its contribution to venture performance should be smaller than that in non-state-owned ventures for the reasons noted earlier. Empirically, Peng and Luo (2000) found that managerial ties with government officials are positively related to firm performance for non-state-owned firms but not for state-owned firms. Therefore, in the new venture context, we propose the following hypothesis:

> *Hypothesis 3: The positive relationship between political networking and new venture performance will be stronger in non-state-owned ventures than in state-owned ventures in a transition economy.*

*Dysfunctional competition.* In transition economies, formal market institutions have not been well developed to govern market transactions and define and protect property rights (Peng and Heath, 1996). It is not unusual for firms to engage in widespread opportunistic and unlawful behaviors (Li and Atuahene-Gima, 2001). Patent and copyright violations, broken contracts and agreements, and unfair competitive practices have become widespread. We argue that managers' political networking will have a stronger relationship with new venture performance when the level of dysfunctional competition is high than when it is low. When the market competition is highly dysfunctional, intellectual property rights may go unprotected, and it may be difficult to monitor and enforce business contracts, which will increase new ventures' concerns about moral hazards in their business environments. Under such conditions, political networking can circumvent the lack of property rights and become a substitute for law enforcement and the legal system. It thus can reduce the risk and uncertainty of new ventures' business environments and facilitate their economic exchanges. In addition, under such conditions, new ventures may even use their managers' political networking to take advantage of the dysfunctional competition in the environment. For example, they may win contracts and business licenses via political networking even though their technologies and products are no better than those of the rivals.

In contrast, when the level of dysfunctional competition is low, the importance of political networking in both reducing risk and winning businesses will be reduced. Our above arguments are consistent with Peng and Luo's (2000: 486) notion that 'social capital embedded in managerial ties may be more important in imperfect competition characterized by weak institutional support and distorted information.' Therefore, we propose the following hypothesis:

> *Hypothesis 4: The positive relationship between political networking and new venture performance will be stronger when the level of dysfunctional competition is high than when it is low in a transition economy.*

### *The contingency value of functional experience*

As noted earlier, with the development and institutionalization of the markets, managers' functional experience becomes important in transition economies. However, the extent to which managers' functional experience can be transformed into new venture performance depends upon the strength of the appropriability regime of their institutional contexts. According to Teece (1986), appropriability refers to the ability of firms to capture rents generated by their innovation activities. Concerns about appropriability originate from the pervasive presence of behavioral uncertainty, combined with the difficulties of specifying intellectual property rights and monitoring and enforcing contracts (Teece, 1986). In our research context, the appropriability regime refers to the extent to which firms are able to capture rents generated by their resources. As Gulati and Singh (1998: 789) argued, 'in a tight appropriability regime, firms can retain the profits they earn from their proprietary resources, while in a loose regime, these profits are subject to involuntary leakage or spillovers to other firms.' Following this logic, we argue



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that managers' functional experience will be more important to new venture performance if the institutional contexts allow new ventures to retain the rents generated by their managers' functional experience. Below we will examine how ownership and dysfunctional competition can moderate the relationship between managers' functional experience and new venture performance.

*Ownership.* As noted earlier, in a transition economy state-owned ventures are founded by the government or its agencies and have great legitimacy and government protection. In contrast, non-state-owned ventures lack legitimacy and government protection, and thus they are in a relatively weak position in the institutional environment (Nee, 1992). Following Teece's (1986) appropriability argument, we expect that the positive relationship between functional experience and new venture performance should be stronger in state-owned ventures than in non-state-owned ventures. As managers' functional experience enables new ventures to develop new technologies and products and build brands, such benefits can be better retained by state-owned ventures because of their legitimacy and government protection. Also, state ownership can provide new ventures with critical information, financial resources, and business opportunities (Lu, 2000). These resources represent complementary assets to managers' functional experience, which can help materialize the benefits of that experience.

In contrast, because non-state-owned ventures lack legitimacy and government protection, the benefits of their managers' functional experience may be involuntarily leaked to other firms, which may copy their innovations, break contracts, etc. In addition, government interference may further weaken the appropriability regime of non-state-owned ventures. For example, Nee (1992: 9) explicitly noted that 'in the absence of well-defined private property rights, private firms are vulnerable to unauthorized interference by distributors who impose illicit levies on them. . . .' Thus government interference can counteract the positive effect of managers' functional experience on performance. Therefore, we propose the following hypothesis:

*Hypothesis 5: The positive relationship between functional experience and new venture performance will be stronger in state-owned ventures than in non-state-owned ventures in a transition economy.*

*Dysfunctional competition.* The level of dysfunctional competition in a new venture's environment can also influence the strength of the appropriability regime in its environment. High levels of dysfunctional competition, which are characterized by patent and copyright violation and difficulties in monitoring and enforcing contracts, represent a weak appropriability regime in Teece's (1986) terminology. Dysfunctional competition also appears to be opportunistic competition in Williamson's (1985) sense of the word, which implies that it is difficult for firms to benefit from their market transactions.

Note that managers' functional experience is a market-based competitive competence that requires the support of a well-developed institutional framework for market competition. For example, even though managers' experience in technology areas can help new ventures develop new technologies and products, lack of intellectual property rights protection in a dysfunctional environment may make it difficult for the ventures to appropriate the potential economic benefits from their innovations (Teece, 1986). The profit potential of innovations will be dissipated through imitations or the unlawful behaviors of other firms. Similarly, as managers' experience in marketing can help build brand image, this could be illegally imitated by rivals.

In contrast, when the environment is characterized by low levels of dysfunctional competition, market institutions are more effective and property rights can be better protected. Under such conditions, the appropriability regime of the new ventures' environment becomes tighter, and as a result new ventures are more likely to retain rents generated by their managers' functional experience. One may argue that even under conditions of high levels of dysfunctional competition, managers' functional experience can still help new ventures stay one step ahead of ventures whose managers lack functional experience. We argue that the benefits of managers' functional experience tend to be lower under such conditions than the benefits under conditions of lower levels of dysfunctional competition for reasons noted above. Therefore, we propose the following hypothesis:

*Hypothesis 6: The positive relationship between functional experience and new venture performance will be stronger when the level of dysfunctional competition is low than when it is high in a transition economy.*

## METHODOLOGY

### Sample and data collection

We randomly selected 300 new technology ventures from a sample frame of 500 firms compiled by the Administrative Office of the Beijing High Technology Experimental Zone, one of the most developed high-technology industry zones in China. These ventures met three criteria used to define a new technology venture in China: (1) the management of the firm was composed of engineers or scientists; (2) 30 percent or more of the firm's employees were technical employees; and (3) it spent 3 percent or more of total sales on R&D (cf. Li and Atuahene-Gima, 2001). Consistent with an accepted definition of a new venture, all sampled firms were 8 years old or younger (cf. McDougall *et al.*, 1994). We first sent letters to the CEOs/general managers of these ventures, explaining the purpose of the study and inviting their participation. We collected the data by administering a questionnaire on-site rather than through the use of archival data and mail surveys because the lack of reliable archival data and the inadequate postal system in China made the use of these methods difficult (Hoskisson *et al.*, 2000). The use of on-site interviews also helped us gain access to the right respondents, ensured the correct use and understanding of the terms, and provided high response rates.

Questions were derived from the literature and in-depth interviews with eight entrepreneurs and 15 managers from 10 new technology ventures in China. The questionnaire was originally designed in English and then translated into Chinese by two management scholars competent in both languages and with substantial research experience in the subject area in China. To avoid cultural bias and to ensure validity, the Chinese version was back-translated into English, and we paid special attention to detecting any significant misunderstandings due to translations.

While it is preferable to use multiple informants, we selected one top manager (the CEO/general manager or a senior manager having a direct reporting relationship with the CEO/general manager) from each of the sampled ventures as the key informant. Prior research has found that top managers provide data as reliable and valid as those from multiple informants and objective data (Miller, Cardinal, and Glick, 1997; Zahra and Covin, 1993). Particularly considering the relatively small size of these ventures, the informants should possess comprehensive knowledge and represent a reliable source for the needed information (Bagozzi and Phillips, 1982).

We received 184 completed and valid questionnaires with a response rate of 38.6 percent (184/500). Of the responses, 54.4 percent were from CEOs/general managers, and the rest were from R&D/engineering or marketing managers. Among the responding ventures, 50.5 percent were in the electronic information industry, 17 percent were in integrated optical-mechanical and electric products, 12.6 percent were in new energy and new materials, 10.4 percent were in new pharmaceuticals and bioengineering, and 9.3 percent were classified as others (e.g., aerospace). There were no significant differences between responding ventures and nonresponding ventures in terms of venture size and age. We collected additional data by sending identical questionnaires to alternative top managers from a random subset ($N = 55$) of the responding firms, of which 45 were returned. All of the correlations of matched variables between the two raters were within the range of 0.90–1.00, indicating strong interrater reliability.

### Measurement

*New venture performance* was measured by eight items. The respondent was asked to rate his or her venture's performance relative to its principal competitors over the last 3 years on return on investment, return on sales, profit growth, return on assets, overall efficiency of operations, sales growth, market share growth, and cash flow from operations. We measured *political networking* with four items adapted from Xin and Pearce (1996). The scale indicates the extent to which the venture's senior management over the past 3 years has (1) spent much effort in cultivating personal connections with officials of government and its agencies, (2) maintained good relationships with officials of state banks and other governmental



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agencies, (3) devoted substantial resources to maintain good relationships with officials of administrative agencies, and (4) spent a lot of money on building relations with the top officials in government. Following McGee *et al*. (1995), *functional experience* was measured with five items that reflect the extent to which members of the senior management had functional experience in the following areas: (1) sales/marketing; (2) R&D/engineering; (3) manufacturing; (4) finance; and (5) administration. This measure indicates the overall experience of a venture's senior management across the various functional areas.

*State ownership* was coded 1 for state-owned ventures and 0 otherwise. Four items were used to measure *dysfunctional competition* (Li and Atuahene-Gima, 2001). They indicate the extent to which the venture's principal industry (i.e., the industry that accounts for the largest percentage of the venture's sales) has experienced the following in the last 3 years: (1) unlawful competitive practices such as illegal copying of new products; (2) counterfeiting of the venture's own products and trademarks by other firms; (3) ineffective market competition laws to protect the venture's intellectual property; and (4) increased unfair competitive practices by other firms.

We controlled for the following variables. First, *venture size* referred to the natural log of the number of full-time employees. Second, *venture age* referred to the number of years since the venture was founded (upper limit was 8 years). Third, *senior management team size* referred to the number of senior managers in the venture. Fourth, *senior management industry experience* referred to the average number of years that a venture's senior managers have spent in the current industry. Fifth, given the importance of product innovation in new technology ventures, we controlled for *sales from new products*, referring to the ratio of the venture's sales that were from new products introduced in the last 3 years. Finally, because half of the sample was from the electronic information industry, we coded the electronic information industry as 0 and all other firms 1 in order to control for industry effects.

Harman's one-factor test was used to check for the presence of common method variance (Podsakoff and Organ, 1986). We subjected all the key measures to a factor analysis and then determined the number of factors accounting for the variance in the measures. The results of the tests indicate no single factor accounted for a majority of the variance. We also examined the scree plots, which showed no sign of a common method bias. Discriminant validity of the constructs was tested by comparing a constrained model in which correlations between two constructs were constrained to 1 with an unconstrained model. The results of the pairwise tests among the constructs indicated that in each case the $\chi^2$ difference was significant at the $p < 0.01$ level, and the fit of the unconstrained model was significantly better than the constrained model (Bagozzi and Phillips, 1982), providing evidence of discriminant validity. In addition, we assessed the reliability of the multi-item scales with Cronbach's alpha. All scales had reliabilities above the 0.70 threshold.

## DATA ANALYSES AND RESULTS

Table 1 presents means, standard deviations, correlations, and reliability coefficients (Cronbach alpha) of variables examined in this study. Table 2 presents the results of hierarchical multiple regressions. To create the interaction terms, both independent and contingent variables were mean centered to reduce the potential problem of multicollinearity (Aiken and West, 1991). We tested our hypotheses based on Model 3, which has the most complete model specification. Hypothesis 1, proposing that political networking will be positively related to new venture performance, is supported ($b = 0.12$, $p < 0.05$). Hypothesis 2, proposing that functional experience will be positively related to new venture performance, is also strongly supported ($b = 0.25$, $p < 0.001$).

Hypothesis 3 proposes that the positive relationship between political networking and new venture performance will be stronger in non-state-owned ventures than in state-owned ones. This hypothesis is not supported because the coefficient for the interaction of political networking and state ownership is not significant ($b = -0.10$, n.s.). Hypothesis 4 predicts that the positive relationship between political networking and new venture performance will be stronger when the level of dysfunctional competition is high than when it is low. This hypothesis is not supported because the coefficient for the interaction of political networking and dysfunctional competition is not significant ($b = 0.06$, n.s.).

Hypothesis 5 suggests that the positive relationship between functional experience and new venture performance will be stronger in state-owned



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Table 1. Correlation matrix and summary statistics[a,b]

| Variables | Mean | S.D. | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1. Venture size | 3.97 | 1.42 | — | | | | | | | | | | |
| 2. Venture age | 4.83 | 2.03 | 0.25** | — | | | | | | | | | |
| 3. Type of industry | 0.49 | 0.50 | 0.19** | −0.04 | — | | | | | | | | |
| 4. Senior management team size | 4.63 | 2.13 | 0.53** | 0.10 | 0.09 | — | | | | | | | |
| 5. Senior management industry experience | 6.85 | 6.31 | 0.12 | 0.13 | 0.11 | 0.04 | — | | | | | | |
| 6. Sales from new products (ratio) | 0.43 | 0.26 | −0.11 | −0.29** | 0.07 | −0.13 | 0.06 | — | | | | | |
| 7. State ownership | 0.16 | 0.37 | 0.22** | 0.09 | −0.12 | 0.04 | 0.25** | −0.09 | — | | | | |
| 8. Dysfunctional competition | 3.36 | 0.82 | −0.01 | −0.06 | 0.01 | −0.04 | −0.14 | 0.00 | −0.07 | (0.71) | | | |
| 9. Political networking | 3.95 | 0.80 | 0.13 | −0.05 | −0.01 | 0.12 | −0.08 | −0.08 | −0.04 | 0.09 | (0.86) | | |
| 10. Functional experience | 3.87 | 0.60 | 0.09 | −0.01 | 0.08 | −0.10 | 0.07 | 0.02 | −0.12 | 0.12 | 0.23** | (0.76) | |
| 11. New venture performance | 3.54 | 0.60 | 0.09 | 0.02 | −0.01 | −0.02 | 0.05 | 0.13 | −0.20** | −0.02 | 0.22** | 0.34** | (0.87) |

[a] $N = 184$.
[b] Numbers in diagonal are reliabilities.
* $p < 0.05$; ** $p < 0.01$

Table 2. Results of regression analyses[a]

| Variables | Model 1 | Model 2 | Model 3 |
|---|---|---|---|
| Constant | 3.33*** (0.28) | 1.95*** (0.38) | 2.00*** (0.38) |
| *Control variables* | | | |
| Venture size | 0.08* (0.04) | 0.05 (0.04) | 0.06 (0.04) |
| Venture age | 0.01 (0.02) | 0.01 (0.02) | 0.02 (0.02) |
| Type of industry | −0.09 (0.09) | −0.09 (0.08) | −0.07 (0.08) |
| Senior management team size | −0.03 (0.02) | −0.02 (0.02) | −0.01 (0.02) |
| Senior management industry experience | 0.01 (0.01) | 0.01 (0.01) | 0.01 (0.01) |
| Sales from new products (ratio) | 0.24 (0.19) | 0.30† (0.18) | 0.33† (0.18) |
| State ownership | −0.40** (0.13) | −0.31** (0.12) | −0.23* (0.11) |
| Dysfunctional competition | −0.02 (0.05) | −0.05 (0.05) | −0.07 (0.05) |
| *Predictors* | | | |
| Political networking | | 0.13* (0.05) | 0.12* (0.05) |
| Functional experience | | 0.26*** (0.07) | 0.25*** (0.07) |
| *Interactions* | | | |
| Political networking × State ownership | | | −0.10 (0.12) |
| Political networking × Dysfunctional competition | | | 0.06 (0.06) |
| Functional experience × State ownership | | | 0.43* (0.19) |
| Functional experience × Dysfunctional competition | | | −0.17* (0.09) |
| $R^2$ | 0.08 | 0.19 | 0.25 |
| Increase in $R^2$ | — | 0.11*** | 0.06* |
| $F$-value | 1.99* | 4.17*** | 3.95*** |

$N = 184$.
[a] Because firm size and senior management team size are highly correlated, in supplementary analyses we dropped senior management team size and the results did not change.
† $p < 0.10$; * $p < 0.05$; ** $p < 0.01$; *** $p < 0.001$ (two-tailed test)

ventures than in non-state-owned ventures. This hypothesis is supported because the coefficient for the interaction of functional experience and state ownership is positive and significant ($b = 0.43$, $p < 0.05$). To facilitate interpretation of this finding, we plotted this interaction effect in Figure 1 by following the procedure described by Aiken and West (1991). To create the plot, all variables except functional experience and state ownership in Model 3 of Table 2 were constrained to their mean values. Functional experience took the values of one standard deviation below and above the mean and state ownership took the values of zero and one (because it is a dummy variable). As shown in the plot in Figure 1, functional experience has a stronger positive relationship with performance in state-owned ventures than in non-state-owned ventures, which is consistent with Hypothesis 5.

Hypothesis 6 states that the positive relationship between functional experience and new venture performance will be stronger when the level of dysfunctional competition is low than when it is high. This hypothesis is supported because the coefficient for the interaction of functional experience and dysfunctional competition is negative and significant ($b = -0.17$, $p < 0.05$). Following a similar procedure as described above, we plotted this interaction effect in Figure 2. The plot in Figure 2 shows that the positive relationship between functional experience and new venture performance is stronger when the level of dysfunctional competition is low than when it is high, providing support for Hypothesis 6.

## DISCUSSION AND CONCLUSION

How do managerial resources matter in new ventures in transition economies? With a sample of new ventures in China's high-technology industries, we examined simultaneously the roles of managers' political networking and functional experience. We found that political networking has a positive relationship with new venture performance. This finding is consistent with other studies of transition economies (e.g., Peng and Luo, 2000; Xin and Pearce, 1996). However, we found that the link between political networking and new



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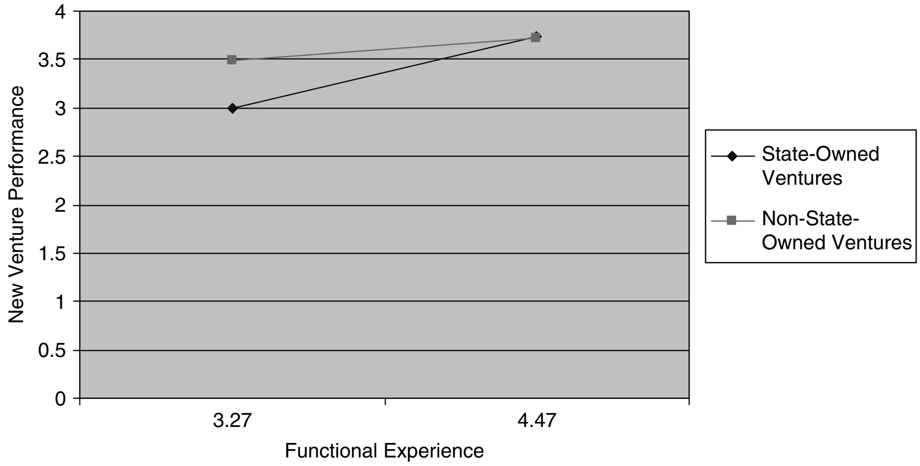


Figure 1. Functional experience and new venture performance: the moderating role of venture ownership

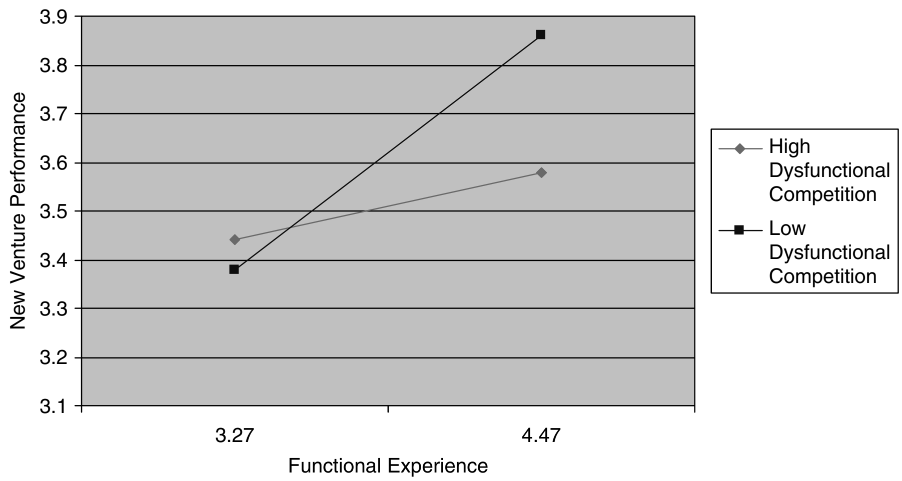


Figure 2. Functional experience and new venture performance: the moderating role of dysfunctional competition

venture performance is not moderated by ownership or dysfunctional competition. This finding is different from that of Peng and Luo (2000), who examined firms in various industries and found that the link between managerial ties with government officials and firm performance is moderated by ownership and industry. This inconsistency may be attributed to the sample difference (new ventures vs. firms in general). It seems that because new ventures face the liability of newness and government plays a significant role in developing high-technology industries in China, political networking has a universal relationship with new venture performance across different institutional contexts.

We found a more complex relationship between managers' functional experience and new venture performance. These two variables are significantly and positively related. Further, their positive relationship is stronger in state-owned ventures than in non-state-owned ventures and when the level of dysfunctional competition is low rather than when it is high. The strong yet contingent link of managers' functional experience with new venture performance suggests two important issues. First, as market transition theorists (e.g., Nee, 1989) have suggested, with the development and institutionalization of markets, managers' expertise as reflected in their experience becomes important. Note that firms examined here are new ventures in high-technology industries, which have emerged along with China's economic transition and have been playing a significant role in developing and commercializing new technologies and



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products and in creating new employment opportunities. Managers' functional experience is crucial in enabling these ventures to explore market opportunities and achieve better performance.

Second, the contingent relationship between managers' functional experience and new venture performance can also be attributed to the characteristics of transition economies. Given the inadequate legal framework that defines and protects property rights in a transition economy, managers' functional experience may not necessarily be transformed into better performance because their strategies, products, and services (or other outcomes that may stem from their functional experience) cannot be effectively protected by law and can be illegally copied by competitors. Our findings that the positive relationship between managers' functional experience and new venture performance is stronger in state-owned ventures and under conditions of lower levels of dysfunctional competition thus suggest that managers' functional experience is more important to new venture performance if the institutional contexts allow the ventures to appropriate the benefits generated by their managers' functional experience, which is consistent with Teece's (1986) appropriability argument.

## Theoretical and managerial implications

The present study makes several important contributions to the literature. First, while managers' role in new ventures has long been highlighted in the literature, most previous studies have focused on new ventures in market economies. Relative to their counterparts in market economies, new ventures in transition economies face more constrained resource conditions because the legal institutional framework and strategic factor markets have not been well developed. Our study contributes to this line of research by empirically demonstrating how and under what conditions various types of managerial resources are linked with new venture performance in a transition economy. Also our study advances the international entrepreneurship literature by providing empirical evidence that institutional contexts affect the role of managerial resources in new venture performance. Consistent with Baker *et al.* (2005), our results suggest that institutional contexts affect the extent to which managers in new ventures are able to appropriate the benefits from their managerial resources (e.g., functional experience).

Second, our findings can contribute to the literature on firms in transition economies. So far, most studies in this area have focused on managerial ties (e.g., Peng and Luo, 2000; Xin and Pearce, 1996) as if managerial ties are the main, if not the only, factor that is important in transition economies. However, it should be noted that given the coexistence of the redistributive mechanism and the market mechanism in transition economies, firms need different types of managerial resources to deal with the redistributive power and the market forces. In this study, we adopted a broader view by examining the roles of managers' political networking and functional experience simultaneously and found that both of them have significantly positive relationships with new venture performance. Our findings represent an important addition to the literature because they suggest that managerial ties are not the only factor (and probably not the most important factor) that contributes to firm success in transition economies. We believe our study will encourage future research on transition economies to go beyond ties or *guanxi* and to focus on a broader range of managerial resources affecting firm success.

Third, our findings can contribute to the resource-based view. Recently, scholars have proposed a contingent resource-based view suggesting that effective deployment of firms' resources is conditioned by contextual factors (Priem and Butler, 2001). Our focus on China's transition economy provided us with a unique opportunity to contribute to this line of research. We integrated the resource-based view with transaction cost economics to examine how institutional contexts can moderate the relationship between managerial resources and new venture performance in a transition economy. In support of Teece's (1986) argument of the appropriability of rents, our findings suggest that managers' functional experience has a stronger relationship with new venture performance if the ventures' institutional contexts allow them to retain the rents generated by their managers' functional experience. These findings provide insights into the interplay of resources and efficiency vs. legitimacy and the impact of appropriability. They suggest that the value of resources actually depends upon the strength of the appropriability regime in a firm's institutional context.

These findings thus contribute to our knowledge of the boundary of the resource-based view.

Our findings also have important practical implications. Practitioners in transition economies, both local ones and foreign investors, have long believed that in transition economies 'who you know is all that counts,' and they have expended significant efforts in building various types of ties. Our results suggest that while political networking remains important, managers' functional experience is also crucial. Indeed, a transition economy is one that is transitioning toward—and thus becoming closer to—a market economy. Hence, firms should pay increasing attention to building market-related competitive competences in order to capture the emerging market opportunities in these economies. Our results also inform that the extent to which firms can benefit from their market-related competitive competences depends upon the strength of the appropriability regime in their institutional contexts. Thus, rather than simply adapting to the environments in a passive way, firms need to proactively strengthen the appropriability regime in order to maximize the benefits from their market-related competitive competences.

### Limitations and future research

This study has several limitations that also suggest directions for future research. First, the study has examined the contingent roles of managers' political networking and functional experience in new venture performance. Further research can examine the roles of other types of managerial human capital (e.g., their education background) and social capital (e.g., their ties with external actors other than government officials). Future research can also benefit from examining contingency variables other than those examined in this study. For example, it would be interesting to examine how the roles of managerial resources differ between high-technology industries and low-technology industries.

Second, our sample was limited to Chinese new technology ventures. A natural extension of our study would be to compare the roles of political networking and functional experience within transition economies and between transition economies and market economies. Third, the use of self-report data may pose such potential problems as the limited recall of the respondents, biased perceptions of past realities, and common method issues. However, we took several actions during data collection to improve both the reliability and the validity of the retrospective reporting. Our post hoc examination and validation analysis indicated no serious common method problems. In particular, considering the supported interaction hypotheses, it is unlikely that respondents would have an 'interaction-based theory' in their minds that could systematically bias their responses to produce these results (Aiken and West, 1991). Finally, the cross-sectional data used in the study do not allow for causal interpretations among the variables. They also do not allow us to examine the 'dynamic' nature of managerial resources. Future studies can benefit from a longitudinal research design. In fact, Kraatz and Zajac (2001: 653) have suggested a very useful approach, 'of first identifying historically valuable resources and subsequently examining their impact over time in a changing environment context.' This approach could enable future research to examine how the roles of different managerial resources change in the process of economic transition.

In conclusion, this study examined the effect of managers' political networking and functional experience on new venture performance across different institutional contexts in China's high-technology industries. The findings contribute to our understanding of the roles of managerial resources in new ventures during the process of institutional development of markets.

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