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The impact of family involvement on the investments of Italian small-medium enterprises in psychically distant countries

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ABSTRACT

In this paper we investigate a sample of 122 Italian manufacturing small to medium-sized family firms, and analyse the effects of the degree of family involvement on their decisions to invest in psychically distant countries. Our findings indicate that higher family involvement tends to correspond to a lower number of foreign direct investments in psychically distant countries. Additionally, the firm's age has a moderating effect on the relationship between family involvement and investments in psychically distant countries. When we analyse younger firms, family involvement turns out to be negatively associated with these investments, while this relationship is slightly positive when we consider older firms. These results allow us to move beyond family/non family owned comparative studies and provide a more nuanced view of family firm internationalization.

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1. Introduction

Family firms are the predominant form of business enterprise in the world (Faccio & Lang, 2002), although the actual percentage varies according to the definition being used and the industry and country under investigation. To date, much attention has focused on establishing how family firms differ from non-family firms, with consensus being reached on the fact that the non-economic factors in the management of the firm, such as desire for family control, emotional attachment and identification of family members with the firm, represent the main differences (Le Breton-Miller & Miller, 2013; Gómez-Mejía, Cruz, Berrone, & Castro, 2011).

Recently, the internationalisation of family-owned small-medium enterprises (SMEs) has attracted research attention (*e.g.* Gallo & Garcia Pont, 1996; Zahra, 2003; Fernandez & Nieto, 2005, 2014; Claver, Rienda, & Quer, 2007; Gómez-Mejía, Makri, & Larraza-Kintana, 2010; Kontinen & Ojala, 2010, 2012). However, while there is general agreement that the idiosyncratic nature of family-owned SMEs influences the internationalisation decision in different ways, the direction of these effects is still not well understood. Clearly, internationalisation can make economic sense for family-owned SMEs (Zahra, 2003, 2005; Casillas, Moreno, & Barbero, 2010) because revenue may increase and risk is spread across many markets (Kim, Hwang, & Burgers, 1993), whilst reducing dependence on a particular (domestic) set of suppliers and customers (Kogut, 1985). However, Gómez-Mejía et al. (2010) found that family firms tend to show lower levels of internationalisation than non-family firms, arguing that non-economic factors preservation can act as a potential inhibiting factor. For example, family owners may wish to maintain managerial control, limiting the firm's dependence on outside managers or stakeholders such as funders, as well as perceiving international markets as being inherently risky (Sharma, Chrisman, & Chua, 1997; James, 1999; Fernandez & Nieto, 2005; Graves & Thomas, 2006; Naldi et al., 2007; Barba Navaretti, Bugamelli, Cristadoro, & Maggioni, 2012; Chang, Ming-Sung, & Kuo, 2014).

Undoubtedly, family ownership is both heterogeneous and complex, and empirical evidence on the impact of family involvement in internationalisation activities is diverse: depending on the conditions, it can be negative (*e.g.*, Casillas & Acedo, 2005; Sirmon, Arregle, Hitt, & Webb, 2008; Fernandez & Nieto, 2005; Gómez-Mejía et al., 2010) or in some cases positive (*e.g.*, Zahra, 2003; Abdellatif, Amann, & Jaussaud, 2010). Consequently, scholars have called for a shift in emphasis of family business studies from comparative family/non-family studies to more in-depth analyses of the heterogeneous nature of family firms (Sharma, Melin, & Nordqvist, 2014). Therefore we respond to this

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challenge by using a sample of Italian family manufacturing SMEs to analyse the relationship between the degree of family involvement and foreign direct investment (FDI) in psychically distant countries and how this relationship changes when the firm's age is considered.

Previous research on Italian family-firm internationalization has mainly focused on the difference between family and non-family firms, in studying their export propensity (Barba Navaretti, Faini, & Tucci, 2008; Cerrato & Piva, 2012; Piva, Rossi-Lamastra, & De Massis, 2013) and foreign investment propensity (Piva et al., 2013). The main findings on Italian family firms are in line with those of several other researches on firms in other countries (Fernandez & Nieto, 2005; Thomas & Graves, 2005; Sirmon et al., 2008) showing that family firms are less likely to export than non-family firms (even if they highlight different results in various industries) (Piva et al., 2013).

In our study we focus on FDI and, in particular, on investments in psychically distant countries. Psychic distance (PD) or "the perceived differences between the characteristics of a firm's domestic environment and those of a foreign country" (Child, Frynas, & Rodriques, 2009:209) has been investigated in family firm internationalisation (Claver et al., 2007; Graves & Thomas, 2008). However, it is still an under-researched area (Laufs & Schwens, 2014). This is surprising, given that psychically distant countries may present promising opportunities (Kontinen & Ojala, 2010; Miller & Breton-Miller, 2006; Stamm & Lubinski, 2011; UNCTAD, 2013; Zahra, 2003). Psychic distance is usually associated with a high level of perceived risk. It consequently represents an important element in the investment decisions of family SMEs worthy of research attention.

Thus, our focus on FDI in psychically distant countries enables us to explore an under-researched area and also to focus on a dependent variable that illustrates the strategic dilemmas that family-owned SMEs face when internationalising (Laufs & Schwens, 2014). We propose that, in family-owned SMEs, the degree of family involvement negatively impacts on investment in psychically distant countries because high levels of family involvement in the ownership/management of the firm may stretch both resources and managerial skills whilst increasing the desire to preserve the family's socio-emotional wealth (Berrone et al., 2012).

We also propose that the problems and perceived risks associated with psychic distance may be particularly critical for younger internationalising family SMEs. Indeed, as highlighted in the Uppsala model (Johansson & Vahlne, 1977), firms increase their market knowledge incrementally, and experience in foreign markets helps reduce risk aversion with regard to internationalisation. Moreover, in older family SMEs it is likely that new generations may bring new international orientation, commitment, and competences (Fernandez & Nieto, 2005; Merino, Monreal-Pérez, & Sánchez-Marín, 2014; Calabrò, Brogi, & Torchia, 2015) potentially enhancing internationalisation.

Our findings contribute to the family business and internationalisation literatures. This research goes beyond a family/non-family SME comparison because it investigates the role of family involvement in family-owned SMEs that use more committed entry modes than exporting in the form of FDI in psychically distant countries, while previous research on family business internationalisation has focused mainly on exporting (Abdellatif et al., 2010; Fernandez & Nieto, 2014). Additionally, we provide novel insights on how the relationship between family involvement and FDI in psychically distant countries changes according to the firm's age, offering a nuanced view of the heterogeneous nature of family-firm internationalisation. Our results highlight that among older family SMEs the degree of family involvement does not have an inhibiting effect on investment in psychically distant countries, whilst this is the case of younger family SMEs. This has important implications for family firms when developing their internationalization process in the early stages of the firm's life cycle.

The remainder of the paper is organised as follows. In the following sections we present a review of the literature and develop two hypotheses. The methodological approach is then presented. Thereafter we present the findings and robustness checks, followed by discussion and our conclusions.

2. Literature review

2.1. Family firms' internationalisation and investments in psychically distant countries

The first reference to the concept of "psychic distance" was made by Beckerman (1956), who highlighted the importance of perceived distance between countries and the consequences for international business. According to Beckerman (1956), trade between countries is determined not only by their physical distance but also by other factors that create a sense of difference, such as language, personal relationships and culture. Some scholars have viewed psychic distance as the uninformed nature or the ignorance of a firm with regard to the characteristics of a foreign market (Kogut & Singh, 1988; Child et al., 2009). According to this perspective, only after increased commitment and understanding of foreign markets do firms internationalize to countries dissimilar to, or culturally distant from, their domestic market (Arenius, 2005).

Hofstede's (1991, 2001) cultural dimensions and Kogut and Singh's (1988) composite index have been widely used to measure psychic distance (see, for example Tihanyi, Griffith, & Russell, 2005). However, it should be noted that culture is only one dimension of psychic distance; therefore to use the Hofstede (1991) dimensions as the sole indicators of psychic distance may be misleading and potentially inaccurate (Dow & Karunaratna, 2006; Evans & Mavondo, 2002; Tihanyi et al., 2005; O'Grady & Lane, 1996). In this regard, Brewer (2007) claimed that there is no conclusive evidence that culture is even a central element of psychic distance. For this reason, other measures have been developed (Brewer, 2007; Dow & Karunaratna, 2006; Evans & Mavondo, 2002; Sousa & Bradley, 2006). The factors commonly used in these studies have been culture, language, religion, political and legal issues, economic conditions, and business practices (Ojala & Tyrväinen, 2009). These studies suggest that the psychic distance concept is influenced by various factors and cannot be approximated by cultural differences alone (Hakanson & Ambos, 2010).

It has been argued that psychic distance is of great importance and plays a strong role in the internationalization process of SMEs and family-owned businesses (Crick & Jones, 2000; Kontinen & Ojala, 2010; Laufs & Schwens, 2014; Madsen & Servais, 1997). When studying investments made by family firms in psychically distant countries, the Uppsala model seems particularly pertinent (Pukall & Calabrò, 2014). The Uppsala model presents internationalisation as an incremental learning approach (Johansson & Vahlne, 1977). It suggests that firms initially tend to focus on the domestic market due to their lack of knowledge about foreign markets, and subsequently start internationalization through exporting to accumulate such knowledge and grow over time (Johansson & Vahlne, 1977, 1990; Claver et al., 2007; Gómez-Mejía et al., 2010; Kontinen & Ojala, 2010). The model implies that firms increase their new market knowledge in a stepwise manner and increasingly commit resources to foreign markets in subsequent cycles. Initially, firms will enter psychically (and often geographically) close markets; later, as learning takes place, they enter new international markets with greater psychic distances.

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