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An integrative process model of organisational failure

Joseph Amankwah-Amoah *

Bristol University, School of Economics, Finance & Management, Social Sciences Complex, 8 Woodland Road Clifton, Bristol, BS8 1TN, United Kingdom

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ABSTRACT

In spite of the perennial interest in organisational failure and burgeoning streams of research, much of the existing literature has developed in isolation across multiple social science disciplines. Consequently, this has obscured the past accomplishments and allowed confusion to persist. The review and synthesis of the literature across scholarly fields led to the development of an integrative process model of causes, stages of decline leading to failure and consequences of organisational failure. The proposed integrated framework brings together an array of theoretical explanations for the causes of business failure. The study uncovered uncharted territories and unresolved issues which have the potential to further illuminate our understanding of the subject. The study offers a number of contributions to theory and practice.

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1. Introduction

Over the past three decades, liquidation, discontinuance, bankruptcy and mortality studies, like many other branches of management, have coined specialised nomenclatures and approaches to describe organisational failure and its consequences (see Cochran, Darrat, & Elkhal, 2006; Evans & Borders, 2014; Mellahi & Wilkinson, 2004). An unfortunate outcome has been that many non-specialists have lost touch with the advances made and key debates in the field (Mellahi & Wilkinson, 2010).

Over time, the burgeoning stream of research has become increasingly complex and fragmented across multiple social science disciplines including accounting, strategy, organisation studies, entrepreneurship and business history. Consequently, the lack of integration has not only failed to stimulate cross-fertilisation but also obscured the past accomplishments made in addressing the fundamental questions such as “why do firms fail?” and “what happens when firms fail?” Against this backdrop, confusion has emerged and the field is also “getting bigger without necessarily maturing” (Mellahi & Wilkinson, 2010, p. 532; Walsh & Bartunek, 2011). Although past studies have called for a much integrated discussion on the causes of business failure (Mellahi & Wilkinson, 2004), to date, scholars have largely sidestepped the key issue.

The main purpose of this study is to review and synthesise the literature on the antecedents and consequences of organisational failure. The study makes at least two main contributions to the literature. First, in contrast to the much of the existing literature, this study develops an integrated process model which links the antecedents, stages

of decline and consequences of organisational failure. In addition, the review of the literature helps in clarifying the various facets of the subject. It also led to the identification of a number of uncharted territories and unresolved issues with potential to further illuminate our understanding of the subject.

The rest of the paper is organised as follows. The next section sets out the definition of organisational failure and defines the scope of the review. This is then followed by an examination of the existing state of knowledge in the field. On the basis of the review and synthesis, the final section outlines directions for future research.

2. Defining organisational failure

Over the years, some scholars have viewed organisational failure as either the discontinuance of the business (Hamilton, 2006; Walsh & Bartunek, 2011) or the discontinuance of ownership of the business (Everett & Watson, 1998). Discontinuance of ownership may occur when the owner makes a decision to offload the firm and its assets to potential buyers or investors. One of the problems of viewing business failure as a discontinuance of business is that it primarily views failure as entry and exit rates (Everett & Watson, 1998). Many businesses often cease operations after the owners retire and therefore to equate such events to failure may not be an accurate reflection (Everett & Watson, 1998). In this context, organisational failure is defined as a situation where the firm ceases operations and loses its identity due to inability to respond and adapt to changes in the external environment in a timely fashion (Cameron, Sutton, & Whetten, 1988; Hager, Galaskiewicz, Bielefeld, & Pins, 1996). In other words, organisational failure refers to “the actual demise of the organization when an entire company goes out of business ... the organization completely ceases to exist” (Marks & Vansteenkiste, 2008, p. 810). This definition excludes studies on firms

* Tel.: +44 0 117 3317936.

E-mail address: Joseph.amankwah-amoah@bristol.ac.uk.

experiencing temporary performance problems and then generates a turnaround.

3. Scope of the review

In order to ensure a wider coverage of the literature, we replicated the systematic literature review approach advanced by Webster and Watson (2002) and Short (2009), and used by past reviewers such as Short, Ketchen, Shook, and Ireland (2010). To assemble the literature, keywords such as discontinuance, insolvency, mortality, death, exit, failure, bankruptcy, liquidation, closure and setbacks, which have all been used to refer to organisational failure, were employed to search electronic databases such as Scopus, ProQuest, EBSCO Business Source Complete, Emerald, ScienceDirect, ISI Web of Knowledge and JSTOR. This approach was particularly useful in identifying and tracing past studies. The preliminary search resulted in the identification of a large number of articles which focused on the broad themes of failure including business, performance, service, system, operations and strategic failures. In order to further narrow down the voluminous number of studies with the general theme, additional keywords were employed in combinations (e.g. “failure”, “closure”, “bankruptcy”, “mortality” and “exit”). This process, in tandem with reading the abstracts and introductions of the articles, led to further elimination of studies outside the scope. This process paved the way for including studies where the focal firm ceases operations. In addition to the search of articles published in academic journals, working papers, a number of book chapters and conference proceedings were also examined for their inclusions to help ensure a comprehensive coverage of the literature. Thus, the study encompasses insights across multiple disciplines such as organisation studies, strategy and entrepreneurship to enrich our understanding of the current state of knowledge. Based on synthesis of the literature, an array of internal (firm-level) and external factors were identified which interact to precipitate business failure. As outlined in Fig. 1, these factors also influence the consequences of business failure. Below, we tease out the array of scholarly works uncovered.

4. Organisational failure: An organising framework

The review demonstrated that the theoretical and empirical research on the antecedents of organisational failure has tended to be polarised between the deterministic and voluntarist perspectives. A deterministic perspective in classical industrial organisation (IO) and organisation ecology (OE) literature suggests that managers are constrained by exogenous factors over which they have little or no control (Moulton, Thomas, & Pruett, 1996). This suggests that organisational leaders are powerless in the face of changes in their environment. On the other hand, the voluntaristic perspective in organisation studies (OS) and organisational psychology (OP) literature suggests that managers' actions, inactions and perceptions are

the fundamental causes of organisational failure (Mellahi & Wilkinson, 2004; Nutt, 1999, 2002). Appendix A provides a summary of studies on organisational failure across multiple disciplines. The table sets out some key findings from each study. Below, we expand on these pivotal findings.

5. Research on the external antecedents to organisational failure

The classical IO traced its roots to the field of economics and assumed that a firm's management team can influence neither industry conditions nor the firm's own performance (Mellahi & Wilkinson, 2004). This perspective rests on the premise that firms cannot influence their own destiny. It argues that firms in an industry are affected by a range of industry-specific and environmental factors which lead to the process of “natural selection”, whereby firms that do not fit their environment are “selected out” and “die” (Tirole, 1988). Therefore, organisational failure is seen as an inevitable consequence of the process of “natural selection” and “survival of the fittest”. The following section outlines the variety of explanations for the causes.

6. Environmental jolt explanations

One of the main streams of research on the external factors is anchored in the Schumpeterian thesis of “creative destruction” (Schumpeter, 1942). According to Schumpeter (1942), jolts in the external environment can generate waves of organisational failure. Environmental jolts are “transient perturbations whose occurrences are difficult to foresee and whose impacts on organisations are disruptive and potentially inimical” (Meyer, 1982, p. 515). Past studies have identified two kinds of environmental jolts—beneficial and hostile (Meyer, 1982). On one hand, beneficial jolts can provide a safe setting and conditions for firms to thrive (Covin & Slevin, 1989). Beneficial jolts include a host of factors such as an increase in the customer population because of demographic changes, reduction in taxes, technological advancements and upswings in the business cycle, which may expand the economic opportunities for the population of firms within an economic niche (Venkataraman & Van de Ven, 1998). Consequently, such beneficial jolts can slow down or even avert the demise of firms (Carter & Van Auken, 2006).

On the other hand, hostile jolts such as a sudden increase in natural disasters, unexpected tax hikes, a drastic shrinkage in the customer population and downswings in the business cycle, may shrink the economic opportunities for the population of firms within an economic niche (Bradley, Aldrich, Shepherd, & Wiklund, 2011; Covin & Slevin, 1989). Scholars in this area have uncovered that such adverse business conditions are more likely to lead to business failure (El Hennawy & Morris, 1983; Platt, 1989). It has been suggested that market forces through measures such as technological change, deregulation and

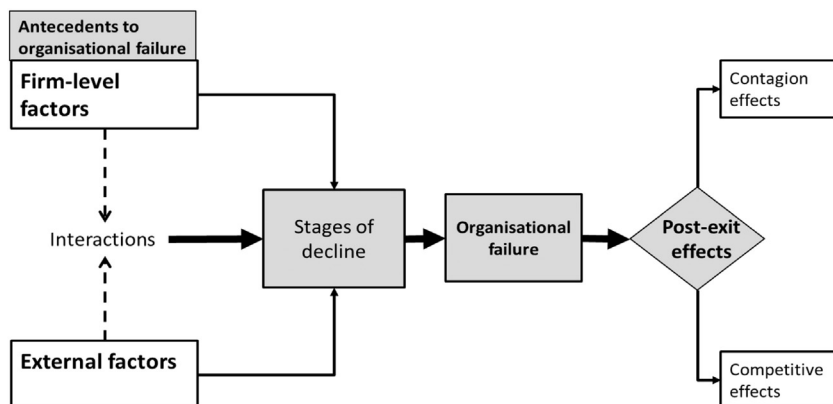


Fig. 1. An integrative process framework of organisational failure research.

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