The influence of family firms on the sustainability of start-up/nascent enterprises: a decision-making perspective

The Influence of Family Firms on the Sustainability of Start-up/Nascent Enterprises: A Decision-Making Perspective

Louise Scholes, You Yi, Raymond Hu, Mathew Hughes, Paul Hughes

Abstract

We examine the influence of family and family businesses on the sustainability of start-up/nascent enterprises set up by family members. Family firms can expand by setting up new enterprises so that their offspring or siblings can start their own business. This has many advantages for the established and for the new firms. For the established firms funds provided for the start-up can be ring-fenced so the established firm can grow with reduced risk. It also provides family firms with a means of training the younger generation before they take over the whole family business. Sustainability for the start-up can come from the provision of additional resources that they often lack such as additional funding, access to a network of stakeholders such as a skilled workforce, customers, suppliers, and management expertise. However, there may be some disadvantage for the fledgling firm with this arrangement if there is conflict in the decision-making process between a dominant family firm founder and the new CEO of the fledgling business. This raises interesting questions about how decision-making in the start-up/nascent firm will be affected by the family firm and how this in turn affects its sustainability in the longer term.

Introduction

The influence of family firms on the sustainability of start-up/nascent high tech enterprises, set up by members of the family, is of interest since family firms can play a significant role in establishing and supporting new businesses. We explore this relatively new area from a decision-making perspective.

Family support of sustainable entrepreneurship, especially in relation to start-up/nascent firms, is an important issue for researchers, practitioners and policy makers because start-ups are the seed bed of all firms and can contribute significantly in the longer term to economic development (Westhead and Wright, 2011). Without sustainable entrepreneurship these firms may not survive. Sustainability is particularly important for start-ups where initial resources are limited yet significant resources are needed for innovation. Strategic decisions at this stage of the business life cycle, and their ultimate impact on resource orchestration, are crucial to success. While there has been a significant body of research focusing on the resource requirements of start-ups (Lee et al., 2001), there has been little research on the context in which the entrepreneurship is occurring (Wright and Stigliani, 2013; Westhead and Wright, 2011; Zahra and Wright, 2011) or on the decision-making processes themselves (Unger et al., 2011) or on the role that family firms play in this entrepreneurial process (Zahra, Wright and Abdelgawad, 2014).

In terms of the context, family firms can set-up new businesses for a variety of reasons. First, it can represent a means of creating new products with a view to growing the business. The risk of failure in this case can be mitigated by ring-fencing funds for the start-up so that if it fails the parent company does not suffer financially (Miller et al., 2015). Second, it provides the family firm with a means of training the next generation, a form of apprenticeship, before they take over the business from the incumbent of the parent firm. For the fledgling firm it could provide an element of sustainability that would otherwise not be there by providing additional resources such as funding, access to its networks of stakeholders (skilled workforce, customers, and suppliers), and additional human resources such as management expertise. Any strategic decisions to start and support new companies will also be related to the goals of the family company whether they are family or non-family centered, economic or non-economic (Chrisman et al., 2012; De Massis, Di Minin & Frattini, 2015).

Decision-making is critical to the strategic choices made by all firms and little attention to date has been paid to research that links individuals interests and cognition to organizations decisions (Gavetti et al., 2007). The management expertise resource is of particular interest here as decisions made as a result of this influence may have positive or negative consequences for the sustainability of the fledgling firm. Influence from the management expertise in the family firm (for example, the founder of the family firm) that leads to appropriate strategic decisions for the fledgling firm could enhance its sustainability but conflict in the decision-making process between a dominant family firm founder and the offspring CEO of the fledgling business may lead to strategic decisions that ultimately damage the business.

Decision-making is therefore crucial for establishing a successful strategic direction for the firm and for appropriate orchestration of resources, and family firms provide the context in which this decision making is taking place and where influence on the high tech start-up/nascent firm by another family firm member can potentially have positive or negative consequences for the young firm. This raises interesting questions about how decision-making in the start-up/nascent firm will be affected by the family firm and how this in turn affects its sustainability in the longer term.

There is a gap in the literature on the role family firms play in entrepreneurial activity in relation to start-up activity and in particular the effect that decision-making has on the sustainability of these ventures. This research therefore addresses calls to look at this in terms of the context of entrepreneurial activity in family firms (Zahra and Wright, 2011; Zahra, Wright & Abdelgawad, 2014; Wright and Stigliani 2013) and also explores the importance of goals on decision-making, and cognition in family firm research (Chrisman et al., 2012; Unger et al., 2011).

The aim is to examine the influence of the family firm founder (or other family member) on the sustainability of start-up/nascent high tech enterprises, set up by the offspring of the family firm founder, from a decision-making perspective.

RQ: Will the influence of the family firm on decision-making enhance or diminish the sustainability of the start-up/nascent firm?

Literature

Family firms can exist in a variety of ownership and governance configurations but little attention has been paid to date about these configurations and the pursuit of entrepreneurial opportunities of family firms (Zahra, Wright and Abdelgawad, 2014). Family firms can set up subsidiaries for the purpose of creating new products, diversifying the business, and by doing so effectively ring-fence risk. The sustainability of start-ups/nascent firms will be related to the strategic decisions made, and these decisions in turn will depend on the cognitive characteristics of the individuals involved and the influence these individuals have over each other. To explore sustainability we will therefore examine both the decision-making processes that take place in the start-up/nascent firm and the cognitive characteristics of the individuals involved in the family firm and in the start-up/nascent firm as these are directly related to the decision-making outcomes. This research therefore combines decision-making theory and cognitive theory to explore the consequences of strategic choices on the sustainability of fledgling ventures that are spun out of family firms.

Decision-making theory is categorized as either normative (planned) or descriptive (improvised). Planning requires processing of information to make rational choices (Wiltbank et al., 2006) whereas improvisation is adaptive and intuitive based on incomplete information (Wiltbank et al., 2006; Bakken, 2008).

The cognitive theory of decision-making can help to understand the way managers think, their mind-set, and the impact this may have on strategic choices. Managerial cognition leads to decisions are made systematically based on accountability, compensation schemes, and quantifiable budgets (Wright et al., 2000) whereas entrepreneurial cognition is associated with the use of heuristics, (simplified decisions) based on limited information and complex situations and is often associated with entrepreneurs (Wright et al., 2000; Barron, 1998). This leads to combinations of mind-set and decision-making (Figure1) where the optimum situation for a start-up/nascent firm is a founder with an entrepreneurial mind-set combined with improvised decisions making (Quadrant D). In the ideal situation the leaders of the two entities would have similar mind-sets and decision-making characteristics; both entrepreneurially minded, both making use of improvised decision making enhancing the sustainability of the fledgling company.

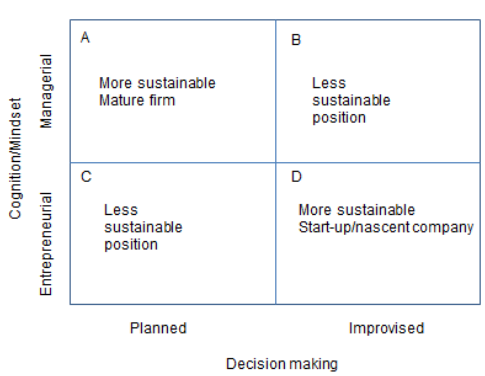

Fig 1. Cognition/Mind-set versus decision making

However if the two leaders have different characteristics then sustainability of these fledgling ventures could be reduced (quadrants A, B or C).

Method

The research will follow a qualitative, case study method, combining interviews, observations and document analysis to explore the effects of the parent family firm on the start-up/nascent company. Data will come from six firms attached to an entrepreneurial incubator at Hubei University of Technology in Wuhan, and six UK family firms with subsidiaries run by offspring. Preliminary data presented here comes from Chinese start-ups in Wuhan (Hubei) who all received government funding and were less than three years old at the time of interview (July 2016)

Preliminary Results

*Company One (*Hubei Niutaili Environmental Technology Ltd)

(1) Parent firm is in the same industry, operating independently but sharing the market. (2) One of the management team is also a relative. (3) The start-up entrepreneur, the founder's son, started the business partly due to lack of employment outside of China. (4) Operational (day-to-day) decisions are made by the board of the start-up (includes the start-up founder). (5) Strategic decisions are made with the family founder.

Company Two (Wuhan Cuiyu Environmental Technology Co. LTD）

(1) The start-up business is in a different industry from the parent firm. (2) The founder of the start-up relies on the network and funding of his father (the parent family firm). (3) Decisions are influenced by the parent of the founder.

References

Bakken, B.E. (2008). On improving dynamic decision-making: implications from multiple-process cognitive theory. Systems Research and Behavioral Science, 25(4) 493-501.

Baron, R. 1998. Cognitive mechanisms in entrepreneurship: Why and when entrepreneurs think differently than other people. Journal of Business Venturing, 13, 275-294.

Chrisman JJ, Chua JH, Pearson AW, et al. (2012). Family involvement, family influence and family-centered non-economic goals in small firms. Entrepreneurship Theory and Practice 36, 267–293.

De Massis A., Di Minin A., & Frattini F. (2015). Family-driven innovation: Resolving the paradox in family firms. California Management Review, 58(1), 5-19

Gavetti, G., Levinthal, D. A. and Ocasio, W. (2007). 'Neo-Carnegie: the Carnegie School's past, present, and reconstructing for the future'. Organization Science, 18, 523–36.

Lee C, Lee K and Pennings JM (2001). Internal capabilities, external networks and performance: A study on technology-based ventures. Strategic Management Journal 22(6-7), 615–640.

Miller, D., Wright, M., Le Breton-Miller, I., & Scholes, L. (2015). Resources and Innovation in Family Businesses: The Janus-Face of Socioemotional Preferences. California Management Review, 58(1), 20–41.

Unger JM, Rauch A, Frese M and Rosenbusch N (2011). Human capital and entrepreneurial success: A meta-analytical review. Journal of Business Venturing 26(3), 341–358

Zahra, S. a., & Wright, M. (2011). Entrepreneurship's Next Act. The Academy of Management Perspectives, 25(4), 67–83.

Westhead, P., & Wright, M. (2011). David Storey's optimism and chance perspective: A case of the Emperor's new clothes? International Small Business Journal, 29(6), 714–729.

Wiltbank, R., Dew, N., Read, S. and Sarasvathy, S.D. (2006). What to do next? The case for non- predictive strategy, Strategic Management Journal, 27(10), 981-98.

Wright M, Hoskisson R and Busenitz L (2000). Entrepreneurial growth through privatization: The upside of management buy-outs. Academy of Management Review 25(3), 591–601.

Wright, M., & Stigliani, I. (2012). Entrepreneurship and growth. International Small Business Journal, 31(1), 3–22.