

Internet entrepreneurship: Social capital, human capital, and performance of Internet ventures in China

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Abstract

This article examines the interaction effects of social capital and human capital (experience) of entrepreneurs on the performance of Internet ventures. The empirical data are composed of the longitudinal surveys of 94 Internet ventures in Beijing, China. The study found that the interaction of social capital and Western experience of entrepreneurs has a positive effect on the survival likelihood of Internet firms whereas the interaction of social capital and startup experience of entrepreneurs has a negative effect on firm performance.

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As China's economy is growing rapidly, the domestic private sector is emerging from the shadows and playing a prominent role in the country's economic development. Owing to the historical, institutional and cultural factors, the private sector in China exhibits a high degree of informality. Many enterprises possess vague property rights, ownership structure, corporate governance mechanisms, and financial records. This gives private entrepreneurs great flexibility to respond to an uncertain world composed of rapidly changing market conditions and unstable government regulations. This environment however also constitutes a great challenge to entrepreneurs to put their businesses on a firmer foot-

ing. Entrepreneurs find that an effective way of managing hostile environments in transition economies is doing business through personal networks of relationships because network ties provide resources and information, and help to find clients, suppliers, and investors, who are socially bound (Batjargal, 2003, 2005a,c, 2006). In this article, I examine the way in which Internet entrepreneurs in China combine their social capital and human capital to create viable businesses.

There are two mainstream arguments about what types of social capital or social networks in terms of structure are beneficial to individuals, groups and organizations. On the one hand, coherent and dense networks enable actors to achieve their goals effectively because of cooperative behavior of members, high trust embedded in relationships and informal social mechanisms that control opportunistic behaviors (Coleman, 1988). On the other hand, sparse and non-redundant networks rich in

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structural holes facilitate actors' access to new information, opportunities and resources promoting success of instrumental actions (Burt, 1992).

The instrumental value of networks however is contingent upon the social context, and behavioral patterns of individuals and organizations (Galaskiewicz and Zaheer, 1999). For example, Burt (1997) argued that structural holes, i.e., disconnections between non-redundant contacts in a network, are especially valuable to managers with few peers. Podolny and Baron (1997) reported that structural holes in individual networks had significant positive and negative effects on career advancement depending on the network content. At organizational level, Gulati and Higgins (2003) established that new firms' ties to prominent venture capital firms are particularly beneficial to IPO success during cold markets, while ties to prominent investment banks are particularly beneficial to IPO success during hot markets.

There is however a considerable gap in the literature on how structural properties of entrepreneurs' networks affect venture performance, and how network structures interact with human capital of entrepreneurs, and influence outcome variables. The purpose of this study is to examine the interaction effects of networks, on the one hand, and new venture startup experience, Internet industry experience, and Western (North American and Western European) experience of entrepreneurs, on the other hand, on the survival of Internet firms.

The country and industry context is the Internet industry in China. The Chinese Internet industry is an emergent sector, and therefore, there are a few commonly accepted rules, norms and "taken for granted" to govern relationships (Nee, 1992). This results in greater institutional and social uncertainties that make personal relationships as important resources to get things done (Xin and Pearce, 1996). Furthermore, study of Internet entrepreneurship in general and Internet ventures in emerging markets in particular is a new research field. I think that this study is one of the first studies of the Chinese information and Internet industry that generated US\$ 99.2 billion in revenues in 2001 (Business Weekly, 2002). Finally, the relationship intense cultural milieu in China makes social networks dynamic and important for performance. These reasons justify the choice of the industry and country contexts of this study.

This article is structured as follows. In Section 1, I examine the Internet industry evolution in China. In the following part, I discuss the research literature on the Chinese version of networks—*guanxi*. In Section 3, I propose formal propositions on social capital, human capital and venture performance in China. Section 4 describes the sample and data collection, the variables

and measurements, and the construct validation procedures. In Sections 5 and 6, I report the findings and discuss them in light of network theory. In Section 7, I discuss the implications, the contributions and the limitations of this study.

1. Internet industry in China

The institutional framework in China has profound effects on the evolution and development of the private sector in the country. The hybrid type of communist and capitalist regulations, norms, and organizations (Nee, 1992) provides both opportunities and constraints for private businesses. Scholars documented that in the 1980–1990s entrepreneurs in China were heavily dependent on officials for permissions, political protection, and resources (Wank, 1999). The ambivalent attitudes of the Chinese government towards private property, and the fast changing political atmosphere forced small entrepreneurs to cultivate and maintain clientelistic ties with officials and other resource holders (Xin and Pearce, 1996).

Unsurprisingly, the emerging Internet industry in China is deeply tied to politics. The Internet industry is feared by the ruling communist elite because of the free information flow that has liberating influences on the population.

The year 1994 is regarded as the start of the Internet connection in China (CNNIC, 2002). The Internet industries cover Internet content providers, portals, Internet service providers, manufacturers of telecom equipment, e-commerce, software and other related activities such as e-education, and online game.

Table 1 chronicles the development of the Internet in China from 1987 to 2004. At the end of 2005, there were 111 million Internet users in the country. The total number of computers connected to the Internet reached 49.5 million. There were 2.6 million domain names, and 694 thousand websites. The total bandwidth of leased international connections reached 136,106M. The top three usages of the Internet were news, search engine, and e-mail (CNNIC, 2006). Users of instant computer-to-computer messaging system totaled 87 million. Blogs-online personal diaries, now number more than 30 million. And search engines receive over 360 million requests a day (Economist, 2006).

The regulatory framework of the Internet in China suffers from overlapping and competing rules and regulations administered by different bodies. The main supervisory agencies are the Information Department of the State Council and the Ministry of Information Industry (MII). The MII assumed responsibility for Inter-

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