Effective Distributor Governance in Emerging Markets:
The Salience of Distributor Role, Relationship Stages and Market Uncertainty

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Abstract

Effective governance of distributors represents a critical success factor for firms operating in emerging markets such as China. To understand this governance issue, this article adopts a role theory framework to delineate the effect of fit between governance strategies and distributor role orientations on channel outcomes. It also examines the way two contingency factors (relationship stages, market uncertainty) may moderate the impact of this fit. On the basis of a four-industry survey of distributors in China, the study confirms the salience of strategic fit between the manufacturer’s governance strategy and distributor’s role orientation (in short, governance fit), in support of propositions postulated in recent channel governance research. The findings also indicate that the effects of this governance fit are dependent on the stages of channel relationship (build-up versus mature) but not market uncertainty. This study extends the current literature and suggests the need for finer, phase-oriented dynamic governance strategies in the China market.

Keywords: role theory, channel management, governance strategy, China market
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A major challenge for a firm to capitalize on its market potential in a host country involves the effective management of its distributors (Anderson and Coughlan 1987; Zhang, Cavusgil, and Roath 2003). This can be accomplished by designing effective governance strategies (Heide 1994) that simultaneously motivate and control various types of distributors (Griffith and Myers 2005). This challenge is particularly salient in an emerging market like China (Griffith and Myers 2005; Walters and Samiee 2003), with its scattered and evolving distribution system driven by continuous reforms in its social and economic institutions (Park Li, and Tse 2006; Hoskisson et al. 2000). Extant literature conceptualizes two major types of governance strategies; economic-based and relational-based strategies that are known to effectively enhance distributor performance in developed economies (Jap and Anderson 2003; Murry and Heide 1998; Wathne and Heide 2000). The question is: Would these governance strategies be effective in markets that have distinctively different business cultures?

Studies have unfolded the issue of “fit” or “alignment” between suppliers and distributors as a boundary condition in which economic- and relational-based governance strategies work. John (1984) points out that when inter-firm attitudinal orientation is not aligned, some governance mechanisms (e.g., monitoring and hierarchical control) promote rather than reduce distributors’ opportunistic behavior. Griffith and Myers (2005) showed that when a firm’s governance mechanism fits the cultural norms of the host country, channel performance improves.

In a recent paper, Heide and Wathne (2006) unfolded the centrality of inter-firm “fit” by applying role theory to managing manufacturer–distributor relationships. They proposed that most distributors assume two types of roles in their channel relationship; (1) the business role, for which firm behaviors reflect utility maximization and self-interests, and (2) the friend role,
in which context firms follow the rules and understanding typical of friends (Montgomery, 1998). They postulate that the manufacturers’ governance strategies must “strategically fit” the role orientation of their distributors to be effective (Heide and Wathne 2006, Grayson 2007). When the manufacturers’ governance strategies fit the distributors’ roles, positive channel outcomes, such as increased collaboration, higher relationship satisfaction and better exchange performance, would result. In contrast, a misfit between governance mechanisms and role orientations leads to resource waste, opportunity costs or even distributor retaliatory actions (Heide and Wathne 2006). The relational role postulate is supported by economic sociology as it is in line with March’s (1994) notions of decision “logics”.

The governance fit proposition is consistent with Zajac et al. (2000)’s contingency perspectives in that a firm’s actions need to align with organizational contingencies such as its value or logics. It also recognizes the centrality of diversified organization norms and heuristics when doing business in a society undergoing economic and cultural transitions (Ralston et al. 1999). Yet, in spite of its theoretical strength, this proposition has not been validated empirically.

Governance fit in channel management is of particular relevance to emerging economies because their markets are complex and unstructured (Hung, Gu and Yim 2007) thus generating distributors with different role orientations (Lenartowicz and Balasubramanian 2009). Furthermore, the collectivistic cultural background in many emerging economies such as China and India give rise to distributors who are relationally skewed (Gu, Hung and Tse 2008).

China, an exemplary emerging economy, has undergone major economic and firm transitions. The networks and connections previously thought to be imperative for business success no longer seem as important because market reforms have helped develop efficient business infrastructures (Peng 2003). An increasing number of distributors now focus on the business itself rather than the relationship between channel partners (Dong, Tse and Cavusgil
The diversity of distributors urges manufacturers to tailor channel governance strategies to fit their distributors’ role orientations.

In an emerging market economy characterized by continuous changes, manufacturers have to approach the issue of governance fit in a dynamic manner (Zajac, Kraatz, and Bresser 2000). In high growth markets, manufacturers often need to expand their market coverage and recruit an increasing number of distributors (Walters and Samiee 2003). The new distributors, though eager, are inexperienced. They tend to have mixed motives driven by their simultaneous needs of survival and growth (EIU 2004). In contrast, mature distributors may have developed a diversity of motives to distributorship (e.g., profit maximization) that are in line with their respective business models and market positions. The diversity of motives and role orientations across different types of distributors render channel governance a challenge. Any attempt to manage them with a uniform and standardized governance policy may be unrealistic (Gu, Kim, Tse and Wang 2010).

As the world economy experiences overlapping spheres of global demand shifts, market uncertainty is becoming a central issue in firm strategies (Hoskisson et al. 2000). Studies have confirmed the salience of market uncertainty on organizational change (Lau, Tse, and Zhou 2002), resource acquisition (Makino, Lau, and Yeh 2002), product innovation (Zhou, Tse and Li 2006) and other firm strategies. Yet, should channel governance be continuously revised in high growth markets? Would the issue of governance fit be more prominent in highly uncertain market environments?

Our study examines the salience of strategic fit between suppliers’ governance mechanisms and distributors’ role orientation (in short, governance fit) in emerging economies. On the basis of a survey of distributors across four industries in China, this study pursues three objectives. First, by integrating insights from governance perspective and role theory, we provide an initial validation of the issue of governance fit in China. Second, we delineate and assess the issue of
governance fit in new and established distributors as firms build their distribution networks in this emerging market. Third, our study assesses the moderating effects of market uncertainty on governance fit. This allows managers to gauge their need for dynamic channel governance strategies. In summary, our study attempts to provide insights into three main questions: Does strategic fit in governance strategy matter in an emerging market like China? Can strategic fit be universally applied to building and maintaining channel relationships? In a market characterized by constant change, does market uncertainty demand a governance strategy that is equally dynamic?

We choose China as the research context for two reasons. First, China has become the world’s largest emerging market. As an economy that has been growing by 10% or more annually, the China market is highly dynamic (Atuahene-Gima and Li, 2002), providing an appropriate platform to examine the sustainability of channel governance fit in high-growth and uncertain market environments. Second, similar to other collectivist cultures, the Chinese value system emphasizes interpersonal and social harmony (Bond 1996; Yang 1994). This may skew some distributors to assume a friend-role orientation in their operation. Yet challenged by intense competition and market dynamics (Li, Poppo and Zhou 2008), distributors are increasingly forced to assume a business-role in their operations. These opposing forces generate a conflicting context that allows us to investigate the salience of strategic fit between suppliers’ governance and distributors’ role orientations in detail.

CONCEPTUAL FRAMEWORK AND HYPOTHESES

Governance Mechanisms and Channel Outcomes

Governance has been the pivotal issue in managing marketing channels (Stern, El-Ansary, and Brown 1989). This perspective (Williamson 1999) has deliberated a wide spectrum of strategies, ranging from market structure–based approaches such as coercive influences, market dependency (Frazier 1983), and relational norms (Heide 1994; Zhang, Cavusgil, and
Roath 2003) to formal strategies such as monitoring and incentive systems (Jap and Ganesan 2000). These governance strategies are designed to suppress partner firms’ opportunistic behaviors and promote desired behaviors. They draw insights from transaction cost approach (e.g., Hill 1990; Williamson 1981) and social exchange theory (Lambe, Wittman, and Spekman 2001) to delineate its nature, the underlying processes, and the effectiveness of these governance strategies. Among them, economic- and relational-based mechanisms emerge as the two most influential types of governance.

Economic governance strategies regard firms in a channel as rational economic units which follow the rule of utility maximization (Jap and Anderson 2003). Driven by self-interest seeking motives, agents give ways to opportunism (Williamson 1981; 1985). This mixed motive generates a steady stream of research pertaining to the types and effectiveness of various economic governance mechanisms. They include incentive designs and monitoring systems that enable firms to promote desired channel behaviors using economic rewards or punishments and suppress opportunistic behaviors. As Heide and Wathne (2006) proposed, we operationalize incentive designs as representative of economic governance strategies.

The second type, relational governance strategies, represents strategies that focus on socio-relational norms and motivations. Social exchange theory (Lambe, Wittman, and Spekman 2001) and relational contracting theory (Macneil 1980) advocate that enduring, collaborative exchanges are established and maintained by social norms (Zhang, Cavusgil, and Roath 2003) in addition to economic means. Relational strategies represent an endogenous mechanism that enhances exchange performance by embedding private and public information flows into a matrix of social ties, instead of resorting to contracts or enforcement by third parties (Uzzi 1999). We choose socialization efforts to represent relational governance strategies. Obviously, these two types of governance strategies complement each other and can
appear simultaneously in marketing channels (Heide and Wathne 2006; Jap and Ganesan 2000).

The key to effective channel governance is to design mechanisms that successfully enhance the firm’s own performance as well as motivating distributors to co-operate and stabilize channel relationships (March 1994). When distributors are satisfied with their relationship with the manufacturer, they are willing to assume long-term channel commitment, and superior channel performance is assured.

Figure 1 displays our proposed framework of the way channel governance fit affects channel outcome. It postulates that the fit between the two types of governance strategies (economic and normative strategies) and the two distributors’ role orientations (business-role and friend-role) leads to positive channel outcomes. It also features the moderation effects of the stage in channel relationship and market uncertainty. We adopt channel performance and channel satisfaction as the two channel outcome constructs. Channel performance is a short-term outcome that captures the manufacturer’s performance gained through association with a certain distributor (Jap and Anderson 2003). Channel satisfaction is a long-term evaluation that reflects a summary appraisal of all aspects of a distributor’s working relationship with the supplier firm (Anderson and Narus 1984). In the following, we discuss the framework constructs and their respective effects.

Distributor Role Orientation: Economic and Normative

Role theory postulates that in social exchanges, one party’s perception of its role defines what it expects, how much it invests in, and how it evaluates the relationship (Biddle 1986). Among several different approaches to role theory, two branches: functional (e.g., Bates and
Harvey 1975; Parsons 1937) and structural (e.g., Burt 1982; Winship and Mandel 1983) role theory have historically enjoyed prominence and received attention in the marketing literature. A functional role refers to the contribution that a party makes to the exchange, which in turn defines its obligations and responsibilities. A structural role refers to a party’s “structural position” in the exchange; that is, the relative position of how the party perceives itself, including its social status and identity. To date, these two role approaches have not been extensively applied in inter-firm relationship research.

Recently, a few marketing scholars have applied role theory to the channel context (Heide and Wathne 2006; Grayson 2007). Heide and Wathne (2006) elucidate that distributors’ perceptions of their responsibility, expectations of their supplier firms and evaluations of their relationship with suppliers are critically connected with how they perceive their own functional and structural roles. Based on role theory, they identified two distinct relational roles in channel relationships: as a businessperson and as a friend (El-Ansary and Stern 1972; Heide and Wathne 2006; Grayson 2007). While the two roles coexist and are interchangeable, one role is likely to dominate the exchange relationship within a specific time frame. When a distributor holds a particular relational role, a corresponding set of behavioral norms, or logics, including the logic of consequences and the logic of appropriateness, guide its behavior (March 1994).

The logic of appropriateness describes a rule-driven decision-making mode, while the logic of consequences refers to decision-making processes in utility maximization (March 1994). We label the prototypical relationship role that corresponds to the logic of consequence as an economic role (labeled as a businessperson role in Heide and Wathne (2006) and Grayson’s (2007)). We regard the term “economic role” more appropriate because this role focuses on profit maximization in the channel relationship. We use the term “normative role” to label the role guided by the logic of appropriateness as it drives normative behaviors that regard the relationship partner as a friend (Dwyer, Schurr, and Oh 1987; Heide and Wathne 2006).
When a distributor attributes its primary role to that of a businessperson in the economic world, its actions would follow the logic of consequences (Heide and Wathne 2006; March 1994). When its primary motivation is utility maximization, its actions would aim to maximize or optimize its own interests and preferences (Risse 2000). In the terminology of game theory (Axelrod 1984), a businessperson plays the game by choosing the strategy (cooperation or defection) that maximizes individual payoffs. A businessperson is motivated to pursue opportunistic behaviors (e.g., quality shirking) at the expense of a partner, if the gains are substantial (Klein 1996). As expected, behaviors that follow the economic role may not necessarily lead to favorable economic performance. Yet, if a distributor adopts an economic role, it will be more responsive to economic governance strategies.

In contrast, when a distributor assumes a normative role in the exchange relationship, the logic of appropriateness applies (March 1994). Accordingly, the distributor aims to form normative ties and operates through the interpretive lens of social norms (Chiles and Mcmackin 1996). Such social norms subsequently lead to shared expectations among parties across different levels, including the broader society (Gouldner 1960), regional and local cultures, ethnic or religious sectors, industry sectors (i.e., standard business practices, trade associations) and professional and occupational sectors (Zucker 1986). This implies that distributors operating with normative roles are more receptive to socialization strategies in generating desirable channel outcomes (Heide and Wathne 2006). Our study extends these fundamental postulates by going beyond the main effects of governance strategies and distributor roles to assess the effects when the two constructs are strategically fit or misfit.

**Governance Fit and Misfit**

What happens when a supplier adopts a governance mechanism that does not match the distributors’ role expectations—that is, when a supplier uses normative mechanisms on a
distributor that assumes an economic role or uses economic mechanisms on a distributor that assumes a normative role?

While no studies have reported on this topic, we can nevertheless derive insights from the literature. Strategic fit refers to “the degree to which the needs, demands, goals, objectives, and/or structures of one component of the strategy is consistent with the needs, demands, goals, objectives, and/or structures of another component” (Nadler and Tushman 1980: 36). In our study context, it refers to the consistency between governance and context (distributor role orientations). Miles and Snow (1994) and Day (1999) both postulate that strategic misfit dampens firm performance and needs to be avoided. We use “governance fit” to refer explicitly to the extent the supplier’s governance mechanism fits the distributor’s role expectations.

In the “governance fit” conditions, economic governance mechanism is deployed to economic-role distributors and normative governance mechanism to normative-role distributors, so that the distributors receive what they expect. According to information signaling theory (Feldman and March 1981), the suppliers’ governance fit behaviors should be well understood, without guesswork or misinterpretation. Actions are predictable, reduce uncertainty, and establish a cooperative platform. Mutual trust grows stronger, thus enhancing satisfaction with the exchange relationship, which in turn promises improved governance efficiency and channel performance.

In contrast, when “governance misfit” occurs, distributors are puzzled and confused about the supplier’s actions and their underlying meanings. For example, if offered higher extrinsic rewards, normative-role distributors may question and doubt the future of their relationship. To these distributors, friendly cooperative actions offer greater security than do explicit incentives (Chiles and McMakin 1996). A misfit strategy also provides a strong impetus to attribute causality to the supplier’s seemingly incomprehensible actions (Raven and Kruglanski 1970). Mutual trust will likely decline, as will channel performance.
Similar sequences of negative events may follow when a supplier deploys normative governance strategies to distributors who assume economic roles. To these distributors, the supplier’s socialization efforts appear economically wasteful (Heide and Wathne 2006). The growing misunderstanding generates negative affect in the exchange relationship and, at times, may lead to opportunist behaviors and other destructive actions.

Challenged by their limited resources, supplier firms must allocate effectively to optimize channel performance and long-term relational outcomes (Rindfleisch and Heide 1997). Although both economic and normative governance mechanisms can be effective, the core task is not to choose between them; but to choose a governance mechanism that fits (Heide and Wathne 2006). Our central tenet states that governance fit and misfit exert significant influence on channel outcomes. In short,

H1: The greater the governance fit, the greater the channel performance and channel satisfaction.
H1a: A distributor’s economic role strengthens the effects of the manufacturer’s economic governance (incentives) on channel performance and channel satisfaction;
H1b: A distributor’s normative role strengthens the effects of the manufacturer’s normative governance (socialization) on channel performance and channel satisfaction.

H2: The greater the governance misfit, the lower the channel performance and channel satisfaction.
H2a: A distributor’s normative role weakens the effects of the manufacturer’s economic governance (incentives) on channel performance and channel satisfaction;
H2b: A distributor’s economic role weakens the effects of the manufacturer’s normative governance (socialization) on channel performance and channel satisfaction.

**Governance Fit (Misfit) and Stages of Channel Relationship**

To ensure sustainable success in a host market, firms need to establish an effective distributor network. In an emerging economy such as China, this challenge has led many multinational firms to adopt unconventional methods to develop distributors and expand their market coverage. During 1995–97, for example, Proctor and Gamble set up more than 100 teams that ventured out, like Indiana Jones, to many of China’s third-tier city and village markets to develop its multi-layer city-village distribution network. In 1998 when China
banned all forms of direct marketing, Avon was forced to turn its direct marketing agents into 6,000 licensed distributors. This forced change benefitted Avon in the end. It now enjoys a well known brand name with an efficient and motivated distributor network throughout China.

Governance strategies need to change as new distributors grow into established networks. As Dwyer et al. (1987) and Jap and Ganesan (2000) show, distributors at various phases of development differ in their orientations, management processes and behaviors. Heide and John (1992) also note that the effectiveness of governance mechanisms depends on the particular phase to which the distributors belong. During the build-up stage, distributors focus on their survival needs and are eager to set up long-term relations with the supplier. Their relationship roles are relatively new, implicit, and equivocal (Dwyer, Schurr, and Oh 1987). Accompanied by inter-distributor competition for regional coverage and trade volume discounts, they are receptive to both economic and normative governance mechanisms. Because of these varying motives, we posit that the effects of governance fit are weaker during the build-up stage of channel development.

As the distributorship matures, the relationship roles get discussed, revised, and formally adopted. Implicit rules take form and may even override the terms in formal contracts. The distributor also settles into well-defined roles and rules of operation (Heide and Wathne 2006). Because the distributor has established its market coverage, its net contribution should increase. The channel relationship, with higher levels of tangible and intangible inputs and outcomes, provides manufacturers and distributors alike with acceptable levels of satisfaction and benefits (Jap and Ganesan 2000). Therefore, a governance misfit would generate strong negative reactions at this stage, casting doubts on the channel relationship. A good fit will instead enhance relationship quality and improve channel performance.

Research on inter-firm learning demonstrates that similarity of behavioral norms between partnership firms form a central part of inter-firm knowledge that facilitates communication
and understanding (Grant 1996; Lane and Lubatkin 1998). The fit of relationship role thus operates as a common set of inter-firm knowledge which ultimately leads to superior channel performance and satisfaction. This inter-firm learning requires sufficient time and frequent interaction to establish, thus its effect will likely occur as channel relationship matures. In short, we propose:

\[ H_{3a} \text{ Governance fit exerts stronger positive effects on channel performance and channel satisfaction during the mature stage than during the channel build-up stage; } \]
\[ H_{3b} \text{ Governance misfit exerts stronger negative effects on channel performance and channel satisfaction during the mature stage than during the build-up stage. } \]

**Governance Fit (Misfit) and Market Uncertainty**

In a dynamic and globalizing economy, uncertainty is inevitable. The challenge to most firms is to be both strategically fit and dynamically capable (Teece, Pisano, and Shuen 1997). The ability of governance mechanisms to motivate and control distributors continuously is a pivotal concern (Jap 1999). While we lack an empirical foundation for our postulate, we posit that governance fit is both relevant and highly salient when market uncertainty increases. First, the greater the uncertainty, the more likely it would be for organizations to enter into exchange relations with other organizations of a similar background (Podolney 1994). This is because quality cannot be directly observed. Second, when demand is uncertain, it is important for manufacturers and retailers to share information (He, Marklund, and Vossen 2008). The partners with governance fit have a better mutual understanding that would facilitate inter-firm information sharing. Third, market uncertainty in general gives rise to an adaptation problem (Heide and Stump 1995). The more similar the role orientations that the partners hold, the more willing they would be to adapt to the changing environment together. Therefore, we propose:

\[ H_{4a} \text{ Governance fit exerts stronger positive effects on channel performance and channel satisfaction in high market uncertainty conditions than in low market uncertainty conditions; } \]
H₄b: Governance misfit exerts stronger negative effects on channel performance and channel satisfaction in high market uncertainty conditions than in low market uncertainty conditions.

**METHOD**

*Research Design*

To test our hypotheses, we require a study that involves multiple firms (to assess the effects of different governance strategies), multiple distributors (to assess different role orientations and distributorship development) and multiple industries (to assess the effects of market uncertainty). Similar to most firm strategy and market channel studies, our study used trained research assistants to conduct face-to-face interview with senior executives. As pointed out in Hoskisson et al (2000) and others (Gu, Hung and Tse 2008; Zhou, Yim and Tse 2005), different research methods have varying limitations (low response rates), potential biases (social desirability) and costs. Among them all, personal interviewing, though being the most expensive, is recognized as the most reliable form of data collection (Hoskisson et al 2000) in an emerging market like China.

Specifically, we surveyed the marketing manager or a senior executive of the distributor firm, who is usually directly involved with the strategic and tactical operations of the firm. These managers are familiar with overall corporate activities as well as the operations between the company and its supplier. In responding to the study, respondents identified and assessed their supplier relationship, a crucial construct in our study.

To ensure stronger external validity, we identified four industries in China for which independent distribution is the primary method, according to the *China Market Yearbook* (Gao et al. 2006), the most commonly used cross-industry reference in the market. These industries include electronics, architectural and fitment materials, lighting and cosmetics. We recruited and trained a team of 10 research students from a major university in Shanghai to conduct face-to-face interviews, as is typical in firm studies in China (Hoskisson et al. 2000) to ensure a
reasonable response rate and quality responses.

Our data collection consisted of two stages. In the first stage, the interviewers conducted in-depth interviews with 20 senior managers from both manufacturing firms and distributors, whose responsibilities include managing their firm’s channel relationships. These interviews provided insights into the particular governance strategies, distributor role orientations and other key constructs in our main study as well as their measurement items.

In the second stage, we identified the most influential trade fairs for each of the four industries. The research team and interviewers attended these national trade fairs to select independent distributors randomly as respondents to our survey. One senior manager of each distributor was contacted for personal interviews. The interviewers informed the respondents of the confidentiality of their responses and explained the academic purpose of the project, then requested their participation. Each respondent received a gift (valued at US$25) and was promised a summary report. Of the 400 distributors contacted, 208 initially agreed to participate; however, of these 208 firms, the senior managers of 17 were unavailable for the interview. Altogether, 191 distributor surveys were completed. After screening and deleting missing data and outliers, we retained 188 distributor surveys for data analysis. We evaluated potential non-response bias by comparing early and late respondents in their scores of the major constructs as well as the number of branches, number of employees (Armstrong and Overton 1977) and types of distribution. We found no significant differences.

Of the 188 firms surveyed, firm size in terms of the number of employees varied widely—43.2% have fewer than 20 employees, 21.3% have 20 to 50 employees, 17.5% have 51 to 200 employees, 12.0% have 201 to 1000, and 6% have more than 1000 employees. The mean length of their relationship with a major supplier was 5.33 years, with 22.3% of the firms having working relationships of less than 2 years, 47.3% of the firms between 2 to 5 years, 25.5% of the firms between 5 to 10 years, and 4.9% of the firms having more than 10 years.
This breakdown represents a fair distribution of firms with different relationship lengths with their major supplier. Most respondents were presidents (25.0%) or senior managers in charge of sales operations (49.5%), confirming that they are the appropriate key informants for the study.

Measures

We modified appropriate existing scales from a literature review for our research purposes. Specifically, all the measures were professionally translated through back translation to ensure conceptual equivalence (Craig and Douglas 2000). We tested and modified the scales based on the results of our pre-survey interviews to ensure item equivalence. Most scales used a Likert scale if 1 (strongly disagree) to 7 (strongly agree). They are listed in the Appendix.

Two constructs (channel performance and channel satisfaction) reflect channel outcomes. For the channel performance measure, we employed a scale reported by Kumar, Stern, and Achrol (1992) pertaining to how well the distributor perceives the performance of its supplier as a result of the collaboration. The channel satisfaction scale came from Jap and Ganesan (2000); it measures the extent to which the distributor is satisfied with the relationship.

We operationalized incentives as the relative magnitude of economic incentives (Murry and Heide 1998). For socialization, we developed the scale based on its definition and description made by Wathne and Heide (2000), which refers to (1) the degree of relational and professional support that supplier has given to the distributor; (2) the form of support, including skill training and information gathering; and (3) the promptness of the responses to distributor complaints and inquiries.

Montgomery (1998) defines a normative role as the tendency to rely on the logic of appropriateness, or a rule-driven decision-making mode (March 1994). No measures of the normative role or the logic of appropriateness have been established previously, so we
pretested and modified items during pre-survey interviews. We adopted some relational norms that most commonly describe friendship in a Chinese business context, namely, integrity, virtue, and justice. To measure the economic role, again with no established measures, we pretested and modified new items in the pre-survey interviews. Among the common perceptions of what constitutes a “businessperson” in China, we identified three items: competition, performance, and unethical practices.

Relationship stage and market uncertainty are dummy variables in our survey. The respondent answered whether his/her company’s relationship with the supplier is new or mature. He/she also evaluated whether the market uncertainty in his/her industry is high or low. In addition, the survey includes control variables including firm size (logarithm of the number of employees) and relationship length (how many years this relationship lasts).

RESULTS

The moderation perspective has been one of the most commonly adopted perspectives in strategic fit management research (Xu, Cavusgil, and White 2006). The basic notion of the moderation perspective is that there is no universally superior strategy and that the impact of predictor variable (strategy) on criterion variable (performance) is dependent on the level of a third variable (e.g., distributor’s role). The interaction between predictor and moderator variables is a determinant of the outcome. In our study, we propose that channel outcomes are jointly determined by channel governance strategy and distributors’ role orientation. Thus, we employed moderated regression analysis to test this interaction term. An advantage of this moderation perspective is that it allows for a test of main and interaction effects simultaneously.

The analysis we use to test the proposed hypotheses consists of two stages. In the first stage, we evaluated the reliability and construct validity of the independent and dependent constructs using Cronbach’s $\alpha$ coefficients and confirmatory factor analysis (CFA). After establishing the
reliability and construct validity, we represented each construct by its summary score. In the second stage, we estimated the analysis equations (which we detail subsequently) using the moderated regression approach provided by Jaccard et al. (1990) and Aiken and West (1991). To reduce multicollinearity between the interaction terms and their components (Jaccard, Wan, and Turrisi 1990), we mean centered each scale that has an interaction term (Aiken and West 1991). We then created the interaction terms by multiplying the relevant mean-centered scales.

To establish the reliability and validity of measures, we performed confirmatory factor analysis. We restricted each measurement item to load on its hypothesized factor. All items revealed significant loadings on their expected constructs, in support of convergent validity. As we show in the Appendix, the factor loadings and model fit indices ($\chi^2 (89) = 136.822, p < 0.001; \text{ confirmatory fit index [CFI] } = 0.98, \text{ goodness-of-fit index [GFI] } = 0.92, \text{ normative fit index [NFI] } = 0.93, \text{ root mean squared error of approximation [RMSEA] } = 0.05$) indicate that our model fits the data well.

Next, we examined the discriminant validity of the measures with a variance extracted test (Fornell and Larcker 1981; Netemeyer, Johnston, and Burton 1990). The average variance extracted indicates the amount of variance captured by the construct’s measures relative to measurement error and the correlations ($\Omega$ estimates) among the latent constructs in the model. Estimates of 0.50 or higher indicate the validity of a construct’s measure; all our constructs achieve this criterion (Appendix A). When we compare the variance-extracted estimates for each pair of constructs with the square of the correlations between the two constructs, we find that both variance extracted estimates for each pair of constructs are greater than their squared correlations, in support of their discriminant validity.

Finally, to establish the internal consistency of the measures, we computed their Cronbach’s $\alpha$ and composite reliabilities. As we show in the Appendix, the $\alpha$ score for each construct is higher than the widely accepted threshold of 0.70, and their composite reliabilities
exceed 0.70. In Table 1, we present the correlation matrix and descriptive statistics of the measures.

Insert Table 1 about here.

In Table 2, we report the results of ordinary least squares moderated regression. When we control for the effects of firm size, relational length, market uncertainty, and relationship stage, firm economic incentives relate positively to performance ($\beta = .49$, $p < .001$) and satisfaction ($\beta = .37$, $p < .001$). Similarly, a manufacturer’s socialization efforts relate positively to performance ($\beta = .18$, $p < .01$) and satisfaction ($\beta = .29$, $p < .001$). These findings are consistent with prior literature (Wathne and Heide, 2000) and our expectations.

Insert Table 2 about here.

Salience of governance fit (misfit). According to H1, governance fit should enhance channel performance and channel satisfaction. As we noted in Table 2, the incentives × economic role interaction effect (H1a) is positive and significant for performance ($\beta = .28$, $p < .01$) and marginally significant for satisfaction ($\beta = .13$, $p < .10$). We find a similar pattern for the socialization × normative role interaction (H1b) in terms of performance ($\beta = .19$, $p < .05$) and satisfaction ($\beta = .15$, $p < .05$). These consistent results for economic and normative governance mechanisms in a multi-industry setting offer strong support for our H1; the governance fit paradigm points to the sensitive need for a governance strategy that accommodates distributors’ perceptions of their relationship roles.

We expect the effects of misfit governance strategies to be negative upon channel outcomes. Specifically, H2a proposes that friendly distributors question the true intentions of incentive governance strategies and thus doubt and sometimes mistrust the exchange relationship. Therefore, the interaction effect of incentive × normative role should be negative and
significant. As Table 2 reveals, the effect on performance ($\beta = -.16, p < .05$) and satisfaction ($\beta = -.11, p < .10$) is consistent with our expectations. Therefore, we find partial support for $H_{2a}$.

$H_{2b}$ postulates that when the distributor adopts an economic role, socialization efforts by the manufacturer will exert weaker effects on the two dependent constructs. The results partially confirm our proposition in $H_{2b}$ because the effect is significantly negative upon performance ($\beta = -.19, p < .05$) and insignificant upon satisfaction ($\beta = .00, n.s.$). Overall, $H_2$ is partially supported. The misfit channel governance strategies seem to have greater performance implications.

**Governance fit and stage of channel relationship.** We subdivided distributors into two groups, according to the respondents’ self-rated channel relationship lifecycle: those in the build-up stage (i.e., they perceive the channel relationship as “new” or “developmental”) and those in the mature stage (who perceive the channel relationship as “mature” or “dying or slowing down”). We then conducted the above regression analysis with the same set of control variables. For the distributors in the build-up stage, the main effects of economic incentives and socialization are both positive and significant; none of the interaction terms are significant. However, among the mature stage distributor group, six out of eight interaction terms are positive and significant (except the interaction between socialization strategy and economic role on performance ($\beta = -.18, p < .10$) and relationship satisfaction, $\beta = .11, n.s.$). A t-test comparison of the regression coefficients between these two groups showed that the incentives $\times$ economic role interaction differs significantly in the build-up and mature stages (performance: $t = 2.792, p < .01$; satisfaction: $t = 3.700, p < .001$). And the interaction between socialization and normative role is significantly different for the two groups (performance: $t = 3.701, p < .001$; satisfaction: $t = 1.678, p < .10$). These results provide support for $H_{3a}$ regarding the salience of governance fit in mature channel relationships. The more developed a
channel relationship is, the more influential the fit between governance mechanisms and the
distributor’s expectations from the relationship.

The effect of incentives × normative role on performance and satisfaction is not
significantly different in the build-up and mature stages (satisfaction: $t = -1.488, n.s.$;
performance: $t = -0.605, n.s.$). Similarly, the interaction between socialization and economic role
is not significantly different upon performance ($t = 0.493, n.s.$) and satisfaction ($t = 1.545, n.s.$)
in the two stages. These results show the complex effects generated by the misfit governance
strategies, which may not dampen the channel outcomes. One thing we can conclude from
these results is that misfit governance strategies can hardly promote channel satisfaction and
performance.

**Governance fit and market uncertainty.** To verify $H_4$, we subdivided the distributors into
two groups, according to the respondents’ perception of market uncertainty (dummy variable).
We performed a similar regression analysis with control variables and performance and
satisfaction as dependent measures. In the low market uncertainty group, seven of eight
interaction terms are insignificant (cf. incentives × economic role on channel performance, $\beta$
$= 0.34, p < .05$), but when market uncertainty is high, all the interaction terms except
socialization × economic role follow the predicted pattern, and six of the eight interaction
terms are significant at $p < .05$. The sub-group regression results indicate that the impacts of
governance fit and misfit follow the patterns as we proposed under high vs. low market
uncertainty conditions. However, the t-test comparisons of the regression coefficients show
that the incentives × economic role interaction does not differ significantly for the low versus
high uncertainty groups (performance: $t = -1.046, n.s.$; satisfaction: $t = 1.005, n.s.$). In the
socialization effort × normative role interaction, the regression coefficients are significantly
different for both dependent variables (performance: $t = 2.024, p < .05$; satisfaction: $t = 2.138,$
$p < .05$). As a result, $H_{4a}$ receives partial support. For the interaction between incentives and
normative role, the effect is significantly different upon performance and satisfaction (performance: \( t = 1.723, p < .10 \), satisfaction: \( t = -2.420, p < .05 \)). The interaction between socialization and economic role exerts significantly different effects for low versus high uncertainty groups on performance (\( t = 1.846, p < .10 \)) but no significant effect between the two groups on satisfaction (\( t = .487, n.s. \)). These results partially support \( H_{4b} \). In summary, the results provide partial support to the proposed stronger effects of governance fit and misfit when market uncertainty is high (\( H_4 \)).

**DISCUSSION AND CONCLUSION**

Recent research in channel management allows researchers to initiate an interesting proposition: the strategic fitness of a firm’s governance strategies helps motivate its distributors. Extending from role theory, the proposition’s central tenet suggests that distributors assume different roles in exchange relationships, so supplier firms must tailor their governance strategies according to these roles. Researchers have endorsed this postulate using economic sociology literature and role theory; our study empirically validates the proposition.

In addition, our study delineates the boundary conditions under which this postulate applies, including distributor development and market uncertainty. We chose China as a study context because in this exemplar transitional economy, the issue of governance strategic fit and boundary conditions are salient as many firms continue to enter and expand their operations in the global market. This study context provides a naturalistic research environment that helps researchers enrich our knowledge of distributor governance.

The results of our multi-industry, multi-firm survey provide various insights for researchers and managers. First, the salience of governance strategic fit implies that firms need to incorporate this as an important consideration to their governance strategy. When the strategy matches their distributor’s role orientation, its effectiveness is enhanced. This issue is not about standardizing or localizing a firm’s governance strategy; rather, it is a matter of recognizing the
orientation of partner firms in the distribution channel. Without such consideration and recognition, mutual trust becomes difficult to develop. In turn, the managerial implication is direct: it is suboptimal to use a uniform governance strategy with different types of distributors.

Our findings suggest that managers should tailor their governance strategies to different types of distributors. While tailor-made channel governance seems complex and costly, our findings point to the need for finer classification of distributors based on their role orientations. In short, the results do not advocate customized, firm-specific governance strategies but propose a finer typology of distributor policies. In a major market like that of China where a supplier would easily have over 2,000 distributors, a finer classification with 4 types of governance strategies (new versus mature, friend-role versus businessperson-role) is both reasonable and economically justifiable.

Second, the effects of a misfit condition are asymmetric; governance misfit depresses channel performance but has no effect upon channel satisfaction. This asymmetry urges researchers to investigate further into the governance misfit conditions. A possible explanation lies in the long-term nature of channel satisfaction and the relative short-term nature of channel performance. It is possible that it takes time for the negative consequences of governance misfit to affect channel satisfaction, which cannot be fully reflected in our cross-sectional dataset.

Third, contrary to the general impression that Chinese distributors have strong inclinations toward profit maximization, results of our study suggest this may be a gross overgeneralization. Economic governance strategies work for distributors who operate with an economic orientation but are less effective for those that operate in a normative role. For distributors who regard the exchange relationship as among friends, an over-utilitarian strategy may be offensive and cast doubts on their future relationship.
Fourth, our study finds that governance strategic fit depends on whether the distributor relationships are new or established. For firms that want to develop new distributors and later do establish these relationships, the findings suggest a dynamic model of governance strategy will pay off in continuing to motivate theses distributors. New distributors are developing their role orientation in the exchange relationship. Thus, both types of governance strategy exert positive effects on exchange satisfaction and performance. As the distributor roles consolidate, the issue of governance fit becomes more salient and demands a strategic perspective towards developing the distributor network. Managerially, our finding runs contrary to the conventional wisdom which states that it generally benefits firms to spend more time with new rather than with established distributors. If anything, a greater understanding between firms and their established distributors is salient. With established market coverage and thus more stable demand, established distributors require more attention than new distributors.

Fifth, our study also examines the effects of governance fit in varying conditions of market uncertainty. In complex business-to-business distributor exchanges, market uncertainty represents a separate force of change that demands attention. In different market uncertainty conditions, our study does not show that the impacts of governance fit differ. In our study, market uncertainty is a dummy variable, which may sacrifice some variations of this construct and lead to the insignificant differences under high versus low market uncertainty conditions. Further investigations of this contingent effect are needed.

Nonetheless, the results offer managers a number of implications. General guidelines for market uncertainty recommend hedging or transferring risk to other partnership firms; our result instead suggests aiming for better strategic fit is a viable alternative. Strengthening distributor ties through a strategically fit governance strategy can be effective. For example, when Amway pulled out of China because of a government policy that banned direct marketing, the firm emphasized trust and promised its agents that their relationship would be
renewed once the policy changed. When the firm returned in 2006, all of its former agents returned, and the firm’s national distributorship revived with a sales growth that topped any of Amway’s other overseas markets within a short time.

Taken together, the findings regarding governance strategic fit and its boundary conditions suggest a new perspective on channel research and management. Contrary to extant literature that emphasizes manufacturer interests, such as the use of market power, taking advantage of distributors’ transaction-specific investment (sunk costs) and monitoring distributors against opportunism, our study suggests another perspective: consideration and recognition of distributors’ roles and behavior. This direction is crucial in the rapidly globalizing world, with its increasing reliance on emerging economies. Our study highlights the need for finer, phase-oriented and dynamic governance strategies to build trusting and effective market channels.

Finally, our study has several limitations that need to be recognized and enriched through further research efforts. First, because its centrality to governance strategies, the issue of governance fit requires further replications. Second, the contingency factors of governance fit deserve more theoretical work. Third, we chose China as an exemplar research context, but other contexts in both emerging and developed economies could further confirm the findings and advance our current knowledge on international marketing channels. Fourth, it is necessary to recognize that our use of personal interview as data collection method may embed social desirability effects that may biases our findings. The use of single informant for firm study also has its limitations.
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Zhou, Kevin Z, Chi Kin (Bennett) Yim, and David K. Tse (2005), "The Effects of Strategic Orientations on Technology- and Market-Based Breakthrough Innovations," *Journal of Marketing*, 69 (April), 42-60.


Figure 1: Framework of Governance Fit and Channel Outcome

**Governance Strategies:**
- Economic (incentive)
- Normative (socialization)

**Distributors’ Role Orientations:**
- Economic role (businessperson)
- Normative role (friend)

Stage of Channel Relationship → Governance Fit → Distributors’ Role Orientations

Channel Outcome
- Channel Performance
- Channel Satisfaction

Market Uncertainty
Table 1: Construct Means and Correlations

<table>
<thead>
<tr>
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<td>.51**</td>
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<td>5. Normative role</td>
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<td>9. Market uncertainty</td>
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* Significant at the $p<.05$ level, ** Significant at the $p<.01$ level.
Table 2 Regression Results

<table>
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<th>Variables</th>
<th>Total Sample (N=188)</th>
<th>Build-up Stage (N=77)</th>
<th>Mature Stage (N=106)</th>
<th>Low Market Uncertainty (N=84)</th>
<th>High Market Uncertainty (N=88)</th>
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<td>CPERF</td>
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<td>Economic incentives</td>
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<td>.66***</td>
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<td>.29***</td>
<td>.16*</td>
<td>.36***</td>
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<td>Normative role (NR)</td>
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<td><strong>Interaction Effects</strong></td>
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<tr>
<td>Incentives × ER</td>
<td>.28**</td>
<td>.13+</td>
<td>-0.03</td>
<td>-0.01</td>
<td>.44***</td>
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<tr>
<td>Socialization × NR</td>
<td>.19+</td>
<td>.15*</td>
<td>-1.14</td>
<td>-0.01</td>
<td>.41***</td>
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<tr>
<td>Incentives × NR</td>
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<td>-1.11</td>
<td>-0.07</td>
<td>-0.06</td>
<td>-.25*</td>
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<tr>
<td>Socialization × ER</td>
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<td>.00</td>
<td>-0.06</td>
<td>-0.20+</td>
<td>-.18+</td>
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<td><strong>Control Variables</strong></td>
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<td>Firm size</td>
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<td>-.27**</td>
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<td>R²</td>
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<td>Adjusted R²</td>
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<td>.47</td>
<td>.40</td>
<td>.45</td>
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*** p < .001, ** p < .01, * p < .05, + p < .10.

Notes: CPERF = channel performance, CSAT = channel satisfaction.
### Appendix:
#### Measurement Items and Validity Assessment

<table>
<thead>
<tr>
<th>Measures</th>
<th>SFL</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Normative governance (socialization):</strong> $\alpha = .890$, $CR=.892$, $AVE=.734$</td>
<td></td>
</tr>
<tr>
<td>1. Our supplier has provided us with a lot of business support on product launch.</td>
<td>0.795</td>
</tr>
<tr>
<td>2. Whenever we need help or suggestions, our supplier responds promptly.</td>
<td>0.860</td>
</tr>
<tr>
<td>3. Our supplier has sent in professionals to assist our business.</td>
<td>0.912</td>
</tr>
<tr>
<td><strong>Economic governance (incentives):</strong> $\alpha = .819$, $CR=.826$, $AVE=.706$</td>
<td></td>
</tr>
<tr>
<td>1. The incentives that our supplier offers us exceed the market standard.</td>
<td>0.760</td>
</tr>
<tr>
<td>2. The incentives that our supplier offers us are satisfactory.</td>
<td>0.913</td>
</tr>
<tr>
<td><strong>Economic role (businessperson):</strong> $\alpha = .861$, $CR=.871$, $AVE=.695$</td>
<td></td>
</tr>
<tr>
<td>1. The marketplace is like a battlefield, only the winners are respected.</td>
<td>0.748</td>
</tr>
<tr>
<td>2. Performance can be achieved regardless of the means used.</td>
<td>0.974</td>
</tr>
<tr>
<td>3. It is natural to use some unethical means to achieve individual success in the marketplace.</td>
<td>0.760</td>
</tr>
<tr>
<td><strong>Normative role (friend):</strong> $\alpha = .924$, $CR=.925$, $AVE=.804$</td>
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<tr>
<td>1. Only firms with integrity can succeed in the Chinese market.</td>
<td>0.894</td>
</tr>
<tr>
<td>2. Ethics and friendship should be valued in business.</td>
<td>0.860</td>
</tr>
<tr>
<td>3. Integrity and justices are the important principles in doing business in China.</td>
<td>0.934</td>
</tr>
<tr>
<td><strong>Channel performance:</strong> $\alpha = .872$, $CR=.864$, $AVE=.760$</td>
<td></td>
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<tr>
<td>1. If we have to give the supplier a performance appraisal, it would be outstanding.</td>
<td>0.874</td>
</tr>
<tr>
<td>2. Taking all the different factors into account, the supplier’s performance has been excellent.</td>
<td>0.870</td>
</tr>
<tr>
<td>3. Through the association with our company, the supplier’s performance has been excellent.</td>
<td>0.736</td>
</tr>
<tr>
<td><strong>Channel satisfaction:</strong> $\alpha = .850$, $CR=.845$, $AVE=.732$</td>
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</tr>
<tr>
<td>1. We are very satisfied with the cooperation extended by our supplier.</td>
<td>0.865</td>
</tr>
<tr>
<td>2. We are very satisfied with the relationship with our supplier.</td>
<td>0.846</td>
</tr>
</tbody>
</table>

#### Overall Model Fit:

$\chi^2 (89) = 136.822, \ p < .001$; GFI = .92; AGFI = .88; CFI = .98; NFI = .93; IFI = .98; RMSEA = .05.

Notes: SFL = standardized factor loading, CR = composite reliability; AVE = average variance extracted.