

AN EXPLORATORY STUDY OF CULTURAL DIFFERENCES

AND PERCEPTIONS OF RELATIONAL RISK

Susana Costa e Silva

Universidade Católica Portuguesa

Rua Diogo Botelho, 1327

4169-005 Porto, Portugal

Phone: 351 22 6196200

ssilva@porto.ucp.pt

Luciara Nardon

Vlerick Leuven Gent Management School

Vlamingenstraat 83

BE-3000 Leuven, Belgium

Phone: 32 16 24 8835

luciara.nardon@vlerick.be

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ABSTRACT

This working paper is part of a research project examining the role of culture and culture differences in foreign partnerships. We build on prior research on culture distance to explore the influence of perceptions of cultural differences on perceived relational risk. Perceived relational risk is defined here as the degree of satisfaction of being involved in business activities with nationals of a given country. Contrary to expectations, preliminary analysis suggests that cultural differences are sometimes perceived as a desirable characteristic and may be associated with lower relational risk. We speculate that culture distance is an asymmetric construct in which the perception of a cultural difference may be interpreted as positive or negative depending on the perspective from which the reading is made and the nature of the task in which the perception is formed. Plans for future research are discussed.

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Susana Costa e Silva, Universidade Católica Portuguesa, Portugal

Luciara Nardon, Vlerick Leuven Gent Management School, Belgium

“At the present time there is a greater need for effective international and cross-cultural communication, collaboration, and cooperation, not only for the effective practice of management but also for the betterment of the human condition. Ample evidence shows that cultures of the world are getting more and more interconnected and that the business world is becoming increasingly global. As economic borders come down, cultural barriers will most likely go up and present new challenges and opportunities in business.” (House, 2004:1)

Introduction

As well described by Robert House (2004) in the opening quote, increasing globalization brings the need to cooperate and collaborate with people from various cultural backgrounds, increasing the range of opportunities available to managers and at the same time posing important challenges. Developing successful relationships with people from different cultures may be challenging for several reasons, including people’s tendency to have preconceived assumptions about how the world works, how individuals behave, and which behaviors are acceptable or unacceptable in a business setting. These ideas are largely influenced by our personal experiences and cultural background.

We tend to approach intercultural situations using our own perceptions, beliefs, values, biases, and assumptions about what is likely to happen as a guide (Kluckhohn 1954; Geertz, 1973; Hofstede, 1980, 1991; Trompenaars and Hampden-Turner, 1998; Schneider and Barsoux, 2003; Steers and Nardon, 2006). As a result, when we engage in exchanges with people from different cultures we often find that the consequences of our actions are different than we expected or intended (Adler, 2002). The results can range from embarrassment to insult to lost business opportunities.

Managers are aware of these challenges and consciously or unconsciously take them into consideration before embarking in a business relationship with foreign counterparts. To this end, common sense suggests that small cultural differences are better than large ones, as higher degrees of difference are likely to result in more problems. This assumption has shaped most of the cross-cultural management literature, and is explicit in several studies using measures of culture distance to predict behavior.

Following this line of thought one would expect the perceived relational risk of an interaction, that is the degree of satisfaction of being involved in business activities with nationals of a given country, would be higher in situations of smaller culture distance. However, contrary to expectations, our preliminary analysis suggests that cultural differences are sometimes perceived as a desirable characteristic and associated with lower perceived relational risk.

This paper presents the results of an exploratory pilot study with Portuguese managers doing business internationally, exploring perceptions of cultural differences and relational risk. We will begin this paper with a review of relevant literature on culture and culture distance. Then, we will present the results of our exploratory interviews and offer some insights on the role of culture distance in shaping relational risk assessment.

National culture and culture distance

The word “culture” has been defined in several ways. Trompenaars (1993), for example, defines culture as the way in which a group of people solves problems and reconciles dilemmas. Clifford Geertz (1973) defines culture as the means by which people communicate, perpetuate, and develop their knowledge about attitudes towards life; culture is the fabric of meaning in terms of which people interpret their experience and guide their action. Kluckhohn’s (1954) approach defines culture as the collection of beliefs, values, behaviors, customs, and attitudes that distinguish the people of one society from another. Finally, Hofstede (1991) suggests that culture is the collective programming of the mind that distinguishes the members of one human group from another. Culture is the glue that ties a group or society together and signifies what they stand for. In both the personal and the business world, culture establishes the rules that govern how people and organizations operate.

Cross-cultural management scholars have recognized that variance in these rules of behavior across nations are likely to have important implications for managers. To this end, significant research has focused on classifying cultures and identifying cultural dimensions that are meaningful to managers, in an attempt to map out meaningful differences. At present, there are several models available to examine the role of culture in organizations. These models focus on different aspects of societal beliefs, norms, or values. Cultural models have been proposed by Kluckhohn and Strodtbeck (1951), Hofstede (1980, 2001), Hall (1959, 1981), Trompenaars (1993), Schwartz (1994), and the GLOBE research team (House et al., 2004)

and have offered useful templates for comparing management processes, HRM policies, and business strategies across national borders.

Of these models, Hofstede's (1980) has enjoyed the most popularity within the cross-cultural management field, as it was the first to focus on management and provide numerical indicators for various countries facilitating its use in empirical investigation of cultural influences on managerial behavior. For instance, Kirkman, et al. (2006) review of 180 studies using Hofstede's (1980, 2001) cultural values framework between 1980 and 2002 suggests that cultural values have been associated with change management, conflict management, decision-making, human resource management, leadership, organization citizenship behavior, work-related attitudes, negotiation behavior, reward allocation, and individual behavior relating to group processes and personality, among others.

Moreover, some authors focus on the cultural differences among nations and recognize that the degree of difference (measured through distance among variables) is likely to have an impact on business. This stream of thought focuses on identifying the role of cultural distance in several business issues (e.g. Kogut and Singh, 1988; Morosini et al., 1998; Manev and Stevenson, 2001). Building on this literature, this research focuses on the way cultural differences are perceived and influence international level business decisions. Below we review the culture distance literature.

Cultural distance

The notion of cultural distance was first introduced by Beckermann (1956), and gained popularity within business studies with in Scandinavian school, which observed that Swedish firms expanded to new markets progressively from lower to higher cultural distance (Johanson and Vahlne, 1977). In their seminal article, Kogut and Singh (1988) introduced a measure of cultural distance which can be used to empirically test the effect of cultural differences in organizational outcomes. The cultural distance index is constructed as an aggregation of Hofstede's four original cultural dimensions (1980): uncertainty avoidance, individualism-collectivism, power distance, and masculinity-femininity. The cultural distance index is computed through the deviation along each of the four cultural dimensions between a country of focus and other countries as illustrated in Figure 1.

Figure 1 – The Kogut and Singh Index

$$CD_j = \sum_{i=1}^4 \left[\frac{(I_{ij} - I_{iu})^2}{V_i} \right] / 4,$$

where, j is the country whose cultural distance is being measured; i, each of the four dimensions; and u the country of reference.

This index was subsequently used in many international business studies investigating topics ranging from foreign direct investment, headquarter-subsidary relations, expatriate selection and adjustment (see for example, Benito & Gripsrud, 1992; Reuer & Tong, 2005). The notion of a cultural distance index is appealing as it eliminates the complexities usually associated with cultural issues, and provides a handy number to be used in empirical modeling.

Following Kogut and Singh (1988), Morosini et al. (1998) proposed an adaptation on Kogut and Singh's index to estimate the cultural distance between Italy and other countries based on Hofstede's four dimensions of culture (see Figure 2). Manev and Stevenson (2001) also used the work of Kogut and Singh (1988) as a base to define cultural distance as the degree to which cultural norms in one country differ from the ones of another. These authors based their research on managers with an expatriate status and reached the conclusion that a minor cultural distance allows the development of stronger instrumental ties between managers. Cultural distance was computed here as a Euclidian distance similar to Kogut and Singh's index (see Figure 3).

Figure 2 – Morosini, Shane and Singh Index

$$CD_j = \sqrt{\sum_{i=1}^4 (I_{ij} - I_{il})^2},$$

where, CD_j is the cultural difference for the j-th country; I_{ij} , the Hofstede's score for the i-th cultural dimension; and j-th country; and I indicates Italy.

Figure 3 – Manev and Stevenson's Index

$$CD_{ij} = \sqrt{\sum_{K=1}^4 (D_{ik} - D_{jk})^2},$$

where CD_{ij} is the cultural distance between managers i and j, and D_{ik} and D_{jk} are the indices for the k-th dimension in i's and j's national cultures.

Despite its popularity, the cultural distance index as originally developed by Kogut and Singh has received some important criticisms. For instance, in a review of the culture distance literature, Shenkar (2001) identified several conceptual and methodological concerns regarding this construct. He suggests the cultural distance index has several hidden faulty assumptions built into it, namely: 1) an illusion of symmetry, or the notion that the role of the cultural distance is identical from the home and host countries point of view; 2) an illusion of stability, or the notion that culture is static and the distance remains constant over time; 3) an illusion of linearity, or the idea that the effect of cultural distance on business issues is linear; 4) an illusion of causality, or the assumption that cultural distance is the only determinant of distance that is relevant; 5) and illusion of discordance, or the notion that cultural differences are undesirable. He also argues that some methodological properties of the cultural distance index are problematic, such as: 1) the assumption of corporate homogeneity, which refers to the fact that the index does not account for organizational culture; 2) the assumption of spatial homogeneity, or the notion that countries are culturally uniform; 3) the assumption of equivalence, or the assumption that all four cultural variables included in the index are equally important.

Finally, some argue that cultural distance is a cultural level measure and therefore can only be used to investigate cultural level phenomenon (Sousa and Bradley, 2004). Even though several authors use cultural distance and psychic distance interchangeably (e.g. Shoham and Albaum, 1995; Lee, 1998), recently Sousa and Bradley (2004) have argued that the two

constructs are conceptually different. These authors argue that cultural distance is a national level phenomenon while psychic distance is an individual level one. Psychic distance is the perception an individual has regarding the cultural difference between the home and foreign countries. As such, it is highly subjective and can't be measured with factual indicators. Additionally, perceptions can be changed by increased experience with the foreign culture. On the other hand, they argue cultural distance refers to the cultural level of analysis and as such should only be applied to country level studies.

However, despite the above criticism, the Kogut and Singh index continues to be widely used, in part due to its convenience and in part due to the lack of a reliable alternative (Dahl, 2004). The Kogut and Singh Index is mainly used in studies focusing on culture's influence on firm's performance (see for instance, Barkema and Vermeulen 1997; Lincoln et al. 1981; Olson 1981; Pothukuchi et al. 2002), with contradictory findings. For instance, Larimo (2003) found that culture distance negatively affect performance, Salk and Brannen (2000) found no effect of culture distance on performance and Morosini and colleagues (1998) and Kessapidou and Varsakelis (2002) found that culture distance positively affects performance. The inconclusive findings of this line of study suggest that current conceptualizations of cultural distance do not fully represent the complexity of business across cultures.

In this study we elaborate on the current literature on culture distance, focusing on the specific issue of relational risk.

Culture distance and relational risk

Scholars have long recognized that engaging in international partnerships brings new business opportunities, but also new challenges and risks. Whereas most of the research in this area emphasizes the advantages of partnering and highlights the need for mutual trust (see for example, Kale et al. 2000, Moorman et al. 1992), the importance of trust is a result of the high risk associated with such international partnerships (Jeffries & Reed, 2000). In other words, international relationships carry risks, and these risks can be mitigated by trust. However, regardless of the level of trust in a relationship, risk is always present, as the attitude of trusting implies that there is risk. Thus, there is no trust if risk is not present. As noted by Nooteboom and colleagues (1997, p. 311) "... trust pays, but it also carries the risk of betrayal."

Trust and risk are therefore important components when evaluating actors' satisfaction with a partnership. Even though most research focuses on levels of trust in foreign partners, we

argue that perceived relational risk is also an important indicator of satisfaction with a partnership. In other words, we argue that the level of satisfaction with a foreign partnership is dependent on the perception of relational risk.

Following Das and Teng (1996), we propose that relational risk is an individual's perception of the risks associated with cooperating with the alliance partner. This risk is subjective, and while it is influenced by objective characteristics of the situation, it is also influenced by each individual's risk preferences, and past experiences (Nooteboom et al., 1997; Ring & Ven, 1992). We argue that the risk implicit in a relationship is reflected in the satisfaction retrieved from that relationship. In other words, we argue that the willingness to engage in a relationship with foreign nationals is influenced by the perception of risk involved in the relationship. Hence, the lower the risk perceived in a relationship, the higher the satisfaction with that partnership. Nevertheless, the problem of risk assessment is not independent from trust itself. In fact, we argue that risk besides being an important element in evaluating satisfaction along with trust, is also an important component of trust.

Scholars have long recognized that interpersonal trust is important for business, because it makes actors more willing to collaborate, increases the likelihood of success (see for instance Madhok, 1995; Ring and Van de Ven, 1992; Smith et al., 1995), and the level of satisfaction of partners (Gulati, 1998; Powell, 1996; Sako, 1998; Zaheer, McEvily, & Perrone, 1998b). Nowadays, as a result of increasing globalization, ease of communication and transportation, parties from different nation states, cultures and languages are increasingly engaging in alliances and other business relationships (Ring et al., 1992). These relationships require "a much better understanding of how trust is developed, or manifested, in different cultures (...)" (Ring and Van de Ven, 1992, p. 496). It will also require an understanding on how trust is developed and manifested across cultures.

The trust one has in a foreign counterpart is influenced by opposing forces. On one hand, the propensity to trust and attitudes toward cooperation are likely to vary across cultures (Steenma et al., 2000; Shane, 1992; Hill, 1990; Fukuyama, 1996), suggesting that people from some cultures may be more likely to trust foreigners than others. On the other hand, trust is facilitated by shared values and beliefs, so one would assume that it is easier to trust people from similar cultures than from distant ones.

The trust literature suggests that trust is built upon different pillars: actor willingness to trust (Aulakh, Kotabe, & Sahay, 1996), belief on integrity and fairness (Zaheer, McEvily, &

Perrone, 1998a), reliability, or likelihood that partner will honor commitments (Anderson & Weitz, 1989), and risk and vulnerability (Bromiley & Cummings, 1995; Lewis & Weigert, 1985; Mayer, Davis, & Schoorman, 1995).

As discussed above, risk and vulnerability are key components of trust, as trust only exists if partners are aware to the possibility of being failed. In other words, when partner in a relationship are vulnerable regarding the other part trust is important (Sabel 1993, Mayer et al. 1995).

In an increasingly global economy, establishing international alliances became imperative for some firms survival and strategic for their continuation. In such environment differences in values, beliefs, assumptions, and contextual realities may at times hinder and at times facilitate developing trust among international partners. In this research we focus on the risk element of trust by exploring the perception of relational risk with foreign counterparts by Portuguese managers.

Research Methods and Analysis

This is the first step of a larger research project exploring perceptions of cultural differences and trust. At this stage, we have conducted five exploratory pilot interviews with Portuguese managers engaged in alliances with foreign partners, in order to understand their preferences in terms of the cultural background of business partners. These interviews were semi-structured to allow personal, attitudinal, and value-laden material to emerge (Jankowicz, 1991).

In this study we focus on how individuals from one culture (specifically, Portuguese) perceive the risk of engaging in business relationships with individuals from other cultures. With this analysis we want to uncover how cultural differences are perceived and the type of impact they have on relational risk assessment. We do not address in this study the role of culture in influencing trusting behavior.

Participants were asked to name, based on their experience, the nationalities (cultures) they most and least liked to do business with. We assume that such preferences stem from the perceived relational risk, that is the “liking to do business” reflects a perceived low relational risk. In order to explore the effects of the transaction itself on their preference, we also asked participants to name the nationalities with which they liked most to engage in social relationships. Find below a brief summary of the interview data as it refers to business relationships, and the respective cultural distance index, as defined by Kogut and Singh.

Table 1 - Revealed preferences to do business

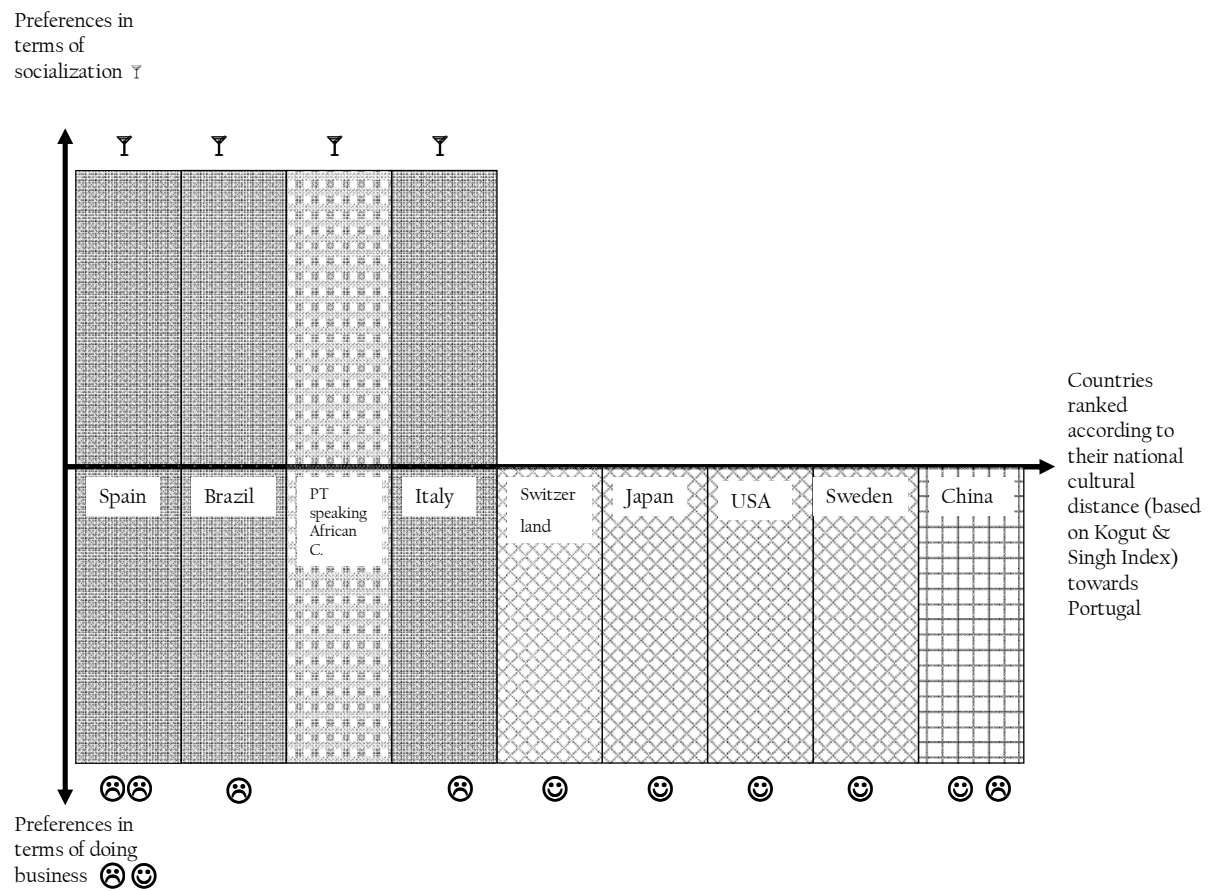
Manager	Countries in which does business	Preferred nations	Kogut and Singh's Index	Least liked nations	Kogut and Singh's Index
1	Sweden, china, Ireland, Spain, Japan	Sweden	4.17	China	NA (high)
2	USA, Germany, Italy, Spain	USA	4.00	Italy	2.50
3	Japan, China, Brazil, Russia	Japan	3.29	Brazil	0.64
4	China, Spain, Portuguese speaking African countries	China*	NA (high)	Spain	0.47
5	France, Germany, Switzerland, Spain, Italy	Switzerland	3.12	Spain	0.47

* Even though we do not have equivalent information to calculate Kogut and Singh's index for China, culture studies on China and Portugal suggest a high degree of national cultural difference.

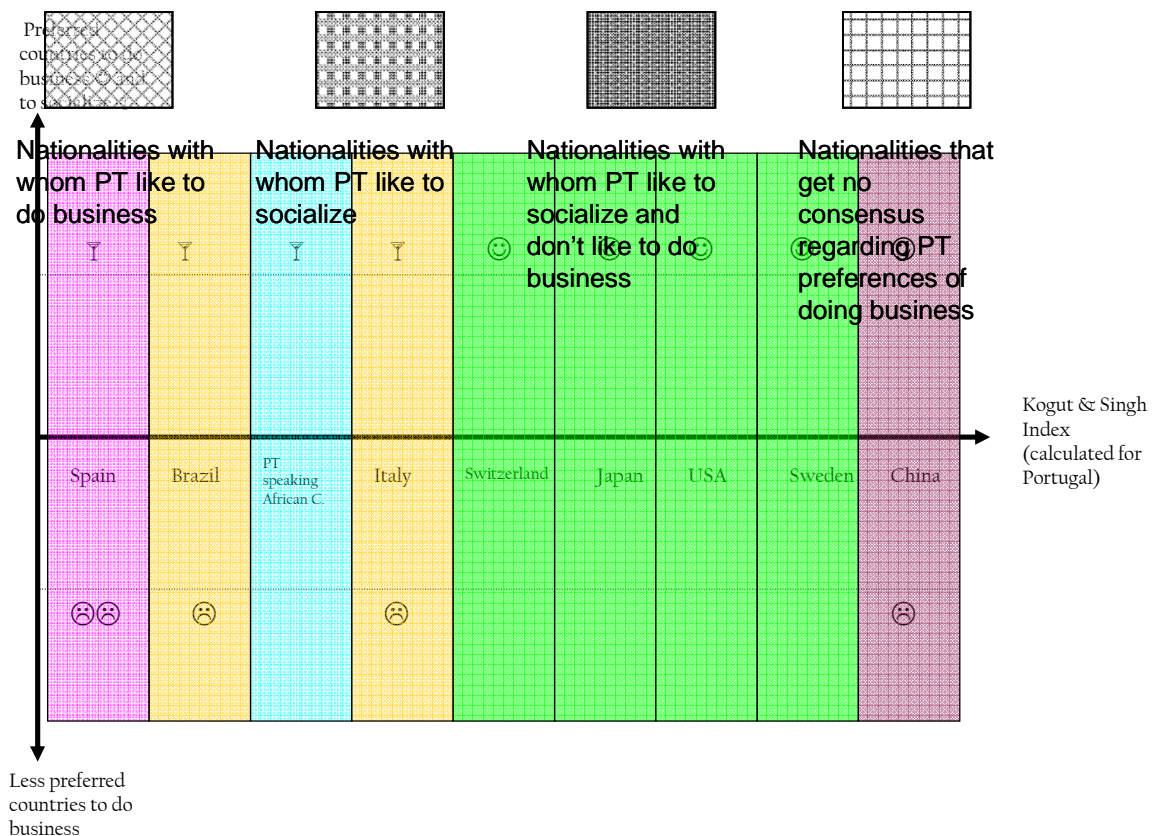
Table 2 - Revealed preferences to socialize

Manager	Countries in which does business	Preferred nations	Kogut and Singh's Index
1	Sweden, China, Ireland, Spain, Japan	Spain	0.47
2	USA, Germany, Italy, Spain	Spain	0.47
3	Japan, China, Brazil, Russia	Brazil	0.64
4	China, Spain, Portuguese speaking African countries	African Portuguese Speaking Countries	1.35
5	France, Germany, Switzerland, Spain, Italy	Italy	2.5

Figure 4 - Preferred countries to do business and to socialize in terms of perceived risk



Note: The X axis tries to give an idea of the national cultural distance between Portugal and the referred countries. Symbols (faces and glasses) represent number of responses in our pilot interviews.



The pilot interviews reveal an interesting and surprising pattern as we may see in Figure 4. Contrary to expectations, the five Portuguese managers interviewed prefer to do business with foreign partners from distant cultures, which we interpret as a perception of lower relational risk. Likewise, four of the interviewees dislike most to do business with partners of closer cultures. Interestingly, when enquired about their preferences in doing business with the nationality they like the most and their own people, they all preferred the foreign partner. These findings suggest that a measure of distance alone is not a good explanation in any direction.

However, cultural differences were recognized as important criteria in assessing their partners, but they were not always considered negative. Instead, the perception of the other's culture was used as an evaluative component comparing to one's own culture. Some cultural

characteristics different from one's own were considered desirable. For example, the Portuguese culture is usually described as polychronic in regards to their perception of time (Hall, 1959, 1981; Steers and Nardon, 2006), meaning that punctuality is not considered a priority as time is seen as flexible, fluid, and relative. Yet, when asked what they disliked about their foreign counterparts they said "they are frequently late" and "they often miss deadlines". Similarly, Portuguese people tend to prefer indirect communication styles, focusing on the context of the communication to interpret messages, what Hall (1959, 1981) calls high context communication. Yet, when asked why they did not like to work with Brazilians, Spaniards, and Italians, the managers in our pilot interviews made comments such as "they don't always follow through on what they say", "they speak indirectly", and "they do not say what they think". Noticing these contradictions one manager said "they are very much like us". Whether they openly acknowledged or not, these managers seemed to think that people from cultures "like ours" were less trustworthy and therefore the risk involved in these partnerships was considered to be higher. This is made more evident when these managers stated they prefer to do business with some foreign cultures rather than with their own people.

On the other hand, when asked about the characteristics of the partners they appreciated, managers' comments highlighted cultural characteristics that were different from their own, such as their direct communication style, assertiveness, and tendency to follow through on their words. Here again managers mentioned "they are different from us" as a positive characteristic.

However, just being different is not enough. For instance, one manager disliked working with the Chinese because they were considered too intricate and difficult to understand. In this case, cultural differences were perceived as negative and difficult to cope with. Yet, another manager liked to do business with the Chinese because he reached a stage of knowledge about them that facilitates business. He states "it took me more than two years to get to know how to negotiate with them, but now that I know how they are, negotiation is easy", which suggests that learning about the other culture may bridge possible gaps between culturally distant partners.

While this data is far from conclusive, it does suggest a learning effect on dealing with culture. It is possible that the impact of cultural differences decrease with exposure to the culture, and that the willingness to trust the other is related to understanding how the other operates. This may explain why low-context, monochronic cultures were appreciated by this

sample. Even though these cultural characteristics are different from the Portuguese, they are perceived as more predictable, and are easier for an outsider to understand.

Take for instance low context communication (Hall, 1959, 1981). Low context communicators rely on words to deliver the message, while high context communicators rely on other cues, such as the parties involved, body language, and the context itself. High context communicators frequently speak indirectly, and “do not say what they mean” as one of our informants suggested. For someone not immersed in the context it is difficult to comprehend the whole meaning of the communication as contextual cues are easily missed. On the other hand, communicating with low context communicators is much easier as “what they say is what they mean.”

The same can be said about time orientation (Hall, 1959, 1981). While individuals in polychronic cultures expect people to be late, there is a tacit understanding of when things will be done. When in a foreign polychronic environment this understanding is not there, and there is a sense of chaos and confusion by not knowing what will happen when, as time perceptions are not clearly spelled out. However, it is easy for a polychronic culture to understand a monochronic person doing things “on time”. While this data is still exploratory, it suggests that some cultural characteristics may facilitate “being trusted”, or offer less risk, suggesting that culture not only influences how willing one is to trust the other, but also how trustworthy one is thought to be. Therefore, our preliminary proposition:

Proposition 1: Some cultural characteristics are perceived as less risky than others.

Proposition 1a: Low context cultures are perceived as less risky than high context cultures.

Proposition 1b: Monochronic cultures are perceived as less risky than polychronic cultures.

Interestingly, however, when the same managers were asked about their preferences for social purposes, their preferences changed to cultures with small cultural distance, such as Italy, Spain, Brazil, and Portuguese speaking African countries. Here, managers claimed they feel more “at home” with such cultures and find their company more enjoyable.

We speculate that the variance in preference is related to the task at hand. Cultural distance in itself is not necessarily an obstacle, but may be perceived sometimes as a positive, sometimes as negative, depending on the nature of the task and the purpose of the relationship. This is in line with Shenkar’s (2001) criticism that current cultural distance measures erroneously assume that the lack of cultural fit results in an obstacle to the transaction. However, he argues, different aspects of culture may be more or less critical to operations, and some

cultural differences may be complementary, while others may be irrelevant. Notice, for instance that the managers in our pilot study did not mention variations in power distribution or different levels of collectivism and individualism. Presumably, these cultural aspects were not relevant in their dealings. Instead, communication styles, time orientation, and to some degree rule orientation were considered more critical by this sample when doing business. However, when the subject was socialization, cultural similarity was considered more important. Therefore, we suggest:

Proposition 2: The perception of foreign partner's relational risk is task dependent.

Preliminary conclusions

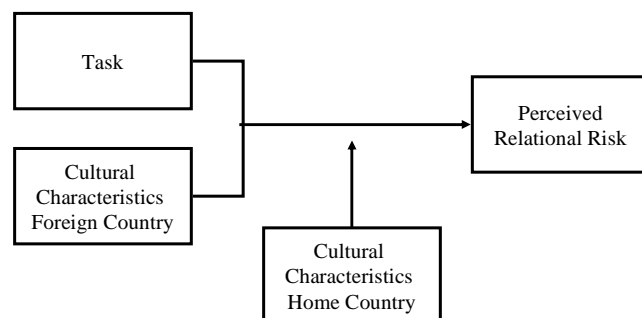
Our pilot interviews suggest that Portuguese managers' assessment of foreign partners' relational risk is influenced by perceptions of national cultural differences, but that the *amount* of national cultural difference is not the most important criteria. Rather, the *type* and *direction* of these differences coupled with the nature of the task or purpose of interaction are more important. In other words, cultural differences are sometimes perceived as desirable, and sometimes perceived as undesirable, depending on the task characteristics. Based on limited data, we speculate that some cultural characteristics are perceived as more desirable than others, and those may be more important than any measure of difference.

Even though our current sample is limited to Portuguese managers, we speculate that in some situations one party may find the other trustworthy but not be reciprocated. That is, cultural differences are not symmetric (Shenkar, 2001) in the sense that the same cultural variable may have different roles to the cultures involved.

Figure 5 illustrates our *tentative* model on the role of cultural differences on relational risk. We speculate that a foreign nation's cultural characteristics combined with the nature of the task are the main drivers of perceived relational risk, but this relationship is moderated by the assessor's home culture. In other words, an individual's assessment of a partner's relational risk, will be determined by a combination of the partner's cultural characteristics and the task at hand – or the purpose of the relationship. However, we speculate that one's own culture of reference is likely to play a role in moderating this relationship (for instance, a culturally based tendency to trust more or less, to accept different perceptions, or to value particular characteristics). Moreover, the role of one's own culture is not in defining a degree of “difference” or cultural distance, but in providing a different perspective and expectations regarding which characteristics are desirable.

For example, if the task at hand asks for punctuality and precise time management, Portuguese managers may perceive the relationship with Swedish managers as a low risk one, as Swedish people are usually associated with a culture of monochronic behavior. Thus, based on how Portuguese value Swedish national features and on the nature of the task, a certain relational risk is asserted to this relationship. Nevertheless, the meaning of “being on-time” is in itself influenced by the cultural characteristics of the home country, and moderates the influence of cultural characteristics on relational risk assessment.

Figure 5 - Cultural differences and perception of relational risk



Next steps of the research project

This paper described the results of our pilot interviews investigating Portuguese managers’ perceived relational risk with foreign partners. The pilot interviews provided us with some tentative propositions and the foundations to develop a more structured interview guide and fine tune our literature review. This project relies on the iterations between data and theory. We are expanding our literature review to adjust our conceptualization of the model presented in figure 1. We are exploring a wider literature relating to culture, cultural differences, cultural distance, and relational risk. Guided by theory, we will develop a structured interview guide and continue to collect and analyze data. We foresee the need to explore perceptions of relational risk in other countries as well as explore dyads in which both cultures’ perceptions of each other can be compared and contrasted.

We believe this project will contribute to the cross-cultural management field both by providing alternative ways of thinking about cultural differences in general and cultural distance in particular as it relates to relational risk assessment.

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