Asia Pacific J Manage (2006) 23: 209–227
DOI 10.1007/s10490-006-7167-8

Getting bank financing: A study of Vietnamese private firms

Ngoc T. B. Le · Sundar Venkatesh · Thang V. Nguyen

Abstract Private firms in transition economies are operating in an extremely uncertain environment, with underdeveloped market institutions, poorly defined property rights, and absence of reliable business data. This raises a very basic question of how owners of these firms persuade bankers to make much needed loans. This study employs an institutional perspective and argues that firms' legitimacy positively influences their accessibility to bank financing. Specifically, this study develops a model that links networking, professional management practices, and growth stage with bank financing and tests that model using a sample of Vietnamese private firms. The results support the hypotheses that growth stage and networking greatly influence firms' accessibility to bank financing, and that the impact of networking on financing is contingent on the growth stage.

Keywords Vietnam · Small and medium-sized enterprises (SMEs) · Bank financing

The burgeoning private business sector is playing an important role in the economic development of transition economies. The private sector has become an additional engine of economic growth, a major generator of foreign exchange through exports, and an important source of employment (e.g., Bilsen and Konings, 1997; Nguyen, Weinstein and Meyer, 2005; Theng and Boon, 1996). This sector appears to be a relatively lucrative new market for commercial banks wishing to diversify their loan portfolios.

N. T. B. Le (✉)
NEU Business School, National Economics University, Giai Phong Road, Hanoi, Vietnam and
Asian Institute of Technology, Thailand (Ph.D. candidate)
e-mail: lbngoc@bsneu.edu.vn

S. Venkatesh
Asian Institute of Technology, Thailand
e-mail: svenkat@ait.ac.th

T. V. Nguyen
NEU Business School, National Economics University, Giai Phong Road, Hanoi, Vietnam and
Faculty of Business Administration, University of Macau, Macau, China
e-mail: tnguyen@umac.mo

External financing is a critical source of funding for firms in transition economies (e.g., see Young, Peng, Ahlstrom, and Bruton, 2002). However, private firms in these economies face an extremely challenging task in accessing external sources of finance. While previous studies in developed economies found that private small and medium enterprsies (SMEs) are high-risk borrowers, there is not even a solid basis for calculating risk in lending to private firms in transition economies (Guseva and Rona-Tas, 2001; Nguyen, Le, and Freeman, 2004; O'Connor, 2000). Transition economies are characterized by market institutions and infrastructures that are largely undeveloped, property rights that are not well defined, and private sector legitimacy that has not been well protected. Data on private firms and the general business environment are either not available or unreliable. As new private firms are established, they have neither developed reputation in the market nor had the necessary history of working with banks. This raises a very basic question of how owners of private firms in transition economies—in the absence of effective market institutions, reliable business data, and established reputation—persuade banks to provide much needed loans.

Two observations motivate this study. First, previous studies on bank financing to SMEs have largely been conducted in the context of developed economies (e.g., Binks and Ennew, 1997; Jankowicz and Hensrich, 1987; Petersen and Rajan, 1994; Ulrich and Cassel, 1975; Van Auken, 2001). Recognizing that SMEs are perceived by banks as high risk borrowers, these studies focus on strategies that help mitigate such high perceived risks. Private SMEs in transition economies, however, face an even more fundamental challenge in accessing bank loans: their relative lack of legitimacy (Boisot and Child, 1996; Peng and Heath, 1996; Tsang, 1994; Nguyen et al., 2005). Owners of these private SMEs are not only tackling the inherently risky task of starting and building a new firm, but also are doing so without the social, political, and legal infrastructure that entrepreneurs in developed economies often take for granted. Thus, their strategies in obtaining legitimacy, in addition to those in mitigating risks, are critical to accessing bank loans.

Second, previous studies of SMEs' external financing have not distinguished between firms at different stages of growth. Since firms at different growth stages have distinct characteristics and also face different problems (Koberg, Ehlenbruck and Sarason, 1996; Terpstra and Olson, 1993; Kazanjian, 1988; Kazanjian and Drazin, 1990; Quinn and Cameron, 1983), obstacles and solutions for getting external financing for private SMEs at different stages of growth can be expected to be different. Treating private firms as a uniform group regardless of their growth stage offers limited research and practical implications. This issue is even more important in transition economies where many private firms are transitioning from one growth stage to the next, and their legitimacy changes accordingly. What should they do to get bank loans at each growth stage?

This research applies institutional theory to examine factors that influence firms' accessibility to bank loans by private SMEs. The central thesis of the paper is that firms with high levels of legitimacy would have better access to external financing (including bank loans). Thus, factors that help firms improve their legitimacy would also help these firms access bank loans more easily. Specifically, we examine the influences of growth stages, professional management practices, and networking on access to bank financing by private SMEs.

We chose Vietnam as the most ideal context to test our hypotheses. Vietnam offers a unique natural laboratory, with an extreme form of entrepreneurship that operates in the absence of well-established market institutions. Entrepreneurs in Vietnam have few role models or exemplars, have little reliable business data and lack skills to develop business plans, have little time to build their reputation, and yet have no choice but to rely on external financing for growth. For this reason the experiences of young Vietnamese firms can offer us lessons about accessing bank loans in the absence of market institutions and sufficient reputation capital. While the lack of cross-national data limits the generalizability of our research, this is offset by the special insights gained from the opportunity to examine the process of accessing bank loans in a nascent market system.

In the next section we provide a review of institutional theory and develop our hypotheses on factors influencing the use of bank financing. The following section briefly describes the Vietnamese context, presents our research methodology and key findings. Discussions of theoretical and managerial implications conclude our paper.

Theoretical framework and hypotheses

This research adopts an institutional perspective and explores factors that influence firms' bank financing. Institutional theory emphasizes the influences of societal systems on organizational behavior. According to this theoretical perspective, institutional factors affect organizations' strategies and processes (Scott, 1995). Organizations that conform to the "rules of the game" (North, 1990) and become "isomorphic" with their environment (Meyer and Rowan, 1977, p.352) would gain the legitimacy and resources needed to survive. Thus, an organization's success depends more on its legitimacy than on efficient coordination and control of productive activities.

An organization's legitimacy refers to the extent that key stakeholders, the general public, key opinion leaders, and/or government officials know about and accept the organization and its practices (Aldrich and Fiol, 1994; Scott, 1995). Aldrich and Fiol (1994) suggested that there are two types of legitimacy. *Cognitive legitimacy* refers to the extent the general public know about the organization and its practices. The highest form of cognitive legitimacy is when a new venture or organization becomes so well known that it is taken for granted. *Sociopolitical legitimacy* refers to the extent to which a new organization conforms to recognized principles or accepted rules and standards. It can be measured by how key stakeholders, the general public, and government officials accept the organization and its practices as "appropriate and right given existing norms and laws" (Aldrich and Fiol, 1994, p.648). Aldrich and Fiol's (1994) typology of legitimacy is similar to Scott's (1995) three dimensions of institutions: regulative, normative (resembles sociopolitical), and cognitive. Thus, an organization can increase its legitimacy by spreading the knowledge of its existence among key stakeholders and the general public, and proving that its practices conform to the society's accepted laws and norms.

Several scholars have suggested that the institutional perspective is the most appropriate for studying firm behavior in transition economies (Hoskisson et al., 2000; Meyer and Nguyen, 2005; Shenkar and von Glinow, 1994). Private firms in transition economies are presented with many business opportunities, but have high uncertainty in the business environment, low levels of order and structure, and are in an early stage of government support (Boisot and Child, 1996; Guseva and Rona-Tas, 2001; Peng and Heath, 1996; Peng, 2003). This provides a fascinating context to test the influence of institutional factors on firm behavior. Several studies have concluded that in the absence of effective market institutions, private firms have to rely on various strategies to gain legitimacy (Peng and Heath, 1996; Tsang, 1994). Examples of these strategies include: networking with government officials, networking with managers of other firms, and networking with relatives and friends (Peng, 2004; Peng and Luo, 2000; Redding, 1990; Xin and Pearce, 1996); allying with state-owned firms (Tsang, 1994); and aligning business practices with best practices that are increasingly accepted by the society (Nguyen and Bryant, 2004; Peng, 2003).

The central thesis of this paper is that in transition economies, a private firm's legitimacy will significantly influence its access to bank financing. Factors that influence firm legitimacy would also influence firm access to bank financing. Drawing on institutional theory and

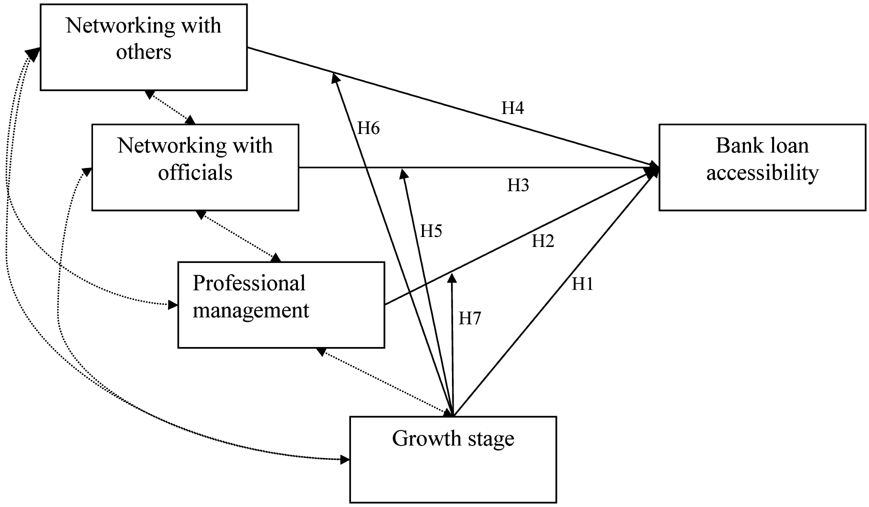

Fig. 1 Theoretical Model

previous relevant empirical studies, we develop hypotheses that link firm Growth stage, Professional management practices, and Networking to Bank loan accessibility. Figure 1 illustrates our theoretical model.

Growth stage and Bank loan accessibility

Institutional theory suggests that firm legitimacy is a function of age. New firms suffer from "liability of newness", i.e. there is an absence of information and evidence regarding their existence and their practices (Aldrich and Fiol, 1994; Hannan and Freeman, 1977). The lack of knowledge, understanding, and acceptance of new firms means their legitimacy is weaker than more established firms. Thus, obtaining legitimacy is central to the process of survival of new firms (Hannan and Freeman, 1994; Shepherd and Zacbarakis, 2003).

The growth of firms is not a smooth and gradual process. Research has provided support for the proposition that firms go through various growth stages (Quinn and Cameron, 1983; Miller & Friesen, 1984). Most scholars rely heavily on the description of the structure an organization has adopted to distinguish growth stages. Kazanjian (1988), on the other hand, describes stages as a problem-based phenomenon. At each stage, firms face a unique set of problems that require unique organizational designs. Empirical studies (Kazanjian, 1988, Koberg et al., 1996) suggest that there are at least two distinct growth stages: the early stage (including Product Conception, Development and Commercialization); and the later stage (Growth and Stability).

We choose Kazanjian's (1988) conceptualization of growth stage for our study because it reflects the impact of institutional factors on firm development. Following the institutional perspective, we argue that firms at the early stage have weaker legitimacy than those at the later stage. Firms at the early stage have neither established their reputations in the market nor developed clear business models. They are subject to a higher rate of failure than those in the later stage (Hannan and Freeman, 1984; Shepherd and Zacbarakis, 2003). Compared to their counterparts in a later stage of growth, firms in the early growth stage are expected to have disadvantages in accessing bank loans. This is especially true in transition economies where new firms do not have strong sociopolitical and economic support. Therefore, we hypothesize:

H1: *The accessibility of bank loans is easier for later-stage firms than for early-stage firms.*

Professional management practices and Bank loan accessibility

Peng (2003) observed that the transitions in emerging economies typically end up with predominantly relationship-based transactions first, and then gradually move to rule-based transactions. During this process, private firms increasingly compete based on competitive resources and capabilities. In other words, best management practices become more and more widely used by private firms as the economies move toward more market-oriented systems.

As a result, the adoption of best practices borrowed from market economies will increasingly help private firms in emerging economies to gain legitimacy. First, by adopting best practices, firms use more legitimate language in their organization's brands, goals, and policies. This language fits with the generally accepted language of the society, and raises cognitive legitimacy. Second, the adoption of best practices increases the use of external assessment criteria, such as the use of modern accounting standards and accepted recruitment processes. This demonstrates the social fitness of the firms (Meyer and Rowan, 1977).

From a banker's point of view, lending to SMEs is a challenging task regardless of the development of the economy. SMEs usually do not disclose all important information related to their firm's business transactions. In addition, most SMEs lack skills in preparing financial statements and business plans. These amplify the problem of information asymmetry (i.e., borrowers have more information about their firms than banks do) (Coleman, 2000; Pettit and Singer, 1985). Moreover, many SMEs management practices, such as highly centralized decision making system, overdependence on one or two key individuals for the firm's survival and growth, an inadequate repertoire of managerial skills and training, and a paternalistic atmosphere, often create a poor business image for SMEs (e.g., Bjerke, 2000; Charan et al., 1980). Yet, professional management is one of the key criteria for banks to grant loans (Pace and Collins, 1976; Jankowicz and Hensrich, 1987). This criterion is even more important when banks lack accurate financial information about the borrowing firms (Deakins and Hussain, 1994). From the bankers' point of view, the lack of professional management practices in the borrowing firms decreases firms' legitimacy. Therefore, an effort to "professionalize" the image through the adoption of best management practices is particularly important to access bank loans. Empirical research indicates strong effects of professional management practices on a firm's access to bank loans (Zinger et al., 2001; Van Auken, 2001; Jankowicz and Hisrich, 1987; Theng and Boon, 1996; Van Auken and Carter, 1989; Ulrich and Cassel, 1975). Hence, we hypothesize:

H2: *A firm's level of professional management practices is positively associated with bank loan accessibility.*

Networking and Bank loan accessibility

Social networks have been found to be especially important for private firms in transition economies to obtain the necessary level of legitimacy (Nguyen et al., 2005; Peng and Heath, 1996; Tsang, 1994; Xin and Pearce, 1996). In the absence of effective market institutions, inter-personal relationships play an important role in spreading knowledge about the firm's existence and its practices. It also helps the firm obtain needed support from key stakeholders and the general public. Numerous empirical studies support this argument (Peng, 2003).

We follow Peng and Luo (2000) and distinguish two types of networks: 1) Networks with government officials; and 2) Networks with managers of other organizations and with relatives and friends (hereafter: Networking with others). As found in several prior studies, networking with government officials helps ease procedures with government organizations and banks (Peng and Luo, 2000; McMillan and Woodruff, 1999; Meyer and Nguyen, 2005). Xin and Pearce (1996) reported that in the Chinese context, close ties with government officials can offset the disadvantages of being a privately owned firm. Effective networking with government officials also has a strong impact on firm performance (Peng and Luo, 2000), increasing the firm's creditworthiness in the lenders' assessment. In other words, networking with government officials increases a firm's legitimacy and its ability to access external sources of finance.

A firm's networking with officials also helps the firm access more aid donations and government support programs. Since aid money and government support programs are usually cheaper than bank loans, firms would prefer to use these sources of financing to bank loans. In addition, connections with government officials may help firms to have access to government funded projects or government customers. These usually are partners with good trade credit. Access to these less expensive sources of finance reduces the need to borrow from banks. Finally, good connections with government officials helps firms to reduce transaction costs in various registration and business activities, such as access to land, information, and other operating licenses (Meyer and Nguyen, 2005). In transition economies, these barriers are costly and sometimes prohibitively high for private firms (Tenev et al., 2003; MPI, 2003). Thus, good connections with government officials could also save money, which otherwise would have been used to deal with bureaucracy to keep the business operational. Therefore we hypothesize:

H3: *The strength of a firm's network with government officials is negatively associated with bank loan accessibility.*

The second type of network, "network with others", is with managers of other organizations and with friends. This network helps firms increase their legitimacy in several ways. First, it helps spread the knowledge of the firm's existence and business practices to key stakeholders and the general public. This is of special importance when firms apply for bank loans. To offset the lack of public data, bankers in transition economies often have to rely extensively on informal information channels to learn about new loan applicants (Nguyen, Le, and Freeman, 2004; O'Connor, 2000). Consistent and positive information from different sources is critical for considering making loans to these applicant firms. The more a firm's managers build a network with others, the higher the chance the firm will be well known to banks. This increases the firm's cognitive legitimacy. Second, an endorsement and referral from a respected individual often helps create a positive image of the firm (Granovetter, 1985; Coleman, 1988), increasing the firm's sociopolitical legitimacy. As a case in point, Peng (2004) found that kinship networks in Chinese villages provided informal enforcement of private property and protected entrepreneurs against predatory cadres. These factors helped reduce uncertainty and raised the survival and success rate of private businesses within the lineage group.

By helping firms increase their legitimacy, networking with others positively influences the firms' accessibility to bank loans and other informal sources of funds (e.g., trade credit, loans from friends and relatives). The informal sources of funds, however, often are smaller, and more expensive than bank loans. We argue that whenever bank loans are available, firms would generally prefer bank loans to informal sources. Therefore, we hypothesize:

> ***H4:*** *The strength of a firm's network with others is positively related to the bank loan accessibility.*

Interaction between Growth stage with Networking and Professional management practices

The influence of professional management practices and networking on the availability of bank financing may not be the same across the two growth stages. At the early stage, networking appears to be a more common and effective strategy to gain legitimacy than at the later stage (Peng, 2003; Peng and Heath, 1996; Tsang, 1994). Since networking with government officials improves firm legitimacy in the eyes of aid donors and government support programs, it increases firm accessibility to these less expensive sources of financing. However, most of the aid money and government support programs are for start-ups—firms at the early stage (Thorne, 1989; Van Auken, 2001). Thus, the negative impact of networking with government officials on bank financing is stronger for firms at the early stage than for firms at the later stage. Therefore, we hypothesize:

> ***H5:*** *The negative relationship between networking with government officials and bank loan accessibility is stronger for firms in their early growth stage than for those in their later growth stage.*

Similarly, networking with others helps firms in their early growth stage to increase legitimacy more than those in their later growth stage. At the early stage, firms have not established their own identity and reputation in the market. Banks and other business partners often rely on the individual reputation of the firm's owners and managers (Butler, Brown, and Wai, 2003; Larson, 1992; Redding, 1990). Similarly, Nguyen et al.'s (2004) found that, for newly established firms, bank officials often focus on the owners' and managers' individual credibility in making loan decisions. In other words, networking with others has a stronger impact on accessing external financial sources for firms in their early growth stage than those in their later growth stage. Because funds from informal sources are more uncertain, expensive, and limited, firms would take advantage of "networking with others" to improve their image with banks and thereby increase their accessibility to bank loans. Thus, we hypothesize:

> ***H6:*** *The positive relationship between networking with others and bank loan accessibility is stronger for firms in their early growth stage than for those in their later growth stage.*

As firms become more established, the positive impact of networking on legitimacy may diminish (Peng, 2003). Butler et al. (2003) suggested that in Southeast Asia, businesspersons tend to be extensively networked, especially those in more established firms. However, the expansion of such networks for more established firms may result in diminishing returns. Peng and Luo (2000) found that networking has less impact on bigger (and usually more established) firms, and that firms need to combine their networking with professional management to gain better performance. From this line of argument, we propose that the adoption of best management practice increases legitimacy more for firms in their later growth stage than for those in their early growth stage. Specifically, we expect that professional management practices will have a stronger effect on access to bank financing for firms at the later growth stage than for those at the early growth stage. Therefore, we hypothesize:

H7: *The positive relationship of professional management practices with bank loan accessibility is stronger for firms in their later growth stage than for those in their early growth stage.*

The Vietnamese Context in Research Method and Findings

We chose Vietnam as the most suitable country to test our hypotheses because the country has gone through a major economic transition process, and yet the formal and informal institutions remain major obstacles to private business (Venard, 1998; Myer and Nguyen, 2005). Economic reform in Vietnam started formally in 1986, and has been primarily implemented since 1989 (Fforde and Vylder, 1996; Buchel and Lai, 2001; Meyer and Nguyen, 2005). The idea of reform in Vietnam was to create a "market economy under socialist guidance" (The VIth Party Congress, 1986). This reflects a dual ideology that describes the government's response to an unresolved battle between two conflicting forces where one pushes toward the market while the other insists on retaining the traditional socialist system.

The dual ideology has caused challenges in developing a comprehensive, market-oriented legal system. Although a number of new laws have been issued in Vietnam, the fundamental objective of providing an even playing field for different sectors is far from being reached (Mallon, 2004; Tenev et al., 2003; Venard, 1998). Managers of private firms view the legal procedure as confusing and ineffective (MPDF, 1999), and few of them are aware of the legal system relating to their businesses (Nguyen and Bryant, 2004). More importantly, enforcement of the newly created laws has been slow and ineffective. This seriously limits the options available for firms to work with new business partners.

Another characteristic of Vietnam's business environment is the underdevelopment state of professional agencies, such as banks and auditing and certification organizations. In developed countries, these organizations serve as a channel through which firms can demonstrate their trustworthiness to new partners (through quality certification or financial audit). In Vietnam, these agencies are sparse in number and nascent in their development. As a result, information on firms is unavailable and unreliable.

Despite these obstacles, the private sector in Vietnam has flourished since the "*Doi moi*" (i.e., Renovation) policy came into effect. The private sector has become an important additional engine of macroeconomic growth, a major source of employment, and a major generator of foreign exchange earnings in Vietnam (Nguyen et al., 2004). However, private firms in Vietnam are facing a number of difficulties, of which limited access to external sources of financing is considered one of the most serious for private sector development. Although bank financing is the most important source of external financing for private firms, these firms have limited access to this source (Nguyen et al., 2004; Tenev et al., 2003). Most firms have to rely on non-external sources of financing, including internal sources of funding (such as companies' reinvested earnings), savings and funds provided by shareholders/management, or the family and friends of management, and loans provided by customers and suppliers. These sources, however, are limited, uncertain, and expensive.

A number of factors serve to constrain greater commercial bank lending to the private sector in Vietnam. First, state-owned banks, which dominate the banking sector, are reluctant to lend to private firms. Second, banks in Vietnam lack legal and information foundations as well as the skills for assessing and managing credit risk (Nguyen et al., 2004; O'Connor, 2000). Finally, bank loans to private firms are very collateral dependent and short-term oriented. Many private firms do not possess the kind of collateral necessary to access bank loans.

Vietnam offers a fascinating context to learn about how private firms gain legitimacy and access to bank loans. Most private firms are young and small. Their status as "privately owned firms" has newly been legitimized, and some of their properties (e.g., land) are owned by the state. Policies and regulations on what they could or could not do are uncertain. There are no public sources that could provide updated and reliable information on them. Yet, they need to persuade banks to lend money to them. In this respect, Vietnam offers an ideal context with an extreme form of entrepreneurship that operates in the absence of a well-established legal infrastructure, contracting norms, and market-oriented ideological underpinnings. The experience of young Vietnamese firms can provide us critical insights into the various conditions and ways by which firms develop legitimacy and access bank loans.

Method

The first stage in our study was to carry out in-depth interviews with six Vietnamese private business owners in manufacturing and ten bank officers who have been involved in lending to private businesses. The objectives of this stage were to test the face validity of the model and our survey instrument. The interviews with bank officers and firm owners were supplemented by documents available from the firms and banks. Each interview lasted from one to three hours. The data from these interviews helped us to better understand the Vietnamese business context from the perspectives of both the firm owners/managers and the bank officials. It also served as a basis for the subsequent survey research, reported in this paper.

Sample and procedure

Following Nguyen et al. (2001), we obtained a list of registered private enterprises from the local government. We hired local researchers who had skills and experience in collecting data to administer the data collection in the two most developed cities (Hanoi in the north and Ho Chi Minh City in the south) and one less developed city in the northern part (Nam Dinh) of Vietnam. These local researchers worked at the cities' Commercial Department or Registration Department. We first trained the local researchers. The local researchers then personally contacted the companies, delivered the surveys, followed-up and collected the surveys. Our respondents were owners or key managers of the firms. By applying this personal approach, we actually obtained a response rate of 95 percent. Out of 214 companies that were randomly selected from the lists approached for responses, 203 completed questionnaires for our analysis

Measures

Growth Stage. Growth stage was measured based on the scale developed by Kazanjian (1988) with some rewording to the titles of the stages to fit with the sample studied. Owner-managers were asked to choose the one that best characterized their business at the time of the survey. We then followed Koberg et al. (1996) to categorize firms in the early and later growth stages.

Networking. For Networking with officials, respondents were asked the extent to which they utilize relationships with government officials at all levels for business purposes. Similarly, for Networking with others, the respondents were asked the extent to which they utilized social networks with managers of other firms, with friends and relatives (who are not government officials) for business purposes in the last three years. Nine questions using a 5-point scale format were used to measure networking, of which six questions were modified from Peng and Luo (2000) and three were newly developed (Cronbach's alpha = .70).

Professional Management Practices. Professional management practices reflect the extent to which a firm adopts best management practices in all functional areas (e.g., marketing, human resource management, operations management, accounting and financial management, strategic management, and planning). Twenty-one questions were adapted from Gadenne (1998) to assess the level to which specific types of professional management practices were used in the firm's business operations. The responses were obtained on a 5-point scale.

Bank Loan Accessibility. It is difficult to directly measure the accessibility of bank loans. We used ratio of bank loan to the firm's total capital as a proxy to estimate the bank loan accessibility. Respondents were asked to indicate bank loans as a percentage of total capital employed by their firms (hereafter: Bank Loan Ratio)

Control Variables. Based on previous studies (Coleman, 2000; Kangasharju, 2000; Crant, 1996; Meyer and Nguyen, 2005), we controlled for owner education, gender, and experience in the current business, their level of proactivity and location (province) of the firm head office.

Analytical methods

We took two steps in testing our hypotheses. In step 1, we split the data into two groups (firms that did borrow from banks and those that did not). We then used logistic regression to examine if the factors hypothesized influence the probability of accessing a bank loan. In step 2, we selected firms that borrowed from banks, took the natural logarithm of the bank loan ratio to create a normally distributed dependent variable. We then examined if the variables of interest influenced the bank loan ratio, using hierarchical regression.

Results

Exploratory data analysis

Factor analysis and reliability analysis were conducted for professional management practices. Twenty-one items that measured the management practices of private manufacturing firms loaded into six factors. Five factors that have Cronbach's alpha of less than .65 were dismissed (DeVellis, 1991). Only one factor had a Cronbach's alpha greater than .65, and was selected for further testing. This professional management measure has six items (product advertising, reward and discipline system, performance appraisal, employee feedback, staff training, written plans and budgets), with a Cronbach's alpha of .80.

Table 1 presents descriptive statistics and correlations of key variables. The results show that the firm's Growth stage, Networking with officials, Networking with others, and Professional management practices were positively correlated with the Probability of having a bank loan ($p < .01$). The average firm in our sample has been in business for 5.5 year, had 66 employees and a chartered capital of VND 2,051 million (equivalent to US$150,000). Generally, firms in the later growth stage had a longer history, larger amounts of chartered capital, and more employees than those in the early growth stage (see Table 2).

Hypotheses testing

We first checked and corrected for violations of the normality assumption, and then proceeded in two steps. In the step 1, we used logistic regression to examine if our independent variables

Table 1 Descriptive statistics and pearson correlations

		Mean	S.D.	1	2	3	4	5	6	7	8	9
1.	Gender (Women)	.18	.38									
2.	Owner education	2.10	3.24	−.02								
3.	Owner experience	13.08	8.56	−.09	−.01							
4.	Owner proactivity	3.98	.62	−.09	.01	.10						
5.	Province	2.12	.83	−.11	.20**	.16*	−.14*					
6.	Growth stage	1.70	.46	−.08	−.07	.08	.19**	−.14*				
7.	Networking with officials	2.99	.81	−.10	.07	.14*	.30**	.07	.10			
8.	Networking with others	3.24	.55	.03	−.09	−.09	.27**	−.06	.25**	.43**		
9.	Management practice	3.50	.66	−.12	−.08	−.09	.29**	−.22**	.30**	.27**	.44**	
10.	Loan probability	.728	.45	−.01	−.18**	−.03	.27**	−16*	.23**	.21**	.38**	.31**
11.	Ln Bank loan	3.22	.64	−.07	−.07	.06	.09	.03	.17*	.01	−.13	−.03

**Correlation is significant at the 0.01 level (2-tailed).
*Correlation is significant at the 0.05 level (2-tailed).

(Growth stage, Professional management, Networking with officials, Networking with others, and the interactions between Growth stage with other variables) influence the Probability of getting bank loan. Table 3 summarizes the logistic regression results.

The model was statistically significant, ($\chi^2 = 52.12$, $p < .001$), indicating that the variables as a set reliably distinguished firms that got a bank loan from those that did not. The model had a success rate of 79.2% in classifying firms into groups. According to the Wald criterion, Networking with officials was negatively related to the Probability of having a bank loan, but this relationship was significant at only a $p < .10$ level. Hypothesis 3 was not supported. Networking with others was positively related to the Probability of having a bank loan ($p < .05$), supporting Hypothesis 4. The interaction between Growth stage and Networking with government officials was positively and significantly associated with the

Table 2 Descriptive Data of the Sample

	Early stage	Later stage	Overall
Company age (year)	3.8	6.3	5.5
Company size (employees)	41	76	66
Company chartered capital (million VND)*	990.8	2051	1720.6

*Exchange rate at the time of the survey: US$1 = VND 15,000

Table 3 Logistic Regression on Probability of Getting Bank Loan

	B	S.E.	Wald
Owner gender	−.09	.51	.04
Owner education	−.16	.16	1.04
Owner experience	−.02	.02	.52
Owner proactivity	.46	.33	1.98
Province	−.29	.25	1.46
Management practice	−.10	1.13	.01
Networking with officials	−1.81[a]	1.05	2.99
Networking with others	4.26*	2.04	4.35
Growth stage	1.79	2.87	.39
Stage*Management	.010	.68	.00
Stage*Networking with officials	1.16*	.58	3.94
Stage*Networking with others	−1.52	1.11	1.88
Constant	−7.88	4.93	2.55
-2 Log Likelihood	183.09		
Cox & Snell R^2	.22		
Nagelkerke R^2	.33		
Model χ^2	52.12***		
Percentage of correct prediction	79.2		

a: $p < .1$; *$p < .05$; **$p < .01$; ***$p < .001$

possibility of having a bank loan ($p < .05$). This suggests that the negative relationship between Networking with officials and the Probability of having a bank loan is stronger for firms at the early stage. Hypothesis 5 was therefore supported. The coefficients of Growth stage (H1), Professional management (H2), and interactions between Growth stage and Networking with others (H6) and with Professional management (H7) were not significant in this logistic regression.

In step 2, we selected only firms that had bank loans. We then performed six hierarchical regression analyses. In Model 1 (control model), only the control variables (owner gender, education, training, and experience, location of head office) were entered into the equation. In Models 2, 3, 4, and 5, the independent variables (Professional management practices, Networking with government officials, Networking with others, and Growth stage) were added one by one into the model. Finally, the interaction variables (Growth stage and Networking with officials; Growth stage and Networking with others, Growth stage and Professional management practices) were entered into the full model (Model 6). If the variables added into Models 2, 3, 4, 5 and 6 have significant effects on the availability of bank financing, then changes in R^2 (from Model 1 to Model 2, from Model 2 to Model 3, etc.) should be significant. We also checked the coefficient of each factor to test the hypotheses. Table 4 summarizes the regression results.

The control model (Model 1) was significant ($F = 2.55$, adjusted $R^2 = .06$, $p < .05$). Owners' education had a significant and negative relationship with the availability of bank financing (ß$= -19$, $p < .01$), suggesting that the higher the owner education, the more likely the firm is to get bank financing (reversed coding on education). Other control variables did not have a significant relationship with the accessibility to bank financing.

Table 4 Results of Regression Analysis on Logarithm of Bank Loan(Coefficients are standardized)

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Control variables						
Owner gender	−.18	−.19*	−.17a	−.15	−.15	−.10
Owner education	−.19*	−.19*	−.20*	−.21*	−.21*	−.21*
Owner experience	.16	.16	.18	.16	.15	.15
Owner proactivity	.01	.02	.06	.08	.08	.06
Province	−.03	−.04	−.02	.02	.02	.03
Main variables						
Management practice		−.06	.01	.06	.06	−.43
Networking with officials			−.24*	−.19	−.19	−1.46**
Networking with others				−.19	−.19	1.81***
Growth stage					.03	1.33*
Interactions						
Stage*management practice						.723
Stage*Networking with officials						1.79**
Stage*Networking with others						−3.79***
F Model	2.552*	2.186*	2.893**	3.021**	2.672**	30.587***
Adjusted R^2	.063	.058	.103	.122	.115	.211
R^2change		.003	.050	.026	.001	.109
F change		.420	6.482*	3.461[a]	.087	5.354**

a: $p < .1$; *$p < .05$; **$p < .01$; ***$p < .001$

When the variables of interest (Professional management practices, Networking with officials, Networking with others, Growth stage) were entered one by one in Models 2, 3, 4, and 5, the models remained significant (please see Table 4 for F and adjusted R^2 statistics). Owner education coefficients remained negative and significant in all models. Except for owner gender in model 2, none of the other control variables were significant.

Growth stage coefficient was not significant in Model 5, but became positive and significant in Model 6 (ß = 1.33, $p<.05$). This indicates that firms at the later growth stage have more access to bank financing than those at the early growth stage. Hypothesis 1 was supported. Professional management practices were not significantly related to bank loan accessibility in any model. Hypothesis 2 was not supported.

Networking with officials had a negative association with bank loan availability in all models and was significant in Model 3 (ß = −.24, $p < .05$) and Model 6 (ß= −1.46, $p < .01$). Hypothesis 3, therefore, was supported. Networking with others was positive and significant in Model 6 (ß= 1.81, $p < .001$). This suggests that when we took into account all other variables and interactions, the more a firm networks with others, the more likely a bank loan is available to the firm. Hypothesis 4 was supported.

The interaction between Growth stage and Networking with officials was positive and significant (ß= 1.79, $p < .01$), suggesting that the negative relationship of Networking with officials on Bank loan accessibility is stronger at the early stage. A simple mean plot (Figure 2) also suggests that networking with official appears to have a clearer negative relationship with bank loan ratios at the early stage than at the later stage. Hypothesis 5 was supported.

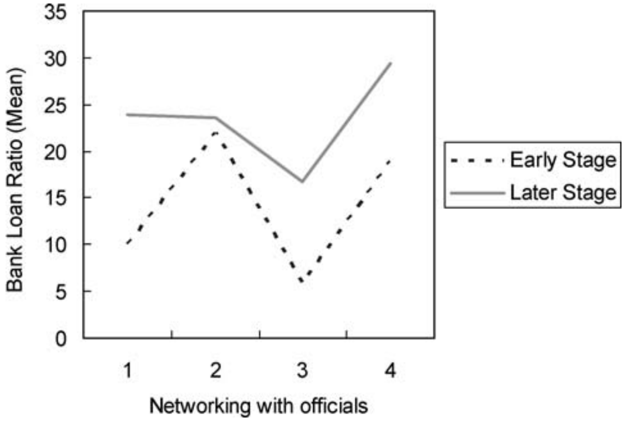

Fig. 2 Mean Plot of Bank Loan Ratios by Networking with Officials at Two Stages

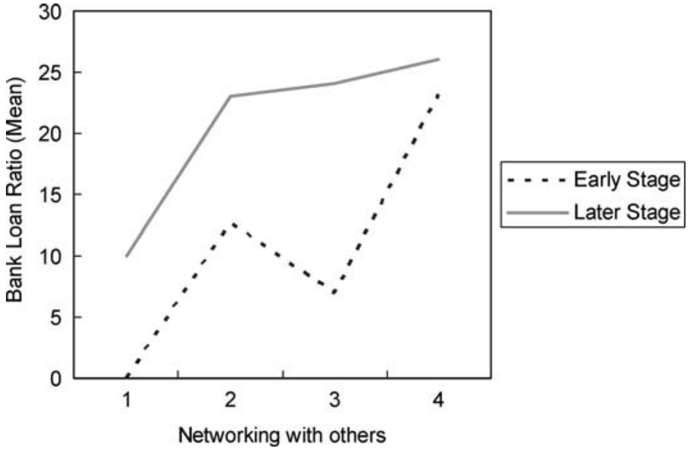

Fig. 3 Mean Plot of Bank Loan Ratios by Networking with Others at Two Stages

Similarly, the interaction between Growth stage and Networking with others had a negative and significant relationship with bank loans (ß=−3.79, $p < .001$). This suggests that the positive relationship between Networking with others and bank loans is stronger for firms at the early stage than for those at the later stage. Figure 3 plots the mean of bank loan ratios on Networking with other managers at two stages. It shows that Networking with others has a stronger positive relationship with bank loan ratios at the early stage than at the later growth stage. Hypothesis 6 was, therefore, supported. In contrast, the interaction between Growth stage and Professional management was not significant. Hypothesis 7 was not supported.

Discussion

Key Results. Our results generally support the thesis that bank loan availability is significantly influenced by firms' legitimacy. We found that firms at the later growth stage have more access to bank financing. Networking with government officials negatively influences bank financing because it helps firms have more access to aid money and government support programs. By contrast, networking with managers of other organizations and friends (networking with others) positively influences firms' accessibility to bank financing. However, the impact of networking on bank financing is stronger for firms at the early stage than for those at the later stage.

Our study makes several important contributions to the management literature. First, our study is one of the few studies that examine the processes and outcomes of institutional influences in transition economies on firms that are not state owned. As Hoskisson et al. (2000) noted, the number of studies using institutional perspective in transition economies is limited, *and* current studies of institutional effects on transition economies have focused mostly on state-owned enterprises. Studies such as our study are important in enriching the institutional perspective and ensuring its generalizability.

Second, by using a contingency approach, we were able to distinguish the benefits of networking for firms at different growth stages. Specifically, we found that the influence of networking on bank financing is stronger for firms at the early growth stage than for those at the later growth stage. This suggests that networking has diminishing influences, and thus, managers need to come up with new competitive weapons as firms grow.

Third, while the role of networking is important anywhere, our study emphasizes its role in building legitimacy for firms in transition economies. A key difference between transition economies like Vietnam and developed economies is the relative role of informal information (from informal networks) and public information. In developed economies, publicly verifiable data (e.g., business data, firm audited reports, and firm history) are the starting point and the foundation of bankers' assessments of firms' creditworthiness (Uzzi and Lancaster, 2003). Informal data (e.g., from social networks) are an add-on, and often serve as background for making loan decisions. In Vietnam, and perhaps other transition economies, informal data often appear to be the foundation of the bankers' assessment of firms' creditworthiness. Public information serves as additional data that can help make the application packages legally justifiable (Nguyen et al., 2004). The importance of informal networks found in this study is consistent with this argument.

We did not find support for our hypotheses regarding the relationships between professional management and bank financing. We offer several possible explanations for this result. First, as Peng (2003) observed in the context of transition economies, the transitions generally move through two phases. The first phase is characterized by a predominantly relationship-based transaction structure, while the second phase is a more rule-based structure. Vietnam may still be in the first phase of its transition in which relationship-based transactions are the norm. In such a context, best management practices may not readily help firms to become "isomorphic" to the environment. Second, our results could also be because of the lack of appropriate knowledge and skills among bank officers about professional management. A number of bank officers may not have been sufficiently trained about professional management practices. These officers lack the skills and knowledge to recognize and appreciate firms with high levels of professional management. We expect that, in time, best management practices may increasingly help firms obtain their legitimacy and access to bank financing.

Managerial Implications. Our data suggest that firms' legitimacy, in addition to their efficiency, is critical to accessing bank loans. The literature has provided rich evidence that networking and professional management practices are critical factors for small firms to enhance their legitimacy and access bank loans. We go further in this study by examining these relationships at different growth stages. Entrepreneurs' networks with government officials have stronger effects in the early growth stage of firms. Under the absence of effective market institutions and infrastructures, social networks appear to be the most effective channels for young start-up firms to be known, endorsed, and trusted. The more people know about them and their qualities, the more chances these firms have in accessing bank loans.

For bankers too, networking is critical. While conventional skills, such as financial analysis and credit scoring are necessary, they may not be greatly applicable in the current Vietnamese context. Instead, such skills as relationships building, data collection and crosschecking, and management auditing (in a broader than just financial sense) may be necessary.

This implies that education and training programs for both private business owners and bankers should pay proper attention to such skills. Besides conventional skills, such as developing business plans and financial analysis, owners of private firms should be trained on developing effective networks. Similarly, bankers should be trained on working under uncertainty—network building, data collection and verification, business sensing, in addition to the more conventional skills that their counterparts in developed countries have.

Limitations and Suggestions for Future Research. The first limitation of this study is our cross-sectional design that limits the validity of the implied causal links of our model. We suggest longitudinal research on how networking and management practices impact bank financing over time. In addition, our measure of bank financing (percentage of bank loans in firm capital structure) does not allow us to fully examine the relationships between management practices and bank financing. Future research should include other measures of bank financing, such as firm owner's assessment of bank loan availability for their firms. Our research was conducted in Vietnam, which does not allow us to compare countries in different phases of transitions (Peng, 2003). We recognize that extending our research into cross-national settings would allow us to better compare the impact of cultural and institutional contexts on bank financing to private firms.

Conclusion

The private sector is believed, and expected to be, an engine of economic development in transition economies. These young and small firms badly need external financial resources for growth. Ironically, they have an extremely difficult time demonstrating their creditworthiness. This paper shows that networking helps firms to resolve this dilemma, though it should be used differently at each growth stage. In time, the private sector may become more competitive. If it does, it will do so because these firms survive through networking, and gradually apply professional management practices. When formal institutions are under-developed, an alternative is to build legitimacy through people in one's networks.

Appendix: Survey items on networking

Six items adapted from Peng and Luo (2000)
(five point Likert scale from "very little" to "very extensive")

Ties with government officials: Please circle the number best describing the extent to which top managers at your firms have utilized personal ties, networks, and connections during the past three years with:

(1) political leaders in various levels of the government
(2) officials in industrial bureaus

(3) officials in regulatory and supporting organizations such as tax bureaus, state banks, commercial administration bureaus, and the like.

Ties with managers at other firms: Please circle the number best describing the extent to which top managers at your firms have utilized personal ties, networks, and connections during the past three years with:

(1) top managers at buyer firms
(2) top mangers at supplier firms
(3) top manager at competitor firms

Three items developed for this research
(five point Likert scale from “*very little*” to “*very extensive*”)

Ties with other managers, relatives and friends: Please circle the number best describing the extent to which top managers at your firms have utilized personal ties, networks, and connections during the past three years with:

(1) members of business associations
(2) members of social clubs or associations
(3) relatives and friends who do not belong to any of the above categories

Acknowledgment The authors thank Scott Bryant and Nick Freeman for their valuable comments on an earlier draft of this paper.

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