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Dependence and trust between suppliers and industrial customers

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# Dependence and trust between suppliers and industrial customers

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## Abstract

Suppliers have experienced unexpected consequences for their businesses due to changing situations for their important customers. Such events may also occur at short notice, at least when it comes to necessary and radical decisions. Often suppliers are not aware of the full extent of these events until it is too late for them to take countermeasures, i.e. develop appropriate strategies. With increasing turbulence in the marketplace, it is clear that firms need to be aware of relationship-oriented marketing strategies. To cope with change the supplier and its customer will need strategies based on jointly understood action. Action, both strategic and operational, is based on each party's meanings concerning why they do business with one another (enactment). Dependence and trust between the parties are issues in their construction of meaning and will therefore underlie their enactment. The purpose of this paper is to investigate dependence and trust between suppliers and industrial customers, implications for action of dependence and trust, and, finally, draw conclusions about dependence and trust for business strategy.

*Dependence.* A firm can be dependent on a specific other firm due to investments in specific assets geared to that firm. A literature survey identifies five types of specific assets: Personal relations, competence, integration of governance systems, dedicated volume of goods/services, and product/process specialization. Another reason for dependence is the structure of the market, which may lack alternative providers of similar products. Then it becomes difficult or impossible due to large switching costs to substitute one firm with another for the provision of good/services.

*Trust.* A literature survey concerning trust leads to the conclusion that important aspects of trust probably vary between different environments and settings where trust is an issue. Since trust between suppliers and industrial customers is the issue in this study, the notion and implications of trust among strategic decision-makers in that empirical setting would be important. By using the trust literature together with an empirical investigation three types of trust for the study are discerned: Relationship-based, competence-based and moral based trust.

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*Dependence and trust.* There is a temporal interplay between trust and dependence. Trust is expectation concerning the future. Dependence differs from trust by being formed in the present time and may therefore become a means to avoid the problems in assessing the future. But when you choose to trust someone, as a consequence you become dependent. Interrelationship between dependence and trust is thus complex and intertwined. It varies with task, situation and persons involved. The order of events in time has an impact. Earlier actions by actors influence later ones. Trust develops stepwise in repeated encounters between the parties. The parties' actions towards each other and the evolvement of action processes seem to be the key to understanding suppliers' and customers' dependence and trust. This interplay is in the paper illustrated with dependence and trust development in two dyads of supplier – industrial customer. In the cases we could discern that meaning construction with dependence and trust, interrelated with action, can lead to improved or deteriorated business relations between the parties. As in the cases patterns of virtuous circles or vicious circles may emerge. Expectations concerning the other party, i.e. trust, could thus change substantially, leading to different types of action than before.

*Conclusions concerning business strategy.* Dependence and trust have different impacts on a firm's strategy and consequently on strategic change. Dependence indicates preconditions for action and what action is precluded due to the characteristics of business between the parties in terms of specific assets and substitutability. In all, dependence sets limits for strategy, wide or narrow. Trust, on the other hand, can be a driving force shaping strategy, opening up possibilities in markets and products as well as governance systems linking parties. But lack of trust and deteriorating trust may also preclude business that could otherwise have been done. There needs to be trust backing up any viable strategy and strategic change. Furthermore, it is vital that the parties concerned convey in their communication what they consider to be meanings in their business. If they have dissimilar views on dependence, action may become disjointed and not understood by the other party. Likewise, openness concerning trust in one another is needed in order to display mutuality in trust or build mutual trust. On industry level trust in supplier relationships at firm level can be promoted by providing information exchange and arenas for that purpose to support potential business partners to embark upon trust development. Society, in its policy-making, can promote trust on firm level by clear-cut rules of the game, which – among other things – will reduce the risks that parties in an exchange will go to disjointed action due to different interpretations of what society requires from firms in business.

## **1 Introduction**

A variety of trends in society's economic life shapes the needs for change and development in business. Increased competition threatens the survival of some firms, or may at least create a depressed financial situation, while others can use their strong position and increase dominance. Competition coupled with recession affect some industry sectors, often creating drastic changes for that industry. Enhanced means of communication and logistical development alter the notion of what constitutes a market in a geographical sense. Novelties of technology may transform the market in its product sense.

These trends may cause changes for the industrial firms such as lost sales, bankruptcy, mergers, or internationalisation leading to restructured supply networks. Such events may also occur with short notice, at least when it comes to necessary and radical decisions. Suppliers

experience unexpected consequences for their businesses due to changing situations for their important industrial customers. Often suppliers are not aware of the full extent of these events until it is too late for them to take countermeasures, i.e. develop appropriate strategies to cope with their own need for change or survival. With increasing turbulence in the marketplace, it is clear that firms need to be aware of relationship-oriented marketing strategies (Sheth and Sharma, 1997).

In this paper, the supplying relationship is focused on long-term relationships between suppliers and industrial customers. Within the long-term relationship transactions occur repeatedly. The supplier's products and market may change over time. To cope with change the supplier and its customer will need strategies based on jointly understood action. Action, both strategic and operational, is based on each party's meanings concerning why they do business with one another (enactment). Dependence and trust between the parties are issues in their construction of meaning and will therefore underlie their enactment. The purpose of this paper is to investigate dependence and trust between suppliers and industrial customers, implications for action of dependence and trust, and, finally, draw conclusions about dependence and trust for business strategy.

The paper is based on a project containing three different parts. The first part was a survey study, in which 140 suppliers answered questions concerning innovation & technology, leadership & planning, supplier & quality, customer focus, employee development and information & benchmarking (Sundqvist, 2002). Results show that the firms scored low in innovation & technology and information & benchmarking. These results were supported by similar results in two parallel studies in two other Swedish regions. Parallel studies have also been performed in New Zealand showing that manufacturing firms in that country fared better in information & benchmarking than their Swedish counterparts (Sanner, 2003), while the Swedish firms scored markedly better in leadership & planning, customer focus, and quality & supplier focus. The second part was an in-depth study of some of the 40 suppliers with more than 50% of their sales going to one or two customers. These firms showed themselves to be less active concerning innovation and new product development, study their markets and competitors less and lacked to a certain extent important engineering competence. The third part of the project is the in-depth study of suppliers – dependence, trust and business strategy.

## **2 Dependence**

A now classical article "Power – Dependence Relations" (Emerson, 1962), showed how someone's relation to different elements in the environment can be analysed in terms of dependence and power. Social relations between actors, where an actor can be either a person or a group, commonly entail ties of mutual dependence between the parties. A is dependent upon B if he aspires to goals or gratifications whose achievement is facilitated by appropriate actions on B's part. Actors experience their dependence situations as contingent on motivation and alternative means for goal achievements: "The dependence of actor A upon actor B is 1/ directly proportional to A's motivational investment in goals mediated by B, and 2/ inversely proportional to the availability of those goals to A outside the A-B relation." (Pfeffer and Salancik, 1978), and see dependence as the product of the importance of a given output to the organisation and the extent to which it is controlled by a relatively few organisations.

Interdependence or mutual dependence means that two persons or organisations are dependent on one another (Thompson, 1967; McCann and Galbraith, 1981; Ring and van de Ven, 1992). Thompson (1967) sees mutual dependence as reciprocal, typical for situations where outputs from organisation A become input in B and, at the same time, outputs from B become input in A. Thus the organisations are not only dependent but may also influence each other's actions. Marketing channel literature takes the theoretical perspective that marketing channels are best viewed as interorganisational systems, and researchers have observed that reciprocal dependence is important to the understanding of channel interaction (El Ansary and Stern, 1972; Anderson and Weitz, 1989; Anderson and Narus, 1990; Buchanan, 1992; Gundlach and Cadotte, 1994). Transaction cost analysis is based on Williamson's view that economic activity is more efficient when conducted either within a single organisation or in a hierarchy rather than in the market (Williamson, 1975; Williamson, 1985). Nevertheless, in later years researchers have extended and modified transaction cost analysis to include bilateral dependence on the market (Johanson and Mattson, 1987; Heide and John, 1988; Heide, 1994; Noorderhaven et al., 1998; Joshi and Stump, 1999; Buvik and Grønhaug, 2000).

Interdependence does not necessarily mean that both parties are dependent on one another for the same reason or to the same extent. Asymmetry is a common theme in the literature (Williamson, 1985; Heide and John, 1988; Buchanan, 1992; Gundlach and Cadotte, 1994; Kumar et al., 1995; Joshi, 1998). Dependence can be balanced or unbalanced (Emerson, 1962; Jacobs, 1974; Pfeffer and Salancik, 1978). In the latter situation one party dominates the relation. The literature often contends that the firm should avoid depending on trade partners, but there are also studies indicating that dependence can bring the firm benefits (Lusch and Brown, 1996). Interdependence and asymmetric relations between suppliers and their buyers have been investigated (Friedman, 1977; Rainnie, 1989; Robinson, 1989; Blackburn, 1992; Morris and Imrie, 1992; Raffa, 1992; Gadde and Håkansson, 1993; Lamming, 1993; Lyons and Bailey, 1993; Curran and Blackburn, 1994; Lusch and Brown, 1996; Lilliecreutz, 1998; Noorderhaven et al., 1998).

What constitutes dependence? A firm can be dependent on a specific other firm due to investments in specific assets geared to that firm. When a firm makes a specialized investment in its partner, transaction-specific assets will exist (Williamson, 1985). It will be dependent on another firm through assets specifically geared towards the exchange partner, assets which can not at all or only by incurring large switching costs be used for other exchange partners. We can identify five types of specific assets: Personal relations, competence, integration of governance systems, dedicated volume of goods/services, and product/process specialization. Another reason for dependence is the structure of the market, which may lack alternative providers of similar products. Then it becomes impossible or difficult due to large switching costs to substitute one firm with another for the provision of good/services.

### ***Asset specificity***

There is a debate among researchers whether relations between organisations are characterised by discrete transactions implying limited communication and narrow content or by relational exchange (Ring and van de Ven, 1992). *Relational exchange* means that each transaction must be viewed in terms of its history and anticipated future. In relational exchange the participants can be expected to engage more in social exchange and norms are based on the expectation of mutuality of interest, essentially prescribing stewardship behaviour, and are designed to enhance the well-being of the relationship as a whole

(Macneil, 1980). The actors invest more in joint activities and resources and in long-term commitment (Johanson and Mattson, 1987). The duration of a relationship is likely to affect the parties' expectations that the relationship will continue (Ganesan, 1994; Berger et al., 1995). The parties adapt to one another in order to support and possibly expand current business. Adaption has an impact on dependence (Dwyer et al., 1987; Hallén et al., 1991). Relational flexibility, information exchange and solidarity between the parties affect dependence (Joshi and Stump, 1999).

Need for the *exchange partner's competence* may create dependence of one firm on another (Håkansson, 1989; Robinson, 1989; Lamming, 1993; Gadde and Håkansson, 2001). It may also include the exchange partner's knowledge upstream, such as the market for raw material, or downstream, e.g. marketing policy for the ultimate consumer market (El Ansary and Stern, 1972).

Efficiency in the flow of goods/services between suppliers and customers may entail integration in systems for order, delivery and payment (Robinson, 1989). By IT-systems such as Just-in-time delivery and Electronic Data Interchange (EDI), as well as specific logistics solutions, parties adjust their administration to each other forming interdependent *governance systems* (Ragatz et al., 1997; Gadde and Håkansson, 2001). Business with one party becomes facilitated more in a relative sense as compared to parties where no joint governance system is applied (Raffa, 1992; Lilliecreutz, 1998). A high degree of vertical integration is partnerships with selected suppliers, with whom joint systems will be developed and become specific assets. This will increase dependence (Heide and John, 1990). Ownership is the ultimate form of control.

If a high *relative volume of goods/services* provided by a firm is dedicated to one party there is resource dependence (Pfeffer and Salancik, 1978; Buvik and Grønhaug, 2000). The volume may also be essential as a contribution to profit (El Ansary and Stern, 1972) and constitutes a large market share (Hallén et al., 1991). The same logic that relative volume makes relative dependence applies to both selling and buying (Gadde and Håkansson, 1993).

Apart from dedicated volume, a focal firm can also be dedicated to another party by *specialization of its goods/services* (Raffa, 1992; Lyons and Bailey, 1993), i.e. there are, due to specialization, fewer alternative buyer/sellers available for that product. The notion of role performance indicates that the one party lives up to the needs of the other party by specialization (Heide and John, 1988). The focal firm's investment in specialized production and processes geared to the needs of a specific firm may create dependence also in the future. Specialization entails dependence when the specialized product would bring large switching costs to sell to or buy from another party (Williamson, 1985; Anderson and Weitz, 1992).

### ***Substitutability***

Dependence is increased when the market has fewer or no potential alternative sources of supplier or customer (El Ansary and Stern, 1972; Pfeffer and Salancik, 1978; Heide and John, 1988). The structure of the market is such that it may be impossible to *substitute one exchange partner for another* (Jacobs, 1974).

## **3 Trust**

Trust as a more or less prominent issue has been increasingly studied by e.g. psychologists, sociologists, economists, management and marketing theorists and in philosophy (Barber, 1983; Hosmer, 1995). There appears to be a widespread agreement on the importance of trust. But as a multifaceted phenomenon lacking agreement on fundamental definitions it lends itself to being grasped and summarised by different views on it.

There are preconditions for trust to emerge in a social setting (Parsons, 1969). All participants must believe that action is aimed at common values. In a business setting, common values like the belief in the market system and professional behaviour as a businessman (“businessmanship”) would be important. These common values must then be possible to translate and convey to common goals. Profitability, survival and development of the firms would be such goals. Parsons (1969) also contends that each participant’s expectations must generally fit into his or her general set of solidarity involvement. In a business context this could be exemplified by joint interests in development of the technology of the actors’ specific industry or survival of business in the area where they are located. Finally there is an issue of role fulfilment: The participants should see each other as belonging to the same or an expected social setting, i.e. “be one of us”. In sum, there is a need for the parties in a trusting situation to relate the persons or the organisations to one another. This could be attained by knowledge of each other, experiences together in the past and maybe also some feeling of affinity.

Two main views of trust can be found in the literature: The first view is trust as the chosen expectation of One that Other will do something in the future that will favour One (see e.g. Luhmann, 1979; Barber, 1983) or at least not put One in a detrimental situation. The second view is based on One’s confidence in Other’s goodwill, i.e. Other’s moral integrity. This article contends that these two views converge in any social activity concerning trust. When One expects Other to act in One’s favour, this expectation will have no meaning if One at the same time does not have confidence in Other’s goodwill. You simply would not have expectations of a person whose moral integrity you do not believe in – unless you have no choice but to put your destiny in somebody else’s hands. You choose to expect, otherwise it is not a matter of trust (Dasgupta, 1988). Furthermore, confidence in goodwill is a state of mind, which becomes important in social action only by connection to expectation. You can have confidence in a person or organisation in your mind, but this will have social consequences only when you enter into some activity involving that person or organisation (Gambetta, 1988). At that moment expectation also becomes an issue.

This paper also contends that a complex phenomenon like trust will never be universally defined, i.e. will never be characterized by one definition that can be used for any theoretical purpose. Definitions have to be elaborated due to specific research issues and study aims, in which different aspects of trust become important: Vulnerability, dependence and commitment are examples of such aspects. In this vein, the wide variety of definitions of trust or its aspects that are used in different studies can be explained. Some examples: Process trust, characteristics trust and institutional trust (Zucker, 1986); economic trust (Larson, 1992); contractual trust, good will trust (Sako and Helper, 1998); personal trust (Luhmann, 1979); system trust (Giddens, 1990); competence trust (Barber, 1983); cognitive trust, emotional trust, behavioural trust (Lewis and Weigert, 1985); information, influence and control conceptualised trust (Zand, 1972); enterprise-based trust (Sanner, 1997); interfirm trust (Gulati, 1995); intentional trust (Nooteboom et al., 1997); calculated trust (Anderson and Narus, 1990); and commitment trust (Tillmar, 2002).



Aspects of trust probably vary between different environments and settings where trust is an issue. Since trust between suppliers and industrial customers is the issue in this study, the notion and implications of trust among strategic decision-makers in that empirical setting would be important. Therefore, in order to compare and verify trust with the trust literature, interviews were made with four CEOs in supplier companies and one director of a customer company's Purchase department. The question to be answered and elaborated was: What is trust between a supplier and an industrial customer? In the Appendix to this paper 49 statements from the respondents are noted.

The statements concern a wide array of opinions, experiences, hopes and fears concerning trust. However, they can be grouped into three strands: Relations, competence and morals.

Firstly, the respondents indicated as important for trust: Respect for each other, a working dialogue – also when problems arise, flexibility and adaptability before the other party, willingness to solve problems and take corrective action, willingness to give help when needed, display understanding, “personal chemistry” between the persons in charge of contacts, i.e. *relation-based trust*.

Secondly, to promote trust they also indicated professionalism in running the business, efficient management, quality in products and processes, timeliness in delivery and payment, work in accordance with stated or agreed requirements, i.e. *competence-based trust*.

Thirdly, a number of statements concerned general ethics and morals: honesty, fairness, keeping promises, honouring agreements, standing by one's word, reciprocity and mutuality in situations where you should yourself live up to what you demand from others, “stick to the rules of the game”, to have businessmanship as a basic value when doing business. This can be labelled *moral-based trust*.

The three strands are partly overlapping, but give a broad picture of the meaning of trust in the empirical environment of the study. As can be seen above the meaning of trust does not differ from what could be found in the literature, it is only more focussed.<sup>1</sup> The three notions of relation-based trust, competence-based trust and moral-based trust will be used in this study.

#### **4 How dependence and trust interplay**

Any social situation with trust implies expectation. Expectation is laden with some uncertainty about whether it will be honoured or not. Expectations not fulfilled will put the truster worse off than if they are fulfilled. The penalty (disutility) One suffers if Other abuses One's expectation may be greater than the benefit (utility) One gains if Other does not abuse that expectation (Deutsch, 1962). Hence the truster will expose himself and become dependent on the trustee (Dwyer et al., 1987).

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<sup>1</sup> Close in meaning to relation-based trust come process-based (Zucker, 1986) personal trust (Luhmann, 1979) and behavioural trust (Lewis & Weigert, 1985). Competence-based trust has a similar notion, competence trust (Barber, 1983). Zucker's (1986) notion of institutional based trust as well as Barber's (1983) and Parsons' discussions concerning the role of the professional contain what is here denoted as moral-based trust.

Seen in a time perspective One forms expectations and enters into dependence with Other at one point of time and experiences expectations as fulfilled or not due to Other's behaviour at a later point of time. There is a temporal interplay between trust and dependence. "Trust concerns the future, as a complexity reduction involving a problematic relationship with time..." "It is to behave as though the future were certain" (Luhmann, 1979). Dependence differs from trust by being formed in the present time and may therefore become a means to avoid the problems in assessing the future. One offers Other dependence in confidence that Other will not abuse One's dependence (Nooteboom et al., 1997). Trust will be the conscious regulation of One's dependence on Other that will vary with the task, the situation and the other person (Deutsch, 1962).

There are two causes for dependence. One cause is dependence that mirrors power (Emerson, 1962). The scope and character of this dependence is determined by the power holder. It is involuntary and enforced upon the dependent. Dependence based on power may exist without any trust. The second cause for dependence is trust. (Heide and John, 1988). You choose to trust someone and as a consequence you become dependent (Luhmann, 1979; Dasgupta, 1988). You enter into this dependence because you deem some expectation of something to be important. If dependence were too cumbersome, you would hesitate to trust. Therefore, you can determine whether or not to enter into this voluntary form of dependence, and have an influence on its scope and character.

As discussed above, dependence can be symmetric or asymmetric between the parties. Reciprocal dependence may thus be a balanced or unbalanced. This has implications for trust between the parties. The issue has been studied. Dependence imbalances are of relatively minor importance if trust is developed. If the less dependent trusts the more dependent, both parties want mutual trust to remain and the less dependent will not use his superiority (Kumar et al., 1995; Geyskens et al., 1996). The issue deserves more studies since there is also opposite evidence that dependence asymmetry affects trust in a negative way (Anderson and Weitz, 1989).

Asset specificity would normally be interrelated with trust. Whether it is based on investments in personal relations, dependence on the exchange partner's competence, joint governance systems, high relative volume of goods/services exchanged or specialization towards the exchange partner, these investments would not have been made without trust between the parties (Johanson and Mattson, 1987; Heide and John, 1988; Gadde and Håkansson, 2001).

Interrelationship between dependence and trust is complex and intertwined. It varies with task, situation and persons involved. The order of events in time has an impact. Earlier events by actors influence later ones (Anderson and Narus, 1990; Hallén et al., 1991; Gundlach and Cadotte, 1994; Geyskens et al., 1996). Trust develops stepwise in repeated encounters between the parties (Luhmann, 1979; Dasgupta, 1988). The parties' action towards each other and the evolution of action processes seem to be the key to understanding suppliers' and customers' dependence and trust (Zand, 1972; Dwyer et al., 1987; Larson, 1992; Ring and van de Ven, 1994).

## **5 Enacting dependence and trust**

Enacting refers to people's concern with making sense of events and experience as a condition for entering into action. It is a process where they attempt to construct meaningful

explanations for situations as a basis to decide to act, what action to take or not to act at all. People engage in ascribing or imposing meaning upon experience including their own actions and use the imposed meaning as a basis for subsequent understanding and action. Thus meaning construction and action become intertwined (Weick, 1979). Meaning construction and action is not a sequential process in the way of one first and then the other. Enacting will be personal in that people use intuition, imagination, vision, revelatory flashes of insight, and creative problem solving in the construction and use of meaning (Gioia, 1986) Enacting will also be contingent upon personal experience, professional competence and abilities. At the same time, human thinking and social functioning are essential aspects of one another in enacting (Weick, 1995).

Enactment concerns outcomes lying ahead and action to come. The future is equivocal, though. Businesspeople need to reduce the abundance of information by meaning in order to act (Gartner et al., 1992). But there can be many possible meanings for a person in one situation and a multitude of clues for information seeking. Clues are often sought in the past. We therefore often attend to new situations as if they were earlier experienced situations, retrospective sensemaking (Weick, 1979; Weick, 1995) The idea of retrospective sensemaking derives from Schütz’s analysis of “the meaning of lived experience” (Schutz, 1967). The past is singled out to guide the present and the future. Retrospectiveness resides in the basic values and beliefs of a person and experience stored in the memory as interpretative schemes.

The framework can be depicted as follows (Fig. 1).

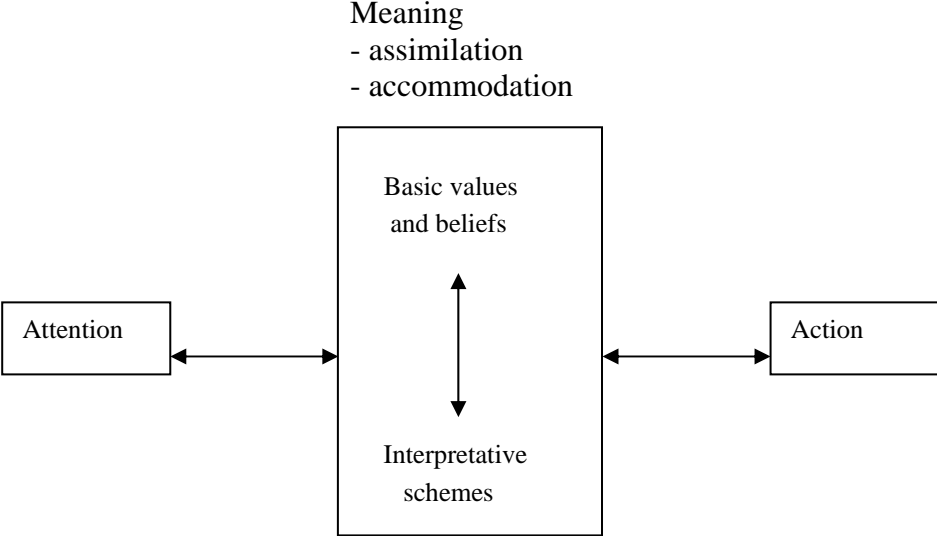


Figure 1. Enactment

Attention, clue seeking and selection of information

The environment brings the individual information for enacting. For any specific situation, where the individual perceives a need or a potential need to act, the entire datum of information tends to be abundant. There is a problem concerning what information to attend to. So the individual needs guidance regarding what information to distinguish for further attention and use, i.e. to reduce complexity (Luhmann, 1979). Now an interplay starts between attention to information and creation of meaning. In the selection of information clues are needed. Clues work as reference points in the large and complicated quantity of

information (Weick, 1979). A meaning attributed at the start of the process can change and develop as a result of the clues selected and applied to information selection. The individual can in an active role through meaning development produce change in her/his environment due to information selected. Attention, clue seeking and selection of information is to a greater or lesser extent done by the individual in conjunction with others.

### Basic values and beliefs

Basic values and beliefs pervade the individual's assumptions about the nature of the world, the role their organisation will play in society, the nature of human beings, truth, relationships, time and space (Schein, 1983). Basic values, even when the bearer is less conscious of them, are expressed in beliefs, assumptions and ideas. Beliefs as rooted in basic values are also stable over time but nevertheless more influenced by meaning construction and reconstruction and may therefore change and develop more than basic values. Attention and action performed may reconstruct meaning and, by that, change beliefs. Conscious or not conscious basic values and beliefs will form and activate the individual's construction of meaning (Weick, 1995). Through meaning they also have an impact on attention and action.

### Interpretative schemes

People develop ways of economising on information and lessening the task of handling the myriad of potentially meaningful clues for action available (Gioia, 1986). This choice problem is difficult and laborious, so they need to simplify. From earlier occasions they use experience that has been stored in memory and brought forward again. Structured, pre-existing knowledge is used to interpret the situation and generate appropriate action. The notions of interpretative scheme and scheme will be used as synonyms denoting structured sets of pre-existing views, and patterns of events/actions that can contribute to meaning and action.

### Assimilation and accommodation of experiences

Meaning construction and understanding involves association of experience with existing interpretative schemes, and alteration by incorporating new interpretative schemes. To handle that, the literature (Gioia, 1986) sometimes uses the notion of "Piagetian framework", in which *assimilation* denotes the incorporation of experience into existing schemes (integration) and *accommodation* refers to construction or alteration of schemes in the face of experience (creation). These processes are either intentional, and therefore under the person's control, or automatic, not conscious.

### Dependence and trust as constructed meaning

The broad overviews in sections 2-4 above indicate dependence and trust to be important in the supplier's and industrial customer's enactment of business. Each of the parties involved uses his interpretative schemes about the other in terms of dependence. How is our relationship? Do we need the other party's competence for our business? Possible joint governance systems are interpreted, just like dependence on volumes and specialization. Could there be reasons for substitutes, an alternative provider/customer? The aspects of dependence reside in values, norms and beliefs, memories from earlier enactments between the parties as well as attention to recent information at hand and clue seeking. Enactment then includes the analogous constructed meaning from the other party, relative dependence

(Emerson, 1962; Kumar et al., 1995; Noorderhaven et al., 1998). Enactment will include both separate and joint action (maybe also joint assessment on dependence in an open atmosphere).

Likewise, a truster gives attention to information in which expectation concerning the trustee is worked upon, clues are bracketed and elaborated in a construction of meaning. Basic values and beliefs concerning trust as well as trust from earlier occasions (Anderson and Narus, 1990) residing in interpretative schemes will be interpreted and brought to the meaning construction. Expectations as constructed meanings concerning a trustee will be an element in action formed and entered upon (Dwyer et al., 1987). Experience concerning trust in the action performed will be worked upon and assimilated or perhaps accommodated into schemes (Zucker, 1986).

#### Action processes

Several enactments over time form action processes. The successive enactments will be contingent on earlier meanings as well as attention to information on a specific occasion. By assimilation and/or accommodation interpretative schemes are used repeatedly and may change in the process. Basic values tend to be stable over time, beliefs may change slowly. Action follows, and will as experience become part of the interpretative scheme. An action process can thus be seen as a chain of interrelated enactments.

### **6 Dependence and trust in two dyads – an illustration**

To illustrate dependence and trust enacted in an action process two dyads will be presented: Two suppliers each in a dyad with an industrial customer.

The industrial customer will be labelled Machinery Inc, a manufacturing company. Machinery dominates a rather small town in the middle of Sweden. It was started in 1904 and has since the 1910's been multinational, nowadays with plants and subsidiaries in more than 40 countries. In its specific manufacturing field, Machinery holds 70 % of the world market. Annual turnover for the whole group worldwide is 8134 Sw. Mkr in 2002, and for Machinery's activities in the small town 380 Sw. Mkr. Nevertheless, the company has been in a difficult financial situation during the last five years and has made efforts to reduce costs in several ways. One way is outsourcing such activities that are not defined as core activities.

The supplier Techno Inc. is a company based on metal cutting and was originally outsourced from Machinery in 1994. Two years later Techno bought outsourced production from another company. Today Techno is sister company in a family-owned group of two firms in the same niche. The basis for Techno was a mechanical engineering shop, which still is on Machinery's premises, and 34 employees, which has now increased to 60. Turnover is 50 Sw mkr. 25-50 % of its turnover is sales to C as compared to almost 100 % in the beginning. In all, 80% goes to large Swedish multinationals. A goal is to increase turnover to small and new customers, while still keeping the volume of sales to the large buyers. Techno also aims at producing more downstream, i.e. doing more construction work and assembly for its customers.

The supplier Electro Inc. is a company in cabling, mechatronics and electronics, situated 160 km from Machinery. Electro is family owned and has existed since 1982. When Machinery in 1998 decided to outsource this part of the production, Electro took over machinery, stocks and 15 employees to form a department in Electro. This department was still situated in

Machinery's town and on Machinery's premises. Some new equipment was bought. Beta planned to get new customers for this manufacturing niche. But things went wrong. Cooperation between Machinery and Electro was hampered by malfunctioning procedures of order and delivery. Several attempts to improve routines failed. Relations between the management of the two companies became strained. Finally, both parties agreed on breaking the agreement. Today they have no business in common. Two other firms have taken over the outsourced activities.

Descriptions and analyses of business in the two dyads are based on interviews with the managing director and the director of the purchase department in the relevant part of Machinery, the managing directors of two suppliers Techno and Electro and studied documents were studied from the three companies.

### ***Dependence and trust in the action process with Techno – Machinery***

At the start, as a supplier, Techno was very dependent on Machinery. Techno took over the staff from Machinery. As a consequence there were tight relationships, so tight that the staff at the company even had problems seeing themselves working in another company. There were also very tight connections in ordering and delivery, partly since the companies were located in the same area. In the beginning nearly 100 % of the orders to Techno came from Machinery. Mutual dependence was very high, since also Machinery looked upon the new company as its former department. The situation has changed throughout the years, though. A new CEO at Techno, coming from another company intensified marketing to new potential customers. Successively, the turnover expanded by sales to new customers. Machinery's orders now account for 30 % of Techno's turnover. Both companies express satisfaction that Techno's dependence has decreased. Machinery sees the advantage of Techno learning from other customers and also that also other firms share in contributing to Techno's overhead costs. The purchasing director of Machinery expressed it:

“They were very clever to quickly get new customers and saw us as a starting aid. We have now a win-win situation with Techno. They invest in machinery and equipment in a way that we believe in increasing quality in their products. We need very little discussion with this supplier”.

And in the words of Techno's CEO:

“I think we have brought down dependence on them to a good level today. It works well. We have a good business relationship and therefore we co-operate in natural way and we pull in the same direction.”

Machinery expresses trust in Techno by the way the supplier has handled its expansion on the market and its willingness to invest for that purpose (competence-based trust). Techno, in turn, has high relation-based trust in Machinery, shown by the way they handle negotiations: They both care for the continuous relationship between the firms. In some other customer relations Techno meets customers that are only using discussions to press down prices. Techno's CEO expresses moral based and relation based trust:

“Machinery is an honest firm. It is a matter of values. They are prepared to take and give in an open way. And we respond by giving them help in different ways now when they have some problems ”

The firms thus started out with similar basic values and beliefs in their roles in business. Interpretative schemes were similar, since backgrounds were similar. Techno went into action that accommodated less dependence and more trust in its counterpart's interpretative schemes.

Machinery, in its turn, displayed in many ways trust towards Techno and backed up the joint aims of a wider market for the outsourced company, which brought self-assurance to Techno (accommodation).

The development by enactments in the action process has been facilitated by the tight contacts between the employees of the firms. Interaction is daily in large or small transactions. So altogether: There is much attention to information between the parties. Aided by similar values, beliefs and interpretative schemes accommodating trust and a mutually beneficial level of dependence, they see their interaction as having meaning. Then action runs smoothly between the parties, facilitating their business.

### *Dependence and trust in the action process with Electro – Machinery*

When Electro bought the business in one of Machinery's departments and integrated it with Electro, it also took over resources from Machinery (people, equipment, building). The former department continued to operate as earlier, since no additional customer came into play. Dependence was high due to close relations and a high relative volume of products purchased. In addition, Machinery's governance system prevailed: procedures for ordering, production planning etc. Specialization in products towards Machinery was very marked. The new management in Electro made some investments and planned to expand its market. But problems arose in its relations to Machinery. Electro wanted to change the governance system towards Electro's own. Machinery did not comply with these changes. External consultants were engaged to work out solutions, but the two managements did not agree on solutions to all the stated problems. Electro demanded economic compensation for their more expensive production. Part of the dispute was settled. Then suddenly Machinery quickly cut the orders to Electro by 50 %. Electro cancelled all agreements with one month's notice. For some of the disputes lawyers were hired and the dissension was brought to court. The branch of Electro in the town of Machinery closed down. The rest of Electro – in another town – is prosperous.

The parties planned to reduce dependence over time together. Since no expansion of Electro's market came and settling the disagreement failed, dependence did not change. Trust was high on both sides from the beginning, but process-based trust and competence-based trust deteriorated quickly. Electro's CEO:

“We worked hard for them in the beginning. We believed in Machinery. But they took too long to decide on rather small matters, sometimes half a year. Promises were broken. They would stick to anything they had done for 30 years. Gradually we lost confidence in them. If we had continued with them, we would have been broke today, the whole company.”

The comment of Machinery's purchasing director:

“Electro did not succeed in getting any synergy out of the cooperation. Only the manager was new. They continued to work as a department within Machinery. No positive effects, only worse and worse. So we had to break off doing business with them. Now we let their successors as suppliers come in to have influence on the construction of our products.”

Communication between Electro and the purchase officer in Machinery was good, but management turnover in Machinery made it difficult to develop good relations with its managers. Deteriorated trust (or development of a process of distrust; cf Luhmann, 1979) could not be compensated for by existing high dependence.

The two firms did not discuss enough what they expected in the agreement with the other party. Electro's CEO:

“We should have had much more accurate documentation from the beginning. And we should have listened much more to the other party's way of thinking. We were two parties who believed we agreed. But we were thinking along two quite different lines.”

Basic values and beliefs were not congruent between the parties. In the process they also displayed different views on how procedures should work and how to cooperate in an efficient manner, i.e. they had different interpretative schemes. When basic values and beliefs differ, it is probably difficult to accommodate experience from action into schemes to make them more alike as a basis for improved jointly understood action. Instead, in this case, due to the differences, accommodation constructed more distance in meaning concerning trust between the parties. Attention to information and clues to the needs of action was disturbed. So the parties could not understand each other's actions, and action became disjointed. Mutual dependence still was at hand, and there was a need for co-operation, but the need could not be fulfilled due to lack of trust, which led to the situation becoming untenable and subsequently running into a clash.

### ***Patterns of enactment: Virtuous and vicious circles in the cases.***

In the two cases we have seen that a chain of meaning construction with dependence and trust interrelated with action can lead to improved or deteriorated business relations between the parties. As in these cases patterns of virtuous circles or vicious circles may emerge (Merton, 1968). Attention to information concerning dependence and trust may have an impact on meanings in the minds of each party. Similar or dissimilar meanings between the parties affect action taken. Action may be jointly understood or the other party's action may not be understood. In either case enactment will become retrospective in that it brings assimilation or accommodation of meaning to existent interpretative schemes. Thus enactment has an impact on further action. In the cases we could discern that expectations concerning the other party, i.e. trust, could change substantially, leading to different types of action than before.

## **7 Conclusions concerning dependence and trust in business strategy**

As discussed above (section 4) dependence is formed in the present time, while trust concerns expectation for the future. So meanings of dependence and meanings of trust have different impacts on a firm's strategy<sup>2</sup>.

Dependence indicates preconditions for action and what action is precluded due to the characteristics of business between the parties in terms of relational exchange, the parties' competence needs, interrelated governance systems, relative volume of goods and services, specialization and substitutability. Given possible action in the present, dependence can be a means to avoid future problems. In all, dependence sets limits for strategy, wide or narrow. If a supplier wants to change its strategy towards an industrial customer – and vice versa – it may need to back up the change by altering the basic relationships in terms of dependence. However, some strategic changes may then be out of reach.

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<sup>2</sup> Strategy is a notion covering contents (goals, ways to reach goals) and processes (future-oriented thinking, planning, learning)



Trust has been called “an important lubricant in any economic system” (Arrow, 1974), which implies trust as a facilitator for business. Trust, based on relations, competence and morals, can be a driving force shaping strategy, opening up possibilities in markets and products as well as governance systems linking parties. Trust can be an important ingredient in a positive development of relations, forming e.g. virtuous circles. But lack of trust and deteriorating trust may also preclude business that could otherwise have been done. There needs to be trust backing up any viable strategy and strategic change.

It is vital that the parties concerned convey in their communication what they consider to be meanings in their business. If they have dissimilar views on dependence symmetry or asymmetry, action may become disjointed and not understood by the other party<sup>3</sup>. Likewise, openness concerning trust in one another is needed in order to display mutuality in trust or build mutual trust.

As discussed above in this paper (Section 1) suppliers experience unexpected consequences for their businesses due to changing situations for their important industrial customers. Often suppliers are not aware of the full extent of these events until it is too late for them to cope with the consequences. But in a relationship characterized by information and trust, signs of coming events and situations can be discovered earlier. This may in its turn facilitate countermeasures, e.g. developing appropriate strategies to cope with the supplier’s own need for change or survival (jointly understood action).

This study has specifically studied trust in one type of changing situation: Outsourcing. Dependence is an important aspect of the outsourcing situation. There are other situations characterised by change, where trust is an issue in making strategies possible or not: Fusions between companies entail a need for amalgamation of values, traditions (interpretative schemes), ways of governance and action. In the restructuring of an industrial customer’s supplier networks, trust is probably important and may determine the changes. Expansion by e.g. internationalisation and other changes deserve further studies, as well as the opposite situation, downsizing. This study has been performed as an ex post study since the processes were well under way enabling each party’ reflections over the process. Another way could be simultaneous process studies, which may bring interesting perspectives on action going on.

So far we have discussed implication between firms, on firm level. What can be done on industry level to promote business action processes on firm level? The role in this sense is to promote communication and provide meeting arenas. Information exchange and arenas for that purpose are needed to support potential business partners embarking upon trust development.

On regional level, actors, roles and forms of cooperation vary between countries as well as between regions inside a country. In the interviews in this study, respondents have pointed at the role of trust between actors in the region as well as locally. Structures such as supplier networks (a virtual firm structure where suppliers cooperate in making offers and production), supplier parks (cooperation and organising between industrial customers, suppliers and other resource providers in an area) all have trust as a basis for initiatives as well as performance.

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<sup>3</sup> Both symmetric and asymmetric dependence can be fruitful. The important thing is that the parties agree on their interpretation of dependence.

Experiences from trust development in such structures and from their forming processes can be interesting to study to benefit new cooperative initiatives.

What can be done by society on a national level to promote business action processes on firm level? Partly the role must be the same as on industry level: Information exchange and arenas for that purpose. But since society's role is policy-making, including norm setting and norm interpretation (laws and regulations), trust on firm level will be promoted by clear-cut rules of the game, which – among other things – will reduce the risks that parties in an exchange will go to disjointed action due to different interpretations of what society requires from firms in business. As shown by (Lane and Bachmann, 1996), trust-based relations between buyer and supplier firms in Britain and Germany are highly dependent on the existence of stable legal, political and social institutions. The issue deserves more comparative studies in different countries to cover cultural differences and similarities. To be aware of such differences and similarities is important in trust-building processes with actors from different countries.

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### Statements from five interview respondents concerning trust (translation from Swedish)

The CEO of a supplier: Trust is

- built on personal relations
- professionalism: in behaviour, competence in-house
- competence in managing the production
- timeliness
- quality
- managing flexibility and adaption towards the customer, e.g the need to split up delivery instead of being delayed
- building on dialogue when things go wrong. Managing problem situations. Correcting what has gone wrong. See the problems and situation and maybe adjust to one another.
- mutually contributing to solutions
- active communication with personal contact is important for trust. Active seeking of solutions when required by the situation. Not to be anonymous.
- giving signals of competence about your product and the business process

The CEO of a supplier: Trust is

- close relations physically and mentally
- when you have succeeded in joint work with systems
- having reference projects
- having reference customers
- knowing the customer well
- managing exchange of resources

The CEO of a supplier. Trust is

- quality
- timeliness in delivery
- showing competence in managing production, displaying short lead times and short production time
- displaying success in forecasting
- managing stocks and material
- agreements backed up by
  - contact/relations,
  - reliability in promises
  - showing responsibility
  - having reference companies
  - competence
  - straight communication
  - dialogue
- willingness to give and take
- being observant to the other party's situations

The CEO of a supplier: Trust is

- yielding sometimes in important matters, such as prices
- having developed a good network
- personal relations



- values, such as honesty in negotiations
- know each other also outside work
- having a good dialogue
- helping each other

Purchasing director of an industrial customer: Trust is

- when the supplier has short lead times for fast delivery
- quality
- timeliness
- displaying efficient production
- living up to expectations
- competence
- respect for each other in business relation
- keeping promises
- keeping yourself what you demand of others
- that both parties have a common view on the rules of the game
- that the other party fulfils his goal when they are also important for us.