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**Americans Doing Business in China:
The Need to Navigate Socio-Cultural Differences to
Succeed**

Yasmin Elyse Baksh

University of Oklahoma

Abstract

Understanding the socio-cultural influences in a given country is an important starting point before embarking on business ventures in that country. This holds true especially in a country like China, which is almost the polar opposite of the United States in many cultural and business ideological areas. In addition to a cultural examination of China using the Hofstede Model, this article will also explore other topics like *guanxi* (the concept of face), corruption, and negotiations along with the legal and administrative procedures necessary to conduct business in China.

Americans Doing Business in China: The Need to Navigate Socio-Cultural Differences to Succeed

The United States and China are two very different cultures and are sometimes, polar opposites when it comes to some beliefs and customs. With increasing contact between China and the U.S. and merging economic interests, it is important for Americans to understand the culture of China. Learning and understanding our differences can help us continue to build political, economic and social relations.

Geert Hofstede's model for understating culture is a widely used for analyzing cultural differences. Hofstede's model identifies five dimensions of culture: power distance, uncertainty avoidance, individualism-collectivism, masculinity-femininity and long-term orientation. Dimensions are given a number on a scale from zero to 125 to indicate where a country lies on the spectrum.

Power distance refers to how power is distributed. In high power distance societies, power lies with society's leaders. There are different levels of rights depending on where you are in the hierarchy. Seniority and wisdom command respect. The law should not be applied equally. The people on top are considered better than everyone else and are entitled to certain perks. Countries with low power distance value equality within the government, organizations and family. Everyone should have equal rights. China is ranked very high in power distance. Hofstede assigned China a power distance number of 80. The average for other Asian countries is 60, while the world average is 55. The United States stands on the other end of the spectrum, with a power distance ranking of 40, well below China's ranking and right below the world average (Geert Hofstede, 2009).

China's high power distance probably stems for the tradition of Confucian philosophy which was well ingrained in Chinese culture for 2,000 years (Graham, 2003). Confucius's teachings emphasized a strict social order in which reverence, respect and unquestionable obedience were endowed to those holding high ranks. Every relationship, except the neighbor to neighbor relationship, was hierarchical. This is drastically different from the basis of American society. The United States was formed on the basis that "all men are created equal," an idea that has endured to this day.

Uncertainty avoidance deals with how a society views ambiguity and the measures they will take to avoid it. High uncertainty avoidance cultures do not like risks and like to know what is going on. They create more rules to ensure predictability. Low uncertainty avoidance cultures do not mind not knowing what will happen. They do not like as many rules and like having a degree of freedom. China has an uncertainty avoidance ranking of 60, close to the world average of 64. The United States' uncertainty avoidance ranking of 46 is low compared to the world average (Hofstede, 2009).

Low uncertainty avoidance indicates that the US is more open to new ideas, thoughts and beliefs. Having an open mind has always been tolerated in the US, whereas in China the people have had much of their life dictated for them throughout history. China has also gone through periods of political and government instability, contributing to their preference of having predictability in their lives.

Individualism-collectivism has to do with the relationship between the individual and the group. In individualistic societies, each person looks out for themselves. In collectivist societies, people belong to a group from birth. This group may consist of family members, extended family and other extended relationships. Everyone in the group looks after each other and is loyal to the group. China has a low individualism ranking of 20 as compared to the average for other Asian countries of 24. This may have to do with China's communist ideals and the emphasis of working together in teams and cooperatives. The

United States has a very high individualism ranking of 90 (Hofstede, 2009). This probably stems from a culture in which personal achievements and success command respect. Also, American children are taught to be independent from a young age, a practice that is carried into adulthood (Jin, 1998).

Masculinity-femininity is how a society values masculine values, like achievement, aggressiveness or competitiveness. A feminine society is more nurturing, caring and modest. Masculinity-femininity also has to do with how gender roles are distributed in society. In feminine societies, men are caring and modest but not as much as women. In masculine societies, men's assertiveness and competitiveness rubs off on women and women are more assertive and competitive than women in feminine countries. The world average for masculinity-femininity is 50. China is ranked right at the world average, while the United States is given a ranking of 62 (Hofstede, 2009). The United States is a very competitive society in which people find honor in their victories. It is natural for the strong to prey on the weak. On the other hand, the Chinese do not believe in bullying to achieve results (Jin, 1998).

The final cultural dimension according to Hofstede is long-term orientation, which is how a society values perseverance, thrift and long-term rewards. Short-term oriented countries value tradition and fulfilling social obligations. China has a long-term orientation ranking of 118, its highest value among all the dimensions. Asian countries are characteristically long-term oriented, but China is well above the average for Asian countries. The United States is a short-term oriented country, with a ranking of 29. The world average is 45 (Hofstede, 2009).

The US and China differ the most on this dimension of culture. The Chinese people are known to have strong work ethic and discipline. Endurance, especially through tough circumstances, is admired. This trait probably has to do with China's Communist history. Mao Zedong's endurance during the Long March earned him respect among the Chinese people. It was after the Long March that Mao ascended to power and became the example for all Chinese people to follow (Graham, 2003). The Chinese are also known for being thrifty, a trait acquired after hundreds of years of political and economic instability. In fact, Chinese households save four times as much as American households (Graham, 2003). These factors contribute to China's high long-term orientation number. Americans think talent, not endurance, will bring success. Thrift is an idea lost to the average American as American citizens have billions of dollars in credit card debt. Americans think for the now and spend their money as such.

Some other cultural aspects in which the US and China differ are on humility, shame and tolerance of diversity. The Chinese view humility as a virtue but Americans think a person has every reason to be proud of their accomplishments and therefore think of humility as a weakness. Shame is remembered for a long time in China and people will go through great lengths to make sure previous shame is forgotten. Past shame is forgotten anyway by Americans because other concerns take precedent. Both cultures are open to diversity; however Americans are more open (Jin, 1998).

Each country's government's mentality also seems to be at polar opposites. China is a communist nation and the United States is a democracy. The Chinese government's goal is to serve the people and public ownership of property is advocated. The United States believes that social progress will happen through personal endeavors and successes of individuals. Private ownership is advocated. However, it seems as though the two governments are converging in their economic and legal practices. China is on its way from a planned economy to a market economy and from a "Rule by the Governor" to a "Rule by Law" legal system (Jin, 1998). The United States is already a market economy and rules by the law. This convergence to US economic and legal standards will perhaps bring the US and China's ideology, and perhaps culture, closer together.

The relationship between the United States and China is becoming increasingly important for each nation. Our economies are becoming increasingly intertwined making social and business ties necessary to maintain friendly relations. Though our cultures are very different, understanding each other's beliefs and practices will help to ensure future cooperation.

When doing business in China, there are several things that must be understood before initiating business activities. There is logistical information, like areas of investment, types of trading systems, types of businesses that can be established, financial institution regulations, labor standards, tax policies and security markets, which must be considered. Chinese business culture, from negotiation practices to the concept of *guanxi*, should also be studied. Understanding all of these aspects of Chinese business will help foreign businesses establish operations and relationships in the Middle Kingdom.

Since the late 1970's, the Chinese government has taken measures to open up China to foreign trade and investment with goals of growing the Chinese economy and improving the living standards of its people. After China's entry into the WTO in 2001, the Congress of the Communist Party of China adopted a "reform and opening up" policy (Doing Business in China, 2009). China has changed its laws to be in accordance with WTO regulations and has changed those laws to be more transparent and open. To encourage foreign investment and create an export-oriented economy, China will give certain industries favorable policies.

In April 2002, the government published a "Catalogue for the Guidance of Foreign Investment Industries," which states that the agriculture, infrastructure, export, high-tech and resource development industries will receive preferential treatment. This policy is meant to attract investment in these areas which the government considers key to China's economic development. This catalogue also states which industries a foreign investor is not allowed to enter at all and also which industries a foreigner can enter only if a Chinese citizen has a controlling share. At the same time, the government has issued an "Advantageous Industries Catalogue for Foreign Investment in Middle and Eastern Regions" which lists industries in other parts of the world in which Chinese citizens may invest in and receive preferential treatment. The Chinese government has also established five special trading zones (Hainan, Shenzhen, Shantou, Xiamen, and Zhuhai), 14 coastal cities and 52 high-tech development zones in which foreign investors will be able to utilize advanced infrastructures, land and a highly qualified workforce (Doing Business in China, 2008).

There are three types of trading systems that the Chinese use to encourage foreign investment and acquire necessary goods. Under the barter trading system, China agrees to import food, equipment or machinery in exchange for needed goods. With the processing and assembling trade system, Chinese factories carry out processing or assembling tasks for foreign companies. The materials imported and the final exported products are exempt from customs fees. The foreign company saves money by using cheap labor and the Chinese benefit from knowledge transfer. In order to bring in new technology, knowledge and equipment needed for government projects, the Chinese have established the compensation trading system. China will build a factory according to the specifications of a foreign company and stock the factory with labor and equipment needed to produce the final product. In return, the foreign company keeps all of the factory output and pays a processing fee to the Chinese government. The Chinese government will later take ownership of the equipment used in the factory. With the necessary equipment and a trained workforce, the Chinese can now produce the desired product (Doing Business in China, 2008).

Foreigners can only establish certain types of businesses in China. Foreign Invested Enterprises (FIEs) take the form of a wholly foreign owned subsidiary, equity joint venture, cooperative joint venture

and joint stock company. A wholly foreign owned subsidiary is a limited liability company set up entirely with the funds of that foreign company. The foreign company bears all gains and losses. An equity joint venture is a limited liability company in which the partners share management of the company as well as gains and losses. A cooperative joint venture is similar to a partnership, gains and losses are distributed according to a contract. A joint stock company is established with the sole purpose of listing stock on Chinese or foreign exchanges. It is funded by domestic and foreign shareholders. Foreign enterprises have business establishments in China or a significant part of their income comes from China and do not fall under the category of foreign investment enterprise. A company may also set up branches in China, but that company assumes all risks over its branches. So far only banks have been allowed to set up branches in China (Doing Business in China, 2008).

FIEs operating in China must keep accounting records and prepare financial statements. Journals, the general ledger and subsidiary ledgers are required. All must be written in Chinese and converted to the RMB. An FIE must hire a Chinese accounting firm to audit their records within five months of the year's end.

The People's Bank of China (PBOC) must approve any foreign financial institution before it decides to establish a base in China. Foreign financial institutions may set up branches, representative offices, subsidiaries or joint ventures in areas approved of by the PBOC. These institutions may only deal in foreign currency and must obtain special permission from the PBOC to deal in RMB. In order to deal in RMB and exchange their foreign currency into RMB a foreign financial institutions and businesses must apply for an Exchange Control Register within 30 days of receiving their business license. They must set up an account with a bank that is allowed to trade foreign currency. The business is now subject to audits and government control of the account. Once established, foreign financial institutions are under regulation of the PBOC. Other government agencies who may take a hand in regulating a foreign financial institution are the Ministry of Finance and the State Administration for Exchange Control. The Labor Contract Law of the People's Republic of China establishes employment regulations and rights for employers and employees in China. If a foreign company brings in expatriates to work for them in China, the expatriate must obtain a work permit. These are essentially the same work permits required for Chinese employees.

The work permit limits the expatriates to carry out activities related specifically to the business they have been hired in. Businesses are allowed to form three types of employment contracts: contracts with fixed terms, contracts with unfixed terms and contracts which terminate once a job is completed. Employers must contribute to social security and insurance funds for their employees according to rules set forth by the State Council (Doing Business in China, 2008). The number of payments that must be made by an employer vary by location. Employers must present a list of names of employees and relevant information about those employees, like their job titles, addresses and bank account numbers, to the local Social Insurance Agency. If an employer decides to amend, add or remove a company policy related to working hours, safety regulations, insurance benefits, employee training, etc., employees must be consulted either through labor unions or a meeting with all employees.

Businesses entering China will find themselves facing many taxes, like value added taxes (17%), business taxes (3%-20%) and consumption taxes (5%-45%). The corporate tax rate, which was set by the National People's Congress, established a 25% tax rate to both foreign and domestic enterprises. This rate is reduced to 20% for smaller companies or companies that are not very profitable. A reduced tax rate of 15% is applicable for high tech industries. The 15% rate will also apply to companies who hire the handicapped, invest in environmental protection or transfer technology to other industries (Doing Business in China, 2008). A foreign company who receives income on its dealings in China will be taxed based on the income earned. If a foreign company's main office is in China, they will be taxed based on

their worldwide income. If a company receives interest, dividends, rent or royalties from dealings in China but is not established in China, that company will be taxed 20% (Doing Business in China, 2008). China has two securities exchanges, the Shanghai Security Exchange and the Shenzhen Security Exchange. All listing and trading of the different categories of shares is done through these two exchanges. An Initial Public Offering can be made in two forms. "A shares" are RMB shares and are bought mainly by domestic investors. "B shares" are in foreign currencies and are bought mainly by foreign investors. Within the "B shares" category, an IPO can then take the form of an "H share" to be traded on the Hong Kong Security Exchange, an "N share" for the New York Stock Exchange, and an "S share" for the Singapore Security Exchange.

A typical Chinese business operates between 9:00 am and 6:00 pm. A five day business week is generally observed, though some businesses require their employees to come in for a half-day on Saturday or work a whole day every other Saturday (China Career Guide 2006). The office space is open with most people working at long tables, shared cubicles or individual cubicles. Only top executives have doors in their offices and doors are rarely closed. The boss-subordinate relationship is strictly observed. Subordinates obey their bosses and bosses show paternalistic concern for subordinates. The people with the highest position in the company will make all the decisions. Subordinates will not voice their own opinions unless the opinion of the boss is known. In meetings between peers, communication is open and sharing ideas is encouraged. If the meeting is formal, the purpose is to share an already made decision rather than to welcome feedback (China Career Guide, 2006). The time horizon for Chinese businesses is about 30 years, whereas in the US the time horizon is every quarter or three months (Jin, 1998).

Before conducting business in China, certain social aspects of Chinese society should be understood. *Guanxi*, or social connections, is necessary to succeed in China. In this complex web of connections, favors are given and returned. Intelligence, talent or wealth will not help you if you do not have the right connections (Chai, 2007). Family ties are the basis of *guanxi* because there is an obligation to help out family members. Those outside the family can be added to a *guanxi* network based on going to the same school, living in the same neighborhood, sharing the same experiences, having a common last name, etc (Flower, 2003). Chinese businesses do not like to deal with foreign companies unless they trust the foreign business. To establish trust, some sort of relationship has to be formed. A relationship can be established through meals, small gifts and favors. Do not expect to get results right away since *guanxi* can take a long time to develop. Establishing *guanxi* can be very beneficial for the long run. Having relationships with the right people can ensure your company gets up to date information and that paperwork is processed faster (Pedersen, 2006).

The concept of face is very important in the Chinese culture. Face is a person's dignity, pride and social standing. Losing face is being seen in a negative light in public. The idea of "saving face" is to maintain a person's appearance of dignity. This means making sure that potentially embarrassing information, like a drug addiction, diseases and abuse, are not found out by the public. Losing face is one of the worse things that can happen to a person and can be quite difficult to overcome, thus the Chinese go through great lengths to save face (Chai, 2007). If when conducting business in China, something happens to cause a Chinese company to lose face, the potential deal will be broken. At the same time, Americans can lose face if they get angry, frustrated or aggressive. This is also a deal breaker. If a Chinese person's actions cause something to go wrong, it is important to talk to that person in private about the matter instead of bringing it up in front of a group. This saves that person the embarrassment of everyone knowing about their mistake. When talking to that person, be passive about it and flatter them. According to May-lee and Winberg Chai, the best way to initiate dialogue would be to say, "A problem has occurred. I know this is not your fault, of course, but I know you will be able to think of a way to help solve this problem" (2007). If a Chinese person will not or does not want to answer a question, he or she

will laugh to cover embarrassment. This may be because the question is not understood or the Chinese person is uncertain about his or her position on the issue. If something is impossible, a Chinese person will say, "It is not convenient." To a westerner, this may sound like there is still a possibility that the request could be fulfilled, but to the Chinese it is a polite way of saying "No." Do not ask for reasons why a request cannot be performed because it is likely that the person will not feel comfortable explaining. If the Chinese person has had the opportunity to discuss the problem with others in private, he or she will bring the issue up again if it has been sorted out (Flower, 2003).

According to Michael Pedersen, China is considered one of the most corrupt countries in the world (2006). Bribery, kickbacks and large commissions occur at every level of government and business and are sometimes needed to get certain tasks accomplished in a timely manner or even to be accomplished at all. This can sometimes put American firms in a tough position due to the stipulations of Foreign Corrupt Policies Act (FCPA), which states that it is illegal to try to influence foreign officials through personal payments or political contributions. There are still ways to establish *guanxi*, ensure paperwork is processed and make business deals without violating the FCPA and falling into corrupt practices. The FCPA does not prohibit grease payments, or payments to low to middle level officials to ensure that they do what they were going to do anyway. Gifts can be given to overcome difficulties in the bureaucracy that may impede business. Gifts can also be considered gratuities to compensate for low wages. Corruption has been decreasing in China due to the influence of foreign companies and the return of Chinese citizens who have been educated abroad. Some have begun to see that bribes can only help in the short-term. It has also been found that when establishing *guanxi* the price of a gift is not as important as the gesture (Pederson, 2006).

It is important to understand that negotiation is different in China than it is in the west. Since the Chinese have great respect for their elders and value social status, western companies should send more senior members or the organization to do negotiating. Sending someone too young will tell the Chinese company that the western company is not serious. The first meeting is considered an opportunity for each side to get to know one another; no decisions will be made. Formal business wear, preferably suits, should be worn by both men and women. Punctuality is important in China. The Chinese will be on time so Westerners should show the same courtesy. A group of Chinese business people will enter the room according to seniority. Hands must be shaken with the most senior members first. One of the first things that will happen is the exchanging of business cards. Business cards should be accepted with both hands and carefully looked at, not just glanced at and stowed away.

It is a good idea for Westerners to bring a lot of business cards with them when going to China. Preferably, these cards should have Chinese translations on them. There will be lengthy presentations about each company during the first meeting. Foreign companies should have all information they give out translated in Chinese (China Career Guide, 2006). When giving a presentation to a Chinese audience, keep eye contact. People who avoid eye contact are considered untrustworthy. The use of jokes, though they may be common in the west, should be used sparingly if at all in a Chinese presentation. The Chinese have a long attention span and will not interrupt the speaker with questions. However, it is common for them to whisper to their associates, take phone calls, or for junior staff to pop into the room with messages during a presentation (Flower, 2008).

The negotiation process itself can be long and tedious. The Chinese value the process of negotiating more than the end result (Graham, 2003). When doing business in China, the relationship comes first and priorities are mixed between business, individual, political and nationalistic goals (Jin, 1998). Americans, who are accustomed to putting business first, must be ready for this. Lots of time will be spent establishing *guanxi* and building trust. This can lead to long nights of eating and drinking with

Chinese associates. It can take weeks, sometimes months before a Chinese company will feel comfortable dealing with a foreign company. This is because the Chinese view a contract as more personal. They have to trust the people they made the contract with and will keep to the terms of the contract to prevent losing face. On the other hand, Americans trust the contract and fulfill the terms of the contract to avoid legal trouble (Jin, 1998). There is no use for Americans to try to rush things unless they want to break a potential business deal.

The Chinese tend to think of things as a whole instead of broken down details. They will ask many questions, often out of order, and the same question may be asked more than once. This can be potentially frustrating to Westerners. The Chinese are more quiet and reserved compared to their outspoken western counterparts. The Chinese will deal in English and Westerners will find their conversational skills weaker than their writing and reading skills. The Chinese tend to prepare for business meetings with foreigners more extensively than foreigners prepare for meetings with Chinese associates. In situations where a Chinese person must answer a question on the spot without prior preparation, they will not be able to answer eloquently. If he or she is given time, an adequate answer to the question will be given at a later occasion (Jin, 1998). When dealing with business associates, the Chinese are more indirect and courteous with their answers.

Favors or occasions where either party loses face are remembered for a long time. On the other hand, Westerners are more direct and tend to remember conflicts that interfere with business (Jin, 1998). If the answer is “no” to a proposal, the Chinese will try their best not to directly say “no” because this is thought to be embarrassing to both parties. When it may seem like the Chinese are attempting to stall, they may be asking for more concessions on the other party’s part or they may be asking for “commissions.” It may be a good idea to bring a Chinese intermediary to help with the negotiation process. The intermediary can help establish *guanxi* and has the advantage of knowing the Chinese culture. He or she can not only speak Chinese but is also able to read subtle cues in body language or words that indicate whether the negotiations are going well or not (Graham, 2003).

The Chinese people’s emphasis on thrift and love of bargaining can turn into offers and counteroffers that seem ridiculous for Westerners. The best thing Westerners can do is play the negotiating game as well and ask questions about how the Chinese arrived at a certain price (Graham, 2003). The actual signing of a contract may be delayed until a significant or lucky date, further prolonging the process. It is important to keep up relations during the wait (China Career Guide, 2006). A long-term relationship is more important to the Chinese than a quick business deal. Even after the contract is signed, the Chinese may still ask for adjustments to the contract (Flower, 2003).

Understanding the world of Chinese business and Chinese business culture is essential before visiting the country for professional purposes. Using this knowledge can help western countries establish successful business deals and relationships valuable to both sides.

Summary

As the United States and China continue to be important trading partners, it is important for Americans to know what to expect before conducting business in China. Having a basic understanding of China will help prevent any embarrassment due to unexpected cultural obstacles and increase chances of business success. By studying the culture and business environment in China, we can not only increase our understanding of China, but also increase understanding of ourselves.

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