International Business Review xxx (xxxx) xxx–xxx

Contents lists available at ScienceDirect

International Business Review

journal homepage: www.elsevier.com/locate/ibusrev

CEO succession and firms' internationalization processes: Insights from German companies

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A R T I C L E I N F O

Keywords:
CEO succession
Internationalization processes
Internationalization rhythm
Number of CEO changes
Succession type
Longitudinal research design
Germany

A B S T R A C T

This article analyses the relationship between CEO succession events and German firms' internationalization processes, which is represented by the degree of internationalization (DOI) growth and internationalization rhythm. Based on a theoretical framework combining elements of agency theory, institutionalism and upper echelons approach, we propose a longitudinal model to examine the relationships of both process variables with the number of CEO changes and succession type (internal vs. external succession), respectively. The results of our study of 102 German firms over 23 years (1990–2012) show an inverted U-shaped impact (no impact) of the number of CEO changes (succession type) on the DOI growth and a positive (negative) monotonic effect on the rhythm of internationalization.

1. Introduction

Scholars in international business have recently emphasized the role of individual decision-makers and particularly CEOs in the internationalization of firms (e.g., Herrmann & Datta, 2006; Laufs, Bembom, & Schwens, 2016). In this vein, mostly the relationships between the characteristics of a top management team or the CEO (e.g., education (Deeks, 1972), experience (Bigley & Wiersema, 2002; Herrmann & Datta, 2006; Laufs, Bembom, & Schwens, 2016)) and *single* internationalization aspects such as market entry modes (Herrmann & Datta, 2002; Nielsen & Nielsen, 2011) or export success (Dichtl, Koeglmayer, & Mueller, 1990) have been investigated, suggesting a static and one-dimensional perspective. A more dynamic view which applies knowledge about the influence of the CEO to internationalization processes is still underdeveloped. Both dimensions have – with few exceptions (e.g., Lin & Liu, 2011, whose study only deals with Taiwanese firms and uses post-succession TMT changes as intermediary between CEO succession and DOI change or Oesterle, Elosge, & Elosge (2016) whose study focuses on CEO narcissism but neglects CEO succession) – hardly been merged yet.

As empirical analyses in the field of general and strategic management impressively show, the influence of the human factor, i.e., the CEO, on a firm's actions and course can be identified by studying CEO succession effects (Virany, Tushman, & Romanelli, 1992). In this context, the upper echelons approach plays a prominent role in explaining the effects of CEO succession: Respective studies are based on the assumption that individuals and, therefore, also CEOs, differ, especially in terms of their cognitive map; accordingly, those differences should affect their decision-making. A CEO change therefore could mean that the new top manager will do things differently than his/her predecessor, leading to changes in the firm's internationalization actions. Moreover, the assumptions of agency theory and institutionalism apply to the dynamic view on how CEO successions impact the internationalization process of firms.

In this research, we therefore run an eclectic approach by combining the different theoretical elements in order to develop hypotheses dealing with succession effects on the internationalization process of a firm. Regarding the internationalization process, we are especially interested in the following two formal dimensions: 1) the degree of internationalization (DOI) growth over time, and 2) the rhythm of internationalization over time. The DOI growth is important to consider in order to gain a general understanding of a firm's internationalization process. Moreover, the concept of rhythm has been shown to facilitate a deeper understanding of the nature of the internationalization process and researchers assume that the rhythm of internationalization directly influences a firm's performance (Vermeulen & Barkema, 2002).

Focusing on CEO succession effects holds several key contributions towards a better understanding of internationalization processes with respect to the influence of strategic decision-makers. First, this research reveals an interplay of the assumptions of upper echelon approach, agency theory, and institutionalism in the international business context. Therefore, the knowledge on the individual decision-maker and

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http://dx.doi.org/10.1016/j.ibusrev.2017.09.004
Received 7 December 2016; Received in revised form 31 July 2017; Accepted 5 September 2017
0969-5931/

his/her influence on the internationalization process is theoretically consolidated and extended, since we believe that taking an eclectic approach with regard to the influence of an individual decision-maker's influence on internationalization processes will be necessary to further elaborate and analyze the mechanisms of this relationship. Second, this research takes a deeper look into the formal elements and modes of internationalization processes which is a prerequisite to understanding the nature and phenomenon of the process itself. Finally, researchers and practitioners alike can gain further insights into the causes of internationalization decisions. This seems important given that internationalization processes affect almost all firms and, due to their link to a company's profit, should be elaborated in further detail. Our contributions can be summed up as follows: Existing theories which deal with strategic decision-makers (agency theory, institutionalism and upper echelons theory) are extended to an international context and functional relationships in internationalization process research which have remained unexplored, i.e., the impact of individual decision-makers, are studied.

2. Theory and hypotheses

2.1. Individual decision-makers in internationalization process theory

Internationalization processes are a classical field of international business research. However, despite of being one of the most important factors influencing the firm's strategy, the individual decision-maker has been relatively unexplored in internationalization process theory so far. Especially the traditional models of the Nordic School (Johanson & Vahlne, 1977, 1990; Johanson & Wiedersheim-Paul, 1975; Luostarinen, 1979) do not explicitly deal with the individual decision-maker as a key player in the internationalization process (Aharoni, Tihanyi, & Connelly, 2011). More recent approaches, such as the GAINS paradigm (Gestalt-oriented Approach of International Business Strategies) (Macharzina & Engelhard, 1991), which is based on the gestalt approach (Miller & Friesen, 1978, 1984), or the three-E-concept (Kutschker, Bäurle, & Schmid, 1997), acknowledge the driving role of CEOs for internationalization. However, they do not make it possible to gain information on the CEO-related mechanisms that shape internationalization processes.

It is therefore not surprising that there are almost no *empirical* studies analyzing the influence of CEOs and CEO succession events specifically on a firm's international development. The resulting lack of knowledge is somewhat surprising as within management and strategy research the influence of CEOs on organizational change is an integral part of to the traditional research objectives. Especially CEO successions are viewed as "critical decision or event" (Miller & Friesen, 1980: 596). Consequently, such CEO changes and respective studies might allow further insights into the functional mechanisms of the relationship between individual decision-makers and internationalization processes in the field of international business. But, most of the studies (in general management) only take single CEO changes into account and neglect a long-term perspective which would be especially important for understanding the development of the firm.

To address our research question – i.e., what is the influence of CEO succession and succession type on a firm's internationalization process – we need to take an eclectic approach and rely on elements provided by agency theory and new institutionalism to explain the general effect of CEO succession on the DOI growth and an upper echelons perspective (Hambrick & Mason, 1984) – in addition to its already demonstrated function as a general argument towards the relevance of CEO succession events for the further development of the firm – to explain individual effects of CEO succession on the rhythm of the internationalization. The general framework of our paper is shown in Fig. 1.

2.2. Agency theory as reference point

The strategic relevance of individual decision-makers has been widely discussed in agency theory (Jensen & Meckling, 1976). The theory is based on the assumption of the separation of ownership and control in organizations (Berle & Means, 1932) and addresses the role of risk in a prominent fashion (Barney & Hesterly, 1996; Beatty & Zajac, 1994). Agents (managers/CEOs) are assumed to be risk averse, while principals (owners) appear to have a neutral attitude towards risk (Eisenhardt, 1989). This is due to the owners' opportunity to diversify a large part of their risk over the capital market by investing in various companies. Furthermore, the self-interest assumption (Fama, 1980) is regularly brought up to explain why companies pursue strategies which do not necessarily match owners' preferences (Amihud & Lev, 1981; Trautwein, 1990).

Especially in the case of high managerial discretion due to dispersed ownership structures (Amihud & Lev, 1999; Crossan, 2011; Crossland & Hambrick, 2011; Salancik & Pfeffer, 1980; Tuschke & Sanders, 2003), managers possess the power to trace personal goals during their employment. Empire-building theory deals with a certain aspect in this context: managers tend to favor diversifying strategies to capture private benefits (Aggarwal & Samwick, 2003; Jensen, 1986) by transferring firm resources to their personal gain (Harris & Raviv, 1991). The resulting opportunities to consume specific perquisites as well as a high degree of power and prestige by controlling a large company represent desirable goals for managers. As a consequence, it might be conceivable that managers – and in this context especially CEOs as the most powerful decision-makers of a firm – pursue strategic decisions that enlarge their personal benefits. These, however, do not necessarily need to be in conflict with the shareholders' interests.

Two important reasons lead us to rely on agency theory as a theoretical basis from which to derive our research question: (1) the theory represents a very prominent, often employed and well-evidenced approach to model the behavior and actions of managers and therefore CEOs; (2) there are a lot of opportunities for managers, e.g. CEOs, to pursue strategic decisions and to maximize personal goals due to the separation of ownership and control.

2.3. Institutionalism as reference point

Within the approach of institutionalism, a major driver for firms' development and success is legitimacy (which can be defined as 'organizations embrac[ing] specific institutional forms or practices because the latter are widely valued within a broader cultural environment.' (Hall & Tayler, 1996, p. 949). We take this basic assumption and transfer it to the individual level: new CEOs strive for the legitimacy of their activities. In doing so, they will be motivated and devote a significant amount of attention and energy to respond to their (new) mandate (Hambrick & Fukutomi, 1991). As one way of doing so might be the enlargement of international activities we believe that the perspective taken by institutionalism will help us to understand how CEOs and respective succession events may influence the internationalization process of firms.

2.4. Upper echelons theory as reference point

Hambrick and Mason's upper echelons theory (1984) tries to clarify the role of decision-makers as drivers of a company's strategy. Following this approach, organizational outcomes are a reflection of the strategic choices of managers. Because of the complexity of situations and the individual cognitive base and values managers have, their perception is limited to selective environmental and organizational stimuli. This results in an individual interpretation of situations and provides the basis for a specific strategic choice (Cyert & March, 1963). In order to predict and measure the managers' cognitive map, background characteristics are used. Hambrick and Mason (1984) argue that