



# Improving performance and reducing cost in buyer–supplier relationships: The role of justice in curtailing opportunism



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## ABSTRACT

Building on social exchange theory, we study the role of justice perceptions in curtailing opportunism and, in turn, improving performance and reducing governance cost in buyer–supplier relationships. Our analysis of 225 dyads in the Chinese home appliance industry indicates that distributive justice is negatively linked to strong form opportunism, whereas procedural justice and interactional justice perceptions are negatively related to weak form opportunism. Additionally, while relationship performance is equally reduced by both forms of opportunism, governance cost increases significantly more with strong form opportunism. We conclude that preserving the formal structure of the exchange through distributive justice and the informal mechanisms of interaction through procedural justice and interactional justice is important in enhancing performance and reducing cost. We caution that we view the role of organizational justice as complementary to economic forces such as contractual and managerial governance.

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## 1. Introduction

Because opportunism in buyer–supplier relationships is commonly seen as an obstacle to fostering cooperation, researchers have paid increased attention to the mechanisms curtailing opportunism in such settings. Traditionally, based on the logic of transaction cost economics, the main focus has been on economic forces such as contractual safeguarding, shared ownership, investments in relationship-specific assets, and managerial governance (Barthelemy & Quelin, 2006; Brown, Dev, & Lee, 2000; Buvik & Reve, 2001; Dahlstrom & Nygaard, 1999; De Vita, Tekaya, & Wang, 2010; Lumineau & Quelin, 2012), all of which require the establishment of formal governance structures. However, in recent analyses of long-term inter-firm collaboration, such as in strategic alliances or international joint ventures, this logic has been complemented with one that is based on social exchange theory (Adams, 1965; Blau, 1964) and considers constraints to firm behavior due to social norms (Luo, 2007b, c, 2008; Poppo & Zenger, 2002). In the context of buyer–supplier relationships, researchers have also recognized the combined role of economic

and social forces with respect to dispute resolution (Lumineau & Henderson, 2012; Lumineau & Oxley, 2012), mutual adaptation (Mukherji & Francis, 2008), and relationship quality (Liu, Li, & Zhang, 2010; Liu, Luo, Yang, & Maksimov, in press).

In essence, social forces complement economic forces in curtailing opportunism and governing long-term inter-firm exchanges (Cai, Yang, & Hu, 2009; Luo, 2006, 2007c; Poppo & Zenger, 2002). Economic transactions become gradually embedded in social relations (Granovetter, 1985). Therefore, social exchange theory can provide important insights on the dynamics of repeated economic transacting beyond those gained from the application of economic theories solely. However, the role of justice ordering, as an important social force (Luo, 2007c), in curbing opportunism and improving relationship outcomes in buyer–supplier relationships has not been adequately addressed in prior research. Justice is fundamental to all social exchange as perceptions of equity nurture continued commitment to an ongoing exchange, even under uncertainty (Adams, 1965). Justice strengthens overall commitment (Johnson, Korsgaard, & Sapienza, 2002), improves resource allocation (Kim & Mauborgne, 1993), and reduces opportunism (Luo, 2007c). It also alleviates relational uncertainty, which may be difficult or even impossible to reduce through formal contracts, and create enduring economic incentives that counter opportunism and promote long-term cooperation (Luo, 2007b).

We offer a formal model where justice perceptions act to curb opportunism and, in turn, reduce governance cost and improve

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relationship performance (see Fig. 1). In examining the effects of three types of justice (distributive, procedural, and interactional), we differentiate between strong form opportunism (a violation of contractual norms) and weak form opportunism (a violation of relational norms). In addition, we explore the improvements in relationship outcomes (such as lower governance cost and higher relationship performance) that stem from curtailing opportunism (Hawkins, Wittmann, & Beyerlein, 2008). We organize our analysis around a two-step sequential model, rather than a mediation model, for two reasons. First, we are interested in the variety of forms and relative strengths of the relationships between the three forms of justice and the two forms of opportunism, as well as between the two forms of opportunism and the two types of relationship outcomes. Second, it is premature to examine a mediation role of opportunism given the nascent operationalization of the construct.

## 2. Theory

### 2.1. Social ordering versus economic ordering

Curbing opportunism in long-term inter-firm exchanges depends fundamentally on two types of forces – economic ordering and social ordering (Luo, 2006, 2007c). Economic ordering is fundamentally based on transaction cost theory (Williamson, 1985, 2005), which assumes that parties in an economic transaction pursue self-interest on the basis of calculativeness. Accordingly, countering opportunism relies on economic forces such as contractual governance and managerial governance to organize and restrict firm behavior. Through contractual governance, parties can specify responsibilities, rights, and penalties, while managerial governance helps to oversee behavior and commitment. The main proposition of this theoretical approach is that to curb opportunism, transacting parties need to design more elaborate and complex contracts and exercise greater formal control.

However, this approach is incomplete to fully address the danger of opportunism because firm behavior is also influenced by social norms. In long-term economic exchanges, transactions become gradually embedded in the social structure of the relationship (Granovetter, 1985). Interactions receive a social, in addition to an economic, dimension where actions are based reciprocally on the rewarding reactions of others. Social ordering is based on social exchange theory, which assumes that actors in a socially embedded exchange follow social principles, such as equity (Adams, 1965) and reciprocity (Blau, 1964). Accordingly, firm behavior, including countering opportunism, can be guided through social forces such as justice, trust, and attachment (Luo, 2006).

An increasing body of research suggests that economic and social orderings are complementary in guiding long-term economic transactions. While economic ordering provides the fundamental institutional framework, social ordering nurtures continuity of an inter-firm exchange (Luo, 2002, 2007c). Economic forces alone are insufficient to

suppress opportunism and promote continuity, especially when external uncertainty is high (Lumineau & Henderson, 2012; Luo, 2007a; Poppo & Zenger, 2002). Without sufficiently strong social forces, parties may not reach cooperative resolutions to conflicts and disputes (Lumineau & Oxley, 2012), especially in buyer–supplier relationships, where commitment to cooperation by each side may depend on different exchange characteristics (Kim, Park, Ryoo, & Park, 2010). Economic forces form an important foundation in different buyer–supplier contexts, while social forces contribute to the quality of the relationship when parties pursue long-term mutual benefits, rather than short-term individual gains (Liu et al., 2010). Accordingly, we view opportunism in buyer–supplier relationships as embedded in both economic and social structures.

### 2.2. Justice perceptions

Justice is fundamental to all types of economic transactions, especially in long-term exchanges that are potentially subject to multiple external and internal uncertainties. As a social force, justice is both a reflection and a complement to the economic forces underpinning a given exchange. We look at three forms of justice – distributive, procedural, and interactional. Distributive justice is related to the economic aspect of a cooperative business relationship, procedural justice is linked to the instrumental side, and interactional justice is associated with the social side. Specifically, distributive justice is the extent to which the distribution of benefits in social exchange is fair in view of each party's contribution, commitment, and assumption of responsibility (Kumar, Scheer, & Steenkamp, 1995; Luo, 2007b). Procedural justice reflects the degree of fairness in the procedures employed to determine how actors are treated and how respective benefits are assigned (Greenberg, 1990; Kumar et al., 1995; Luo, 2007b). Interactional justice refers to the quality and fairness of interpersonal treatment during the enactment of organizational decisions and procedures and highlights the human aspects of interaction reflected in the expressions of respect, politeness, honesty, and dignity (Bies & Moag, 1986; Luo, 2007b).

### 2.3. Two forms of opportunism

Williamson (1985) defines opportunism as 'self-interest seeking with guile' or 'the incomplete or distorted disclosure of information, especially to calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse' (p. 47). In the context of business partnerships, opportunism is broadly defined as the 'behavior by a partner firm that is motivated to pursue its self-interest with deceit to achieve gains at the expense of the other alliance member' (Das & Rahman, 2010: p. 57). It refers to the act or behavior performed by one party to seek its unilateral gains at the expense of the other by breaking implicit or explicit contracts, abusing power, withholding or distorting information,

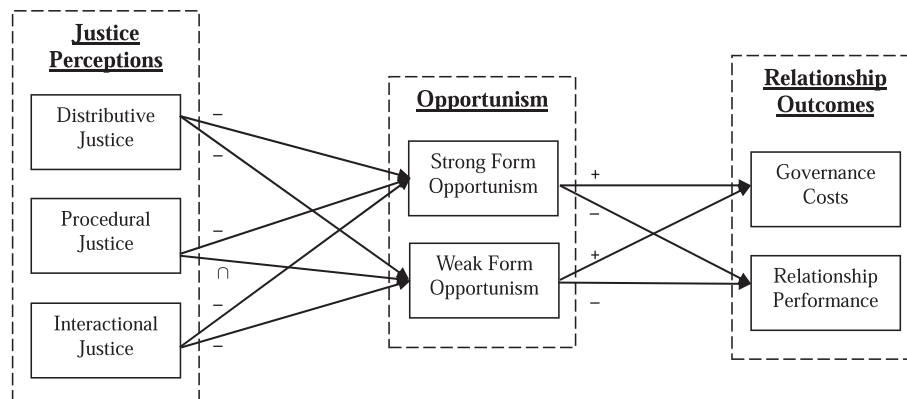


Fig. 1. Conceptual model.

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