DETERMINANTS OF CONTINUITY IN CONVENTIONAL INDUSTRIAL CHANNEL DYADS

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Recently, increasing attention has been paid to the question of how to build stable, long-term relationships between manufacturers and members of conventional channels. This descriptive field study concerns a basic requirement for building long-term relationships, which is the expectation by a marketing intermediary that the relationship will last. Hypotheses about the continuity of relationships are developed from the literature on social exchange, bargaining, and negotiation. These hypotheses are framed as a simultaneous equation system, which is estimated via three-stage least squares on a sample of 690 relationships (dyads) involving manufacturers and their independent sales agents (manufacturers' representatives). Results substantially support the model, highlighting the importance of interpersonal relationships in insuring the continuity of the dyad.

(Distribution Channels; Sales Force Management; Interorganizational Relations; Strategic Alliances)

Market globalization and deregulation are intensifying competitive rivalry and motivating manufacturers to develop strategic advantages by establishing long-term relationships with channel members, as well as customers and suppliers (Mattsson 1978). These relationships have been referred to as "networks" (Thorelli 1984) and "domesticated markets" (Arndt 1979).

Conventional distribution channels (independent intermediaries selling the products of multiple manufacturers to multiple buyers) have historically been and continue to be the most common method of distributing goods and services (Stern and El-Ansary 1982). Further, the usage of independents, such as manufacturers' representatives and distributors, is growing rapidly and is expected to continue (Reinhart and Coleman 1976, Taylor 1981). Indeed, Business Week (1986a) forecasts that the hallmark of the post-industrial corporation will be vertical disaggregation, i.e. the extensive use of independent entities, such as distributors. However, control and coordination may be sacrificed when independent entities perform business activities. The development of long-term relationships is an approach that combines the advantages of vertically integrated distribution systems (control and coordination) with the advantages of systems utilizing independent channel members (flexibility, scale economies, efficiency, and low overhead).

The degree to which a long-term relationship has been established with a channel

1 See Anderson and Weitz (1986) for a discussion of the advantages and disadvantages of vertical integration.
member is reflected in the channel member's perception of the likelihood that the relationship will continue. At the most basic level, a manufacturer cannot hope to garner the benefits expected from a long-term relationship unless the channel member is convinced the relationship is likely to last. Given the expectation of continuity, research (Etgar 1976, Arndt 1979, Thorelli 1984, Williamson 1985) indicates that independent channel members are more likely to:

- assist the manufacturer in new product development,
- conduct and report formal and informal market research concerning the manufacturer's products,
- engage in activities with a longer term payoff, e.g. missionary selling, customer education, and other forms of sales support,
- be responsive to the manufacturer's requests,
- react to unforeseen contingencies with flexibility and good will.

This paper integrates prior research on continuity in relationships to develop a framework describing the channel member's perception of relationship continuity with manufacturers (producers) as a function of the characteristics of the producer, the producer's policy decisions and procedures, and the nature of the producer-channel member relationship. The framework and associated hypotheses are tested by estimating a simultaneous equation system using data describing 690 relationships from the channel member's perspective. Managerial implications and directions for future research are presented.

Theoretical Framework

The theoretical framework shown in Figure 1 extends prior research on channel relationships by incorporating behavioral research on social exchange, bargaining, and negotiations. In this section, we develop the model according to its three major elements: continuity, trust, and communications.

Continuity of Relationship

The model in Figure 1 indicates that the continuity of a channel relationship, as seen by the channel member, is a function of the (1) trust between the parties, (2) imbalance

![Figure 1. Hypothesized Relationships.](attachment:figure1.png)
of power, (3) communication between parties, (4) stakes in the relationship, (5) manufacturer’s reputation for “fair play,” (6) age of the dyad. Each of these relationships is discussed in the remainder of this section.

**Trust.** We define trust as one party’s belief that its needs will be fulfilled in the future by actions undertaken by the other party. This definition is consistent with the following definition used by Pruitt (1981, p. 16) in the context of negotiation: trust is the belief that the other party is also ready to undertake coordinative actions. Trust plays a critical role in the development of long-term relationships because short-term inequities are inevitable in any relationship (Williamson 1985). At the most basic level, one party must undertake actions before the other party and thus must rely on the other party to honor its commitments (Kronman 1985). Thus, any type of coordinative behavior leaves parties in the relationship open to exploitation. Through trust, parties in a relationship develop confidence that, over the long-term, short-term inequities will be corrected to yield a long-term benefit (Dwyer, Schurr and Oh 1986). Mutual trust is more likely than one-way trust. A channel member is unlikely to have faith in a producer if the channel member believes the producer mistrusts it (Burgess and Huston 1983).

**Power Imbalance.** Power is defined as the ability of one party (A) to get another party (B) to undertake an activity that B would not normally do. More formally stated, A’s power over B is the difference between the probability of B’s undertaking an activity after A has intervened and the probability of B undertaking the activity without A intervening (Stern and El-Ansary 1982). The concept of power can also be viewed in terms of dependency. When A is highly dependent on B, B is more powerful (Emerson 1962). In a channel context, the availability of alternative distributors would reduce the producer’s dependency on a distributor and thus contribute to its power over the distributor. Conversely, the availability of alternative suppliers would contribute to the distributor’s power over the supplier.

While the immediate impact of power is apparent, the long-term effectiveness of power as a control mechanism has been questioned (Emerson 1962, Cook and Emerson 1978). When a power imbalance exists, the high-power channel member will attempt to exploit its advantage and the low-power channel member will become dissatisfied with the relationship (Anderson and Narus 1984). Thus, imbalanced channel relationships are characterized by less cooperation and greater conflict (Dwyer, Schurr and Oh 1987, Robicheaux and El-Ansary 1975, Stern and Reve 1980). This result is also found in bargaining research (Pruitt 1981). Snyder and Diesing (1977) suggest that bargaining relationships shift from competitive to cooperative when a power balance is achieved. Research on social exchange has also found that relationships balanced in terms of power are more stable than unbalanced relationships (Burgess and Huston 1983). Thus, we suggest that asymmetries in power force one channel member to act in a manner that is not consistent with its economic interests and motivates the channel member to right the imbalance.²

Of course, imbalance also occurs when the distributor dominates the producer. When this occurs, the producer may also feel its economic interests threatened, which jeopardizes the continuity of the relationship in the long term. In this vein, Ford (1978) finds that

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² The actions of franchised automobile dealers in the United States illustrate the instability of achieving long-term relationships based on exploiting a power imbalance. Traditional U.S. automobile manufacturers have used their superior power position to control their franchised dealers. To shield themselves from the potentially adverse economic consequences resulting from the power imbalance, dealers initially lobbied for legislative protection. More recently, the imbalance of power has been corrected by the development of super dealers who have leveraged multiple dealerships, often involving foreign manufacturers, to diminish the power of U.S. manufacturers and blunt their ability to control channel activities (Business Week 1986b).
in stable channels no member possesses enough power to assume the "channel captain" role.

Communications. Intensive two-way communication concerning plans, programs, expectations, goal setting, and performance evaluation is critical for resolving disputes and coordinating actions (Arndt 1979). Walton and McKelsie (1965) emphasize the need for explicit communication for achieving and monitoring integrative agreements and for preventing misunderstandings from arising. Intensive communication should lead to better informed parties, which in turn should make each party more confident in the relationship and more willing to keep it alive. Consistent with this reasoning, Rosson (1977) found that new car dealers considering which manufacturer to represent relied heavily on the accessibility of management to make their selection.

Stakes. The level of stakes refers to the importance of the activities involved in the relationship to at least one of the parties. When a relationship is unimportant to the parties involved (they have low stakes in the dyad), neither party will be willing to invest much effort in the relationship (Dwyer, Schurr and Oh 1986). Due to a lack of effort, the parties will focus attention on other opportunities (Pruitt 1981, Burgess and Huston 1983, Scanzoni 1983). In contrast, if at least one party has significant stakes in the dyad, s/he will be motivated to pay attention to the relationship, thereby increasing the likelihood of continuation.³ Note that our conceptualization of stakes differs from dependency. Stakes indicates the importance of activities associated with the relationship, not importance of the specific relationship.

Reputation. Producers develop a reputation among channel members concerning whether they "play fairly." Their reputation declines the more frequently they terminate relations and appropriate profitable accounts and territories (Research Institute of America 1975). Often such manufacturers set impossibly high standards for their agents. And as such manufacturers are demanding, they tend to be dissatisfied and prone to change channel members. Hence, their relationships with channel members can be expected to destabilize and ultimately terminate.

Age of Relationship. Channel relationships can exhibit considerable inertia. Relationships that have lasted a long time are more likely to continue than relationships that are younger because over time adjustments are made, unsatisfactory and unalterable dyads terminate, and the surviving dyads achieve a high degree of fit. This result repeatedly occurs in studies of the longevity of marriages (Burgess and Huston 1983).

The preceding arguments are summarized in the following proposition:

\[ P_1, \quad \text{The continuity of a channel relationship increases as:} \]
(a) the level of trust between the channel members increases,
(b) the power in the relationship becomes more balanced,
(c) communication between the channel members increases,
(d) stakes in the relationship increase,
(e) the manufacturer’s reputation for fairness to channel members improves,
(f) the relationship persists over time.

Determinants of Trust in a Channel Relationship

The concept of trust has been little used in channels research. Dwyer, Schurr and Oh (1986) argue that "as a pivotal facet of expectation development, trust deserves priority attention" (p. 28). Manufacturers send "signals" that they intend to work together with

³ Pruitt (1981) reviews bargaining literature wherein the parties in games manifest more cooperative behavior when at least one party stands to make significant profits (or losses) from the game’s outcome.
channel members over the long run by safeguarding their reputations and by supporting the channel member's efforts. These signals help build the level of mutual trust in a dyad.

Reputation. Individuals and firms provide signals of their future actions through their presentations. People are especially attuned to behaviors which allow them to infer cooperative rather than competitive tendencies. An individual is more willing to commit to another if the other person holds a reputation for cooperative behavior (Pruitt 1981). The same mechanism operates among firms and serves to check misbehavior, thereby building trust, especially in long-term relationships (MacCauley 1963).

One way that producers signal their intentions is by the frequency with which they terminate relations and the degree to which they appropriate profitable accounts and territories. The producer’s resulting reputation for “foul play” should make a channel member think that the manufacturer is strictly concerned with its own interests, rather than being concerned with the mutual welfare of the dyad. Channel members are more trusting if they see manufacturers cooperating with other parties (Pruitt 1981).

Support. Providing backup support (e.g. product training, promotional materials, response to requests for information) is an important way for manufacturers to influence downstream members of conventional channels (Etgar 1978b). Lack of such support is a common complaint among channel members, leading to resentment and poor relationships. On the other hand, manufacturers who support the downstream members of the channel are rewarded with better relationships (Delano 1984).

Aside from sending signals about their trustworthiness, producers can also build trust levels by developing a common perspective with their agents. A common perspective facilitates a sense of understanding, agreement, even similarity. This in turn builds up the parties’ confidence in each other, giving each party the belief that it can count on the other. Four elements of a common perspective are: goal congruence, shared values, an established (older) relationship, and two-way communication.

Goal Congruence. One of the most difficult and pervasive problems in channel management is disagreement over goals, particularly in respect to growth objectives (Stern and El-Ansary 1982). This is to be expected when independent organizations must work together, but it undermines relationships by creating conflict over goals and the tactics to achieve them. When a dyad agrees on goals, conflict is minimized and trust can develop (Stern and El-Ansary 1982).

Cultural Similarity. Much has been written about the effect of cultural and geographical barriers on the nature of business relationships (Davidson 1982). These barriers create divergent values, which make it difficult to come to trust the other party. In particular, problems often arise in the common situation whereby a channel member is from one country and the manufacturer is from another. These problems are particularly acute when the two countries are far apart culturally and/or geographically (Root 1982). The essence of the problem is lack of shared values and methods, which manifests itself as differences in cognitive styles, operating methods and choices. Hence, dyads involving foreign (in our case, non-U.S.) manufacturers are expected to be more fragile.

Age. One reason why older dyads continue is that experience breeds trust. Scanzoni (1983) and Pruitt (1981) argue that the older a relationship, the greater the likelihood it has passed through a critical “shakeout” period of conflict and influence attempts by both sides. If the dyad survives this period, the foundation is laid for personal trust, mutual liking, and a good working relationship. Further, even without passing through crises, partners come to learn each other's idiosyncracies and deepen mutual understanding over time (Williamson 1983). This improves the affective quality of the relationship (see Sullivan and Peterson 1982).
Communication. Communication improves trust by resolving disputes and misunderstandings and by aligning perceptions and expectations (Etgar 1979). Further, communication reduces role ambiguity; in turn, independent channel members prefer dealing with manufacturers who present them with less role ambiguity (Teas and Sibley 1980). Finally, much of communication is informal and behind the scenes, which greatly enhances trust and coordinative behavior (Pruitt 1981).

Power Imbalance. When one party possesses inordinate leverage over the other, the weaker party becomes mistrustful, i.e. apprehensive about the stronger party’s intentions (Pruitt 1981, Dwyer, Schurr and Oh 1986). As noted earlier, there is ample evidence that their concern is justified: stronger parties often exploit the dependence of their partners. Hence, we expect that power imbalances will diminish the level of trust in a channel dyad.

In summary, we propose that:

\[ P_2. \ A \text{ channel member’s trust in a manufacturer increases:} \]
\[ (a) \text{ the better the manufacturer’s reputation in its dealings with channel members}, \]
\[ (b) \text{ the more the manufacturer offers sales support}, \]
\[ (c) \text{ the more congruent the manufacturer’s and channel member’s goals}, \]
\[ (d) \text{ the greater the cultural similarity between the manufacturer and channel member}, \]
\[ (e) \text{ the older the dyad}, \]
\[ (f) \text{ the higher the communication level in the dyad}, \]
\[ (g) \text{ the more balanced the power in the dyad}. \]

Determinants of Communication

Communication between manufacturer and agent, though widely recognized to be important to building and maintaining a relationship, frequently occurs at very low levels. This is because communication requires time and effort, which parties may not find time (or motivation) to invest. Further, communication can be unpleasant, leading to avoidance of further communication. Below we examine five factors which influence the level of unpleasantness of communication, as well as the parties’ implicit calculation as to whether a relationship is worth the time and effort of communicating.

Stakes. Minor relationships do not warrant the time, effort, and opportunity cost of a great deal of communication (Research Institute of America 1975). When one or both sides have small stakes in the dyad, one or both sides will not make the effort to communicate.

Cultural Similarity. When cultural similarity is slight, differences in thoughts, values, and actions should necessitate high levels of communication to iron them out. However, in practice a common reaction is to withdraw, operating relatively independently (Root 1982). Sometimes this is because the principal does not even attempt to understand the foreign market, preferring to delegate to the agent. Sometimes low communication occurs simply because working out the differences would require more time and effort than the relationship warrants or would create unpleasant confrontations.

Competence of Liaison Personnel. The channel member regularly comes into contact with boundary spanning personnel employed by the manufacturer. These include regional sales managers, technical support staff, and assorted personnel from marketing, production, shipping, and accounting. How well these boundary spanners do their jobs impacts how well the channel member performs. Hence, it is critical that liaison personnel be perceived by the channel member as competent. If not, the channel member may refuse to “waste time” communicating with them (Research Institute of America 1975). Channel members may “bypass the factory” (reduce communication) and devise their own solutions when liaison personnel are perceived as ineffective.
Age of Relationship. Over time, parties become well acquainted with each other, which allows them to predict each other’s reactions and to coordinate activities, even with less communication. The understandings that develop over time permit efficiencies in communicating, which constitute a significant experience-based asset (Williamson 1985). This suggests that older relationships can get by with lower levels of communication than do younger relationships.

Trust. In social relationships, people tend to talk to those with whom they feel comfortable, while avoiding those with whom they are uncomfortable. Similarly, salespeople tend to call on customers with whom they have good relationships, while avoiding the potential unpleasantness of calling on customers with whom they have less pleasant relationships (Shapiro 1977). Hence, we expect that the players in a trusting channel dyad will communicate more than those in less trusting dyads.

These arguments lead to our third proposition.

\[ P_3. \quad \text{The communication level in the dyad increases:} \]
(a) \text{the higher the stakes in the relationship,}
(b) \text{the more culturally similar are the manufacturer and channel member,}
(c) \text{the more the channel member perceives the manufacturer’s liaison personnel as competent,}
(d) \text{the younger the dyad,}
(e) \text{the higher the trust level in the relationship.}

Data Analysis and Results

The Setting

The channel member selected for this study is the independent sales agent or manufacturers’ representative (“rep”). Reps, which are widely used in most industries, sell the products of multiple manufacturers (“principals”) (Anderson 1985). Their “portfolio” of principals provides complementary rather than competing products, which the rep sells in return for a commission. The manufacturers’ representative bears all sales expenses, the largest of which is usually the cost of personnel. Reps are sales agents only. Unlike distributors, they do not take title to what they sell. Thus, the manufacturer retains pricing authority, stocks, ships, and extends credit. The rep is often the first step in the channel of distribution. The relative simplicity of the task (selling only) makes this channel relationship somewhat easier to study, as there are fewer potential confounding factors to measure.

Data Collection

Three hundred member firms attending the annual Electronic Representatives Association (ERA) convention were asked to participate in a study of patterns of time allocation among principals. In return for their cooperation, rep firms received a computerized analysis of their present time allocation compared to the optimal time allocation, as derived via a decision calculus method. The time allocation results are not part of the current study.

Ninety-five firms (a 32% response rate) filled out an extensive questionnaire detailing the nature of their relations with each of their top (largest in commission dollar terms) eight principals. After missing data and allowing for reps with fewer than eight principals, 690 relationships (dyads) form the data base of this study. The questionnaire was completed by the person with the most knowledge of the firm’s relationships with its principals, generally the owner. In larger firms, which have managing partners, the owner conferred with the manager to respond.
The average 1983 sales volume\(^4\) of the agencies in the sample was $13.7 million, generating $706,000 in commission income. On average, the agencies had 15 employees, including 7 outside salespeople, and 15 principals, of which the top 8 generated 89% of commissions and used 90% of the rep agency’s available selling time. Hence, for practical purposes, most of the rep’s portfolio of principals was covered in data collection.

These agencies are not a random sample of ERA members, nor for that matter of reps in general. Our respondents are larger, more experienced, and better established rep agencies. It is interesting to see what relationships these firms enter and sustain, given their experience and success. However, these reps presumably have already deleted many “mistaken” (ill advised) relationships from their portfolio. The effect should be to reduce real variance in the measures, making insignificant results more likely. On the other hand, the relatively large sample size (690) increases statistical power, as well as the odds of reflecting a wide range of dyads.

**Measures**

The questionnaire, developed and pretested with the assistance of ERA, obliged respondents to respond to each question or scale item for all principals before proceeding to the next question. The purpose was to minimize halo effects across questions. The measures of the constructs are summarized in Table 1. CONTINUATION, TRUST, COMMUNICATION, IMBALANCE (of power), REPUTATION, CONGRUENCE (of goals), and COMPETENCE were assessed with multiple-item scales; STAKES was measured using a two-item index; AGE was simply the duration of the relationship; and SIMILARITY (of cultures) was a one-zero indicator of a U.S. producer.

The reliabilities of most scales are consistent with Nunnally’s (1978) criterion of coefficient alpha of 0.7; however, the reliabilities of CONTINUATION, IMBALANCE, and REPUTATION are below this criterion but greater than the 0.5 level of much of the published research in marketing (Churchill and Peter 1984).

**Validation of CONTINUATION Measure.** Five months after the first wave of data collection, a second wave was collected. This wave contained a large number of sensitive and difficult time allocation questions. Hence, of 95 reps responding initially, 80 responded to the follow-up. These 80 indicated, for each relationship, whether it had been terminated. Of 551 relationships, 25 had ended. Of the terminated group, the mean CONTINUATION score is 9.20, while in the nonterminated group, the mean CONTINUATION score is higher, 11.52 (since CONTINUATION is the sum of two 7-point scales, 14 is the maximum). This difference is statistically significant at the 0.01 level, even when dummy variables for the agencies are introduced to control for the possibility of an agency effect.\(^5\) Although five months is a short time, it appears that the CONTINUATION measure is a valid indicator of the likelihood a relationship will continue.

The correlation matrix of these measures appears in Table 2. There appears to be no evidence of serious multicollinearity among the exogenous variables (4 through 11 in Table 2).

**Model Estimation and Results**

**Testing for Agency Effects**

The system of equations represented in Figure 1 was estimated via three-stage least squares (3SLS), a method which offers a combination of consistent estimators and high

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\(^4\) Data were collected in 1984.

\(^5\) When the CONTINUATION measure is regressed upon a dummy variable for termination, the termination dummy is significant, which is not altered by adding agency dummies.
TABLE 1

Summary of Measures

<table>
<thead>
<tr>
<th>Construct</th>
<th>Sample Item (Response Scale)</th>
<th>Number of Items</th>
<th>Cronbach Alpha</th>
</tr>
</thead>
<tbody>
<tr>
<td>CONTINUATION (expectation)</td>
<td>Likelihood of being terminated in next two years (not very likely–very likely)(\text{(R)})</td>
<td>2</td>
<td>0.65</td>
</tr>
<tr>
<td>TRUST</td>
<td>How much you trust the principal to be fair (very little–great deal of trust)</td>
<td>2</td>
<td>0.84</td>
</tr>
<tr>
<td>COMMUNICATION</td>
<td>Detail in which principal communicates expectations (very little–great detail)</td>
<td>11</td>
<td>0.87</td>
</tr>
<tr>
<td>IMBALANCE (of power)</td>
<td>Who possesses more power in your relationship? (This principal is more powerful–equal–our firm is more powerful)(\text{(D)})</td>
<td>2</td>
<td>0.58</td>
</tr>
<tr>
<td>REPUTATION (negative)</td>
<td>How frequently does this principal replace existing reps? (never–very often)*</td>
<td>2</td>
<td>0.52</td>
</tr>
<tr>
<td>AGE</td>
<td>Length of time representing principal (logarithm)</td>
<td>1</td>
<td>—</td>
</tr>
<tr>
<td>CONGRUENCE (of goals)</td>
<td>Agreement on growth objectives (little–much agreement)*</td>
<td>2</td>
<td>0.80</td>
</tr>
<tr>
<td>SUPPORT</td>
<td>Evaluation of backup support (poor backup–excellent backup)*</td>
<td>1</td>
<td>—</td>
</tr>
<tr>
<td>COMPETENCE</td>
<td>Competency of principal personnel you deal with (not very–very competent)*</td>
<td>2</td>
<td>0.90</td>
</tr>
<tr>
<td>SIMILARITY (cultural)</td>
<td>1 = US principal 0 = foreign principal</td>
<td>1</td>
<td>—</td>
</tr>
<tr>
<td>STAKES</td>
<td>What percentage of the principal’s sales dollars is generated by this rep agency? What percentage of the rep’s income is generated by this principal? (summed index)</td>
<td>2</td>
<td>—</td>
</tr>
</tbody>
</table>

\(\text{*} = \text{measured on seven-point scales.}\)
\(\text{(R)} = \text{item reversed.}\)
\(\text{(D)} = \text{item converted to absolute value of: [response–4] where 4 is the midpoint (labeled “equal”).}\)

efficiency (Intriligator 1978). But because each dyad is one of up to 8 reported by each rep agency, an issue here is the possible lack of independence of the observations. Hopkins (1982) notes that this is a pervasive problem and suggests that researchers test for the

TABLE 2

Correlation Matrix

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
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<tr>
<td>6</td>
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<td>11</td>
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</tr>
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</table>
possibility of “group effects” in “individual” observations, even when there is no reason
to expect group effects (here, features of the sales agency which may confound the
principal/agent relationship).

Agency effects, if any, can be incorporated via a dummy variable for each agency.
Four “demographics” of the agency (the number of full-time equivalent employees,
annual revenues, annual sales expenses, and the number of principals represented) may
also prove relevant.

With no a priori reason to expect agency effects, one approach would be to include
all possible agency effects in each equation of the system represented in Figure 1. Un-
fortunately, however, the agency variables as a whole are highly collinear. Hence, the
addition of approximately 300 terms (94 of 95 agency dummies plus the four agency
demographics in each of three equations) would complicate estimation of the system.
Further, there is no a priori reason to expect agency effects.

Therefore, a more parsimonious procedure was used to pre-select the most relevant
agency effects. First, the model was estimated as is (no agency effects). Then the residuals
of the equations for CONTINUATION, TRUST, and COMMUNICATIONS were re-
gressed in stepwise fashion against: (i) the four demographic descriptors of the agencies;
(ii) dummy variables representing the agencies. If the residuals are “white noise” (i.e.
there are no group effects), these residuals will be unrelated to the agency variables.
However, in this case, the residuals do appear to be related to some of the agency dummies
and demographics. Hence, 24 agency dummies were added to the continuity equation,
28 were added to the trust equation, and 23 dummies (plus number of full-time-equivalent
employees) were added to the communication equation.

These selected group effects were then included in a re-estimation (via three-stage-
least squares) of the model in Figure 1.

Estimation Results

The results, in general, are in accord with the hypothesized relationships. The estimated
parameters are reported in Table 3. The group effects variables introduced as controls
are not reported, as they are not of substantive interest.

Continuation of the Dyad. Relationships which reps expect to continue characterized
by a high level of trust (0.88) and few signals implying the principal has a negative
reputation (−0.22). These relationships are also older (0.31) and involve higher stakes
(0.17). Power imbalance has a negative effect (−0.07), significant at the 0.05 level (one-
tailed test), while communication does not have a statistically significant impact on the
perceived probability that the relationship will continue.

Trust. As seen above, trust has an important impact on the stability of the dyad.
Trust in turn is enhanced by the degree of two-way communication between principal
and agent (0.88). Trustful relationships also tend to be older (0.15). Relationships with
foreign principals are not significantly different from those with American principals.
However, more trusting relationships occur with principals who provide support (0.21)
and whose goals are perceived as congruent with the rep’s (0.48). Markedly less trust
arises when a principal has a poor reputation in dealing with reps (−0.28). Further, reps
perceive a lower level of mutual trust when leverage is imbalanced, i.e. one party dominates
the other (−0.05, significant in a one-tailed test).

Communication. The extent of two-way communication is greater in dyads with

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6 We thank Abba Krieger and Paul Green for suggesting this approach.
7 First-stage (no group effects) and second-stage (group effects included) results are not greatly different: however, the first-stage results are more often nonsignificant and include one wrong sign. The omission of group effects, then, is a misspecification that masks relationships of interest.
### TABLE 3

**Estimation Results**

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>CONTINUATION</th>
<th>TRUST</th>
<th>COMMUNICATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>INTERCEPT</td>
<td>11.26 (64.40)**</td>
<td>-0.11 (0.75)</td>
<td>0.89 (1.14)</td>
</tr>
<tr>
<td>TRUST</td>
<td>0.88 (11.80)**</td>
<td>NA</td>
<td>1.72 (9.11)**</td>
</tr>
<tr>
<td>COMMUNICATION</td>
<td>0.02 (0.91)</td>
<td>0.05 (3.21)**</td>
<td>NA</td>
</tr>
<tr>
<td>LN (AGE)</td>
<td>0.31 (4.31)**</td>
<td>0.15 (3.42)**</td>
<td>-0.73 (3.21)**</td>
</tr>
<tr>
<td>STAKES</td>
<td>0.17 (3.78)**</td>
<td>NA</td>
<td>0.95 (6.77)**</td>
</tr>
<tr>
<td>IMBALANCE (of power)</td>
<td>-0.07 (1.70)*</td>
<td>-0.05 (1.83)*</td>
<td>NA</td>
</tr>
<tr>
<td>REPUTATION (negative)</td>
<td>-0.17 (3.07)*</td>
<td>-0.28 (9.69)**</td>
<td>NA</td>
</tr>
<tr>
<td>SIMILARITY (cultural)</td>
<td>NA</td>
<td>-0.05 (0.37)</td>
<td>0.09 (0.12)</td>
</tr>
<tr>
<td>SUPPORT</td>
<td>NA</td>
<td>0.21 (3.67)**</td>
<td>NA</td>
</tr>
<tr>
<td>CONGRUENCE (of goals)</td>
<td>NA</td>
<td>0.48 (14.46)**</td>
<td>NA</td>
</tr>
<tr>
<td>COMPETENCE</td>
<td>NA</td>
<td>NA</td>
<td>0.73 (5.24)**</td>
</tr>
<tr>
<td>$R^2$ (from 2SLS)</td>
<td>0.57</td>
<td>0.70</td>
<td>0.46</td>
</tr>
<tr>
<td>System weighted $R^2$</td>
<td>0.66</td>
<td></td>
<td></td>
</tr>
<tr>
<td>$N$</td>
<td>681</td>
<td>681</td>
<td>681</td>
</tr>
</tbody>
</table>

$t$ statistics are in parentheses.

** Significant at $p < 0.01$.

* Significant at $p < 0.05$.

higher trust levels (1.72). Further, older relationships involve less communication rather than more (−0.73), suggesting the parties have developed such a good understanding of each other that they can make their points more efficiently (i.e., with a lower level of communication). Communication levels do not appear to be lower with foreign principals, despite potential barriers. Finally, more communication occurs in dyads which involve higher stakes to one or both parties (0.95) and in which the principal’s personnel are perceived to be competent (0.73).

**Discussion**

The data are largely in accord with the proposed model. In particular, stable dyads are characterized by cordial interpersonal relationships. This underscores the importance of trust, even in business transactions, as a supplement to or even a substitute for formal legal contracts. It appears that business relationships are indeed governed as much by implicit understandings and practices as by legal obligations (MacNeil 1978, Goldberg 1980).

The mutual trust of a relationship is in turn strongly influenced by the level of communications in the dyad. Trusting dyads involve a high level of two-way communication, even to the point of becoming involved in each other’s business planning. Thus, communication, while it does not appear to have a direct impact on the continuity of the relationship, is critical to build the trusting relationships that in turn create stability.

Older, established dyads appear to possess inertia, that is, a built-in tendency to continue. Further, older relationships are more trusting. They are also “communication efficient”: less intensive communication occurs, presumably because the point can be made relatively easily when the dyad involves established, well understood partners. The results suggest that dyads which survive the relatively fragile early years are a significant asset to both principals and agents.
Dyads which involve significant stakes are also more likely to continue that are minor relationships. These relationships warrant more effort on the part of at least one partner. Hence, such dyads have higher levels of communication (making them more trustful). Further, such dyads are less likely to terminate, even after allowing for the effect of greater communication.

Consistent with the bargaining and negotiation literature, conventional channel dyads where one partner dominates the other are less stable. In such relationships, trust deteriorates, as does the agent's confidence in the future of the dyad. It is noteworthy that power imbalances are much more common in administered channels, such as in franchising arrangements. Within such structures, the participants often recognize the power imbalance a priori; indeed, franchising has been described as an arrangement wherein the franchisee voluntarily cedes power in return for contractual guarantees of high levels of assistance from the franchisor (Anand and Stern 1985). But in conventional channels, power imbalances are the exception. In the absence of an elaborate contingent claims contract (Williamson 1985), such imbalances appear to have a destabilizing effect.

Manufacturers' past behavior also appear to affect their current relationships, even if the behavior involved other agents. A negative history with channel members sours the relationship, indirectly destabilizing the dyad. A reputational mechanism appears to exist and to operate in such a way as to penalize manufacturers who repeatedly drop and replace agents and who encroach on the agency's business by appropriating house accounts. This is reflected in Apple Computer's announcement that it will no longer hold house accounts in order to "solidify dealer ties" (Sales and Marketing Management 1985, p. 60).

 Principals interested in solidifying channel ties by other means can do so by improving the level of trust in their channel relationships. This can be done by heightening communication, offering better sales support, and selecting channel members with similar goals (or gradually cultivating similar goals). It may also be done by appointing competent personnel to perform the boundary spanning (liaison) role with the channel member. Competent personnel means better communication, which in turn increases trust.

Foreign manufacturers who have entered the U.S. market may not be representative of foreign manufacturers in general. These manufacturers appear, from these data, to be as capable of building trusting relationships and of achieving high levels of communication as are American principals, in spite of possible cultural and geographical barriers.

Limitations

A drawback of this study is the modest reliability of several of our measures. Lack of reliability attenuates correlation, which makes insignificant results more likely. The generally significant findings here may be due in part to the large sample size. Churchill and Peter (1984) note that it is common to trade reliability (multiple items) for sample size (since responses are more likely if questionnaires are shorter).

While the model shown in Figure 1 reflects interpretation of relevant research, there are alternative relationships that could be considered. Clearly, our specification is not unique. However, it is supported by prior research.

Finally, one industry, rather than several, is represented. However, the industry (electronic components) is very large and broad, containing multiple sectors at various stage of maturity. Hence, this industry should be fairly representative rather than idiosyncratic.

Future Directions

An intriguing possibility is to recast the age of a relationship. The social exchange literature suggests that trust is enhanced by the cumulative experience of the parties in the dyad. This study used age as a proxy for cumulative experience. However, young relationships may be very intense, while old relationships may have always occurred at
a low level. Hence, a measure of cumulative experience, rather than lifespan, may better capture the history of a dyad. Another area for future research concerns the other side of the coin: what factors create the expectation of continuity on the part of the manufacturer.

Conclusion

We have examined a subset of the many factors that stabilize relationships in channels of distribution. The results suggest that manufacturers wishing to create lasting relationships within conventional channels can indeed do so; stability can be achieved without creating special arrangements, such as franchising. Stability can be enhanced by avoiding building a poor reputation for treatment of channel members, making the dyad an important relationship to at least one party (raising the stakes), and by cultivating trust. Trust, in turn, is enhanced by congruent goals, a good reputation, and good communication (facilitated by competent liaison personnel). Older relationships appear to be more stable than newer ones, perhaps reflecting a process of working on our problems and developing understandings. These older dyads do not seem to need high communication levels, suggesting that communication efficiencies accrue over time.

Perhaps most striking is the interlocking role of communication and trust. Trust facilitates communication, and in turn communication builds trust (a critical determinant of relationship continuity). It is common to overlook or downplay the importance of human relations in business dealings, and this is often appropriate. However, at least from the viewpoint of the independent channel member, creating and sustaining long-lived arrangements appears to require an element of the personal.8

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