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Does business group affiliation help firms achieve superior performance during industrial downturns? An empirical examination

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ABSTRACT

Does affiliation with a business group enhance a firm's performance? What is the potential effect of this affiliation especially in declining economic periods? The literature provides contradictory results on this proposition. In this study, the authors explore the role of business group affiliation as a firm-specific factor and its impact in different environments, adding to our understanding of the firm-growth phenomenon. The empirical context is a large sample of firms registered in the United Kingdom, drawn from the FAME database. The analysis provides evidence for significant impact of business group affiliations on firm growth, especially during adverse economic conditions. However, the business group–firm growth relationship is moderated by firm-specific characteristics (e.g. firm size), and group specific characteristics (e.g. type of ownership and country of origin). Regarding the latter, it is specifically revealed that the impact of group affiliation is not uniform across all countries, a possibility that has been ignored in the international business literature. Among its contributions, this research introduces a novel typology of firms in growing and declining industries. The proposed typology enables us to advance propositions with respect to varying trajectories of business affiliations for firms of different size and nationality/region of origin of business groups.

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1. Introduction

Downturns are part of the industry life cycle. All industries periodically suffer from fluctuations in the demand for their products and services, imposing serious challenges to the firms operating in them (Ma, Yao, & Xi, 2006; Mascarenhas & Aaker, 1989). The 2008 global economic recession is a bitter reminder of such dramatic disruptions. Decline in customer demand and sales, productivity and profitability, accelerated competitive rivalry, and deep organisational changes of the

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surviving firms are only some of the reported outcomes of such periods. Nevertheless, even the most adverse conditions do not affect all firms uniformly. Some, operating in the same sector, not only escape the worst impact (Bamiatzi & Kirchmaier, in press; Geroski & Gregg, 1997; Kitching, Blackburn, Smallbone, & Dixon, 2009) but also use such downturns to restructure and refocus into more profitable market segments (Purkayastha, Manolova, & Edelman, 2012; Tan & Matthews, 2010). The research reported in this article finds strong empirical evidence for the view that firms can grow while operating in such 'adverse' conditions.

The observation that firms grow and prosper despite operating in declining markets, while at the same time others, trapped in a negative climate, shrink and downsize, suggests that firm-specific factors are able to offset the negative effect of adverse environmental conditions on firm performance. This is consistent with the long-established contention in the strategic management research, propounding the prevalence of firm versus industry effects (e.g. Bamiatzi & Hall, 2009; Hawawini, Subramanian, & Verdin, 2003; Rumelt, 1991; Short, Ketchen, Palmer, & Hult, 2007), resulting in differences among firms in the same industries.

In the present study, further light is shed on the above phenomenon by exploring a factor that has received limited attention in the relevant literature – the role of business group affiliation. By business groups, we refer to the constellation of independent firms that share common ownership and administrative control. The overall objective is to explore the impact of business group affiliations among firms that operate in declining industries. What are the benefits bestowed upon those firms as a result of their affiliation to domestic and international business groups? We contend that this issue is of utmost importance to scholars of international business since the effect of group affiliation is *not* uniform across all countries. In other words, the 'country of origin' may influence the relationship between business group affiliation and firm performance – a possibility that is yet to be examined.

The role of business group affiliation in emerging markets, like Chile, South Korea, Turkey, and India, has already received some attention in the past. In emerging markets, typically suffering from serious market inefficiencies, business groups have been credited to act as "functional (market) substitutes" (Guillen, 2000: 363), providing the stability these markets require. Consequently their existence has been closely related to the performance of their affiliated firms (Douma, George, & Kabir, 2006; Khanna & Rivkin, 2001; Singh, Nejadmalayeri, & Mathur, 2007; Stuart, 2000). Empirically though, consensus has yet to be reached in regards to the impact of such affiliations on individual firm performance. In fact, whilst some studies portray business groups as positively influencing firm performance, others provide evidence over their 'parasitic' nature and their consequent disruptive role on performance (Khanna & Yafeh, 2007). The current study bridges this gap in the literature by providing fresh data depicting a clearer view of the role of business group affiliation on particularly firm growth.

While the literature on the role of business group affiliations in emerging markets is considerable, this issue has been largely ignored in advanced economy settings. The few studies on business group affiliation in advanced economies confirm the existence of such formations among especially high-growth firms, but not their direct contribution on individual firm performance (Iacobucci & Rosa, 2005; Lechner & Leyronas, 2009). We contend that it is timely to extend the literature beyond the context of the emerging markets. After all, even in the advanced markets, conditions do exist where industries or markets fail (e.g. during industrial downturns and/or recessionary periods). Under these circumstances, stability provided by the business group affiliations can prove extremely beneficial, especially to the most affected members of the industry, the smaller firms (Pearce & Michael, 1997; Varum & Rocha, 2011).

The United Kingdom, in particular, represents an appropriate setting for empirical testing for several reasons. First, it offers diversity in terms of the existence of business groups, and type and scale of firms and industries. Second, it has experienced both economic growth and bust cycles in recent years. Third, a highly reliable longitudinal database exists about industries and firms. This database incorporates critical variables which allow us to test for additional relationships. Utilising a sample of 62,000 firms from 450 SIC-4 sectors, the present research sheds considerable light on the role of business group formations during adverse conditions by exploring their impact on individual firm performance in declining industries. Probit analysis is employed to estimate main effects of business group affiliation as well as moderating effects (firm size, ownership type, and country of origin). Findings are further compared and contrasted with evidence from growing industries to provide a clear ground for new theory building.

The remainder of this article is organised as follows. First the theoretical background that has inspired our research questions is explored. Next, the methodology is described, followed by the findings. Concluding remarks, limitations, and practical implications are offered in the final section, along with future research propositions.

2. Theoretical background

2.1. Theory of firm growth and the environment

Deciphering the 'black box' of firm growth has attracted the interest of both academics and practitioners for more than five decades (for a seminal exposition, see Edith Penrose, 1959; for an exhaustive literature review see Macpherson & Holt, 2007; Mascarenhas & Aaker, 1989; McKelvie & Wiklund, 2010; Storey, Keasey, Watson, & Wynarczyk, 1994). Nevertheless, despite the voluminous extant empirical research, our knowledge of what makes firms grow is incomplete (Davidsson, Achtenhagen, Naldi, & Parker, 2007; Provan, Fish, & Sydow, 2007) especially under adverse economic conditions.

One reason for this is the existence of numerous internal and external factors associated with firm growth, hindering the comparability and generalisation of past findings (Davidsson, Delmar, & Wiklund, 2008). Yet only a handful of these factors

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