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Institutional logics, family firm governance and performance

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A B S T R A C T

Positive and negative views of family firms and their performance abound. Although there have been explanations for this divergence based on conditions of governance and context, the institutional environment has been less thoroughly explored as a source of these differences. We argue that the blend of family and market institutional logics in the regional communities where firms operate can have an important impact on the governance arrangements and financial performance of family firms. Specifically, we find that family-intensive governance is more common where family logic predominates in a region, and does best when this logic remains at modest levels or is countered by market logic. We test and support these notions in a comprehensive sample of private family firms in Italy, an ideal context in which distinct historically-determined logics exists among its 20 regions.

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Executive summary

An important question among practitioners and academics is whether the involvement of family members in top corporate positions is beneficial or harmful for firm performance. On the one hand, appointing family members to run a family firm may be suboptimal due to nepotism (Schulze et al., 2001) and human capital inadequacies (Mehrotra et al., 2013). On the other hand, companies led by family members may enjoy the benefits of devoted stewardship and personal commitment (Arrègle et al., 2008; James, 1999, 2006; Miller and Le Breton-Miller, 2005; Ward, 2006).

We reconcile these perspectives by investigating how institutional logics in the region of a firm's headquarters affect both the selection of governance arrangements and the performance of the family firm. We focus on the role of two different logics: the logic of the family and that of the market. We argue that a combination of these logics may benefit family firm performance. Specifically, in regions where a family logic is juxtaposed with a market logic, a balanced, multifaceted identity and set of norms by firm principals becomes more likely, and that in turn can have a positive effect on family firm performance.

We conducted our study in Italy, which is characterized by profound cultural and institutional differences across geographic regions, often dating back in origin to the medieval states (Colli et al., 2003; Helliwell and Putnam, 1995; Terrasi, 1999). Italy also is appropriate for our study as family firms represent a major part of its economy and are a fount of entrepreneurship there (Cucculelli and Micucci, 2008). Our empirical analysis indicates that when family and market logics are *both* strong, their potentially negative impacts on performance are less likely to surface: specifically, a meritocratic market logic may counter the nepotism common within the

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family logic, while devoted family stewardship may combat the possible opportunism of a purely market logic. In short, firms with family-intensive governance exhibit superior operating performance when powerful family logics are counterbalanced by strong market logics, and also when regional family logics are less dominant.

Our study demonstrates that the blending of institutional logics has significant implications for family firm performance. These findings indicate that family firm principals and leaders should pay heed to their institutional environment. They must inform themselves of the richness of institutional influences, which provide opportunities to embrace the best of both logics - family motivation, dedication and cohesion where the family logic is prevalent within a region, and market-based meritocracy that avoids short-termism and opportunism. In so doing it will be essential for these parties to avoid over-reliance on weak family talent, while also not relying too much on outsiders with too narrow and short-term a perspective. To serve as guidelines, family business owners would be wise to become aware of exemplary national and international governance practices, instead of relying too much on local models and traditions.

1. Introduction

Opposing positive and negative perspectives of family firms continue to prevail. Some argue that family firm performance is compromised by altruistic tendencies such as dysfunctional nepotism in selecting firm leaders (Schulze et al., 2001), with ultimate harm to business performance from entrenchment and conservatism (Bertrand and Schoar, 2006; Bloom and Van Reenen, 2007). By contrast, other scholars claim that families are excellent stewards of their firms whose investments in the robustness of the business and its stakeholders as well as their entrepreneurial resilience drive superior performance (Arrègle et al., 2008; James, 1999, 2006; Miller and Le Breton-Miller, 2005; Ward, 2006).

To reconcile these perspectives, the literature has examined alternative modes of governance (Miller et al., 2007), levels of family involvement (Gedajlovic et al., 2012), and family dynamics (Gersick et al., 1997; Kets de Vries, 1996). Other studies have begun to explore the impact of the environment as reflected by the development in the legal system (Liu et al., 2012), labor institutions (Van Essen et al., 2013), markets (Aguilera et al., 2008; Carney, 2007), and national culture (Allouche et al., 2008). However, most of the family firm literature thus far has failed to examine the critical fine-grained institutional variations that may exist at the community level. In an early demonstration of the potential value of this approach, Banalieva et al. (2015) have revealed the vital impact of Chinese regional economic reforms on family firm outcomes. We build on this promising new area by examining and showing how the institutional context at the community level can affect the nature of family firm governance structures, and in turn firm performance, and in so doing further reconcile positive and negative views of family firms.

The community context can be characterized richly by a blend of logics that may bear profoundly upon a family firm - specifically, logics of the market and the family (Friedland and Alford, 1991; Marquis and Lounsbury, 2007). A logic is the socially constructed set of cultural symbols and practices - assumptions, values and beliefs - by which parties “provide meaning to their daily activity, organize time and space, and reproduce their lives and experiences” (Thornton et al., 2012: 2). The nature and blend of logics vary considerably across communities with disparate social histories and migratory patterns (Greenwood et al., 2010, 2011).

We shall argue that the strength and predominance of a *family* logic within a community - its embrace of family-related identities and values - will determine whether family-intensive firm governance arrangements will reflect positive family priorities of stewardship, that is devoted and sustained care for an organization and the long-term well-being of its stakeholders (Arrègle et al., 2008; Eddleston et al., 2012; Miller and Le Breton-Miller, 2005; Welsh et al. 2013), versus more negative priorities such as nepotism, family conflict and entrenchment that erode firm performance (Bertrand and Schoar, 2006; Bloom and Van Reenen, 2007; Eddleston and Kellermanns, 2007; Gómez-Mejía et al., 2007). We also examine the market logic of meritocracy, the strength of which within a community also can play a role, for instance by instilling business discipline in a way that counters the potentially negative aspects of family-intensive governance and nepotism.

Our insights contribute to the family business literature by reconciling the stewardship and behavioral agency perspectives on these firms, showing how the institutional logics in a region can have a profound impact on the nature and effectiveness of family governance. They also augment the work on institutional logics where stable blends and varying strengths of multiple logics are less prominent, or where conflicts among logics are emphasized (Pache and Santos, 2013; Pratt and Corley, 2007; Pratt and Kraatz, 2009). We maintain that the embrace of multiple logics may be both likely and desirable (Pache and Santos, 2013). For example, where the family logic is juxtaposed with market logic in a community, a multifaceted identity and set of norms becomes more probable by business principals, and that, as we shall see, can have important normative consequences for family firm performance. In short, the focus on local communities allows us to capture how the mixture of broadly held logics constitute a field that in its nuances can facilitate or restrict effective human agency in organizations.

We chose Italy as the setting for our study as the geographical and administrative definition of its 20 regions reflect profound cultural and institutional differences going back in origin to the medieval states (Colli et al., 2003; Helliwell and Putnam, 1995; Terrasi, 1999), revealing very different communities with stable and homogeneous levels and blends of family and market logics. Italy also is especially appropriate for our study as it is a country with relatively little geographic mobility (Bonin, 2008), so that the principals of family firms tend to remain in the communities in which they were raised, which also are the communities in which their businesses reside, and thus reflect local values in their decision-making. Moreover, family firms represent a large fraction of the Italian economy and are a fount of entrepreneurship there (Cucculelli and Micucci, 2008).

Our paper is structured as follows. We first present some conceptual background on institutional family and market logics and their connections to the conduct and performance of family firms; we then present our hypotheses before describing our methods, findings, and discussion.

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