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# The role of internal social capital in organisational innovation. An empirical study of family firms

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ABSTRACT

Using a sample of 172 Spanish family firms and two responders per firm, consisting of a family member and a non-family member (344 returned questionnaires), we examine the effects of internal social capital on organisational innovation. Building on the relational, cognitive, and structural view, and on social capital theory, we propose that internal networking relationships between family members (family social capital) and between non-family members (non-family social capital) in family firms facilitates innovation. Moreover, its benefits flow from the relationships among the firm's internal groups. The results of structural equation models indicate that the social capital of both family members and non-family members has a direct and positive effect on innovation. Further, our findings provide evidence that non-family social capital is just as effective as family social capital for family firm innovation, establishing a new line of research from an empirical perspective. The findings also test whether social factors are key assets of family firm innovation.



## Introduction

The current economic crisis has accentuated the need for innovative business practices. The interest in innovation stems from an increasingly turbulent environment, in which firms must seek and execute innovation to overcome inertial forces and remain competitive (e.g., Floyd & Lane, 2000). Organisations must adapt more quickly to more changes in more complex environments than ever before, and in this context, organisational innovation is critical for survival, a sustainable competitive advantage, and performance (e.g., Damanpour, 1991). This situation applies to family firms as well (e.g., Craig & Moores, 2006; De Massis, Frattini, & Lichtenthaler, 2013a; De Massis, Frattini, Pizzurno, & Cassia, 2013b). An organisation's capability to innovate is closely tied to its internal resources and its ability to utilise these internal resources. In this respect, there is a need for a better understanding of how internal resources (i.e., internal social capital (SC)) create a competitive advantage (Barney & Arikan, 2001), and how these internal resources are utilised to achieve that advantage (Sirmon & Hitt, 2003).

The literature recognises the importance of internal SC as a key asset in developing innovation capabilities, defining it as an organisational value, which is formed based on the relationships between its members in order to cooperate, share information, and coordinate collective activities (Adler & Kwon, 2002; Freel, 2000; Nahapiet & Ghoshal, 1998). Several studies have analysed the effect of internal SC on innovation (e.g., Hult, Hurley, & Knight, 2004; Moran, 2005; Nahapiet & Ghoshal, 1998; Tsai & Ghoshal, 1998) and have shown that internal SC is critical to the development of innovation (Subramaniam & Youndt, 2005).

Since SC encompasses norms and trust, but also includes social networks, both formal and informal (Nahapiet & Ghoshal, 1998), social relationships facilitate knowledge exchange by reducing uncertainty about organisational functions and enabling knowledge sharing (Leana & Van Buren, 1999; Subramaniam & Youndt, 2005; Tsai & Ghoshal, 1998). Intra-organisational knowledge sharing can influence a firm's capacity to innovate as it supports creativity and inspires new ideas that enhance organisational competitiveness (Aragon-Correa, García-Morales, & Crodon-Pozo, 2007; Perry-Smith & Shalley, 2003). Moreover, SC facilitates innovation by motivating the cooperation, communication, and coordination among different members in a firm (Adler & Kwon, 2002; Nahapiet & Ghoshal, 1998).

However, most research treats internal SC as homogenous, irrespective of what groups or collectives coexist within the organisation. This may not be an appropriate representation of the situation, since more than one social group coexist in most organisations, including formal groups such as departments or divisions, and informal groups such as founders or family firm

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members (Arregle, Hitt, Sirmon, & Very, 2007). These groups do not necessarily have similar dynamics, relationships, and social interactions, and in turn, this could affect the different forms of internal SC that develops.

Our study is an attempt to address this issue, and refine and extend the understanding of the relationship between internal SC and innovation, since there is little research on the differences in SC among groups within the same organisation. Further, to the best of the authors' knowledge, few of these studies have analysed the relationship between internal SC and innovation in the context of family firms, and still fewer have considered the two social groups that most family firms include (Arregle et al., 2007): the family members' group and the non-family members' group. As discussed, family firms are characterized by the presence of at least two groups, family and non-family members, who form two distinct but complementary groups that may strongly influence the creation of internal SC in family firms (Arregle et al., 2007; Nahapiet & Ghoshal, 1998; Tsai & Ghoshal, 1998). Therefore, our study is an attempt to extend understanding of the relationship between the SC of these two groups and innovation in family firms. Scholars assert that advanced, long-term orientation of family firms and other useful resources and capabilities, or distinctive 'familiness' (Habbershon & Williams, 1999), may influence innovation. Family influence and employee relationships (family members and non-family members) may contribute to enhance the firm's ability to identify and develop innovative opportunities that could not be identified and developed otherwise (Carrasco-Hernandez & Jimenez-Jimenez, 2013; De Massis et al., 2013a; Zellweger, Nason, & Nordqvist, 2012). Effectiveness at the family group level and non-family group level is measured by such standards as, for example, reaching agreed-upon goals, and being able to come together in the future to do more work if needed (Wise, 2014).

To address this gap in the literature, the purpose of this study is threefold. First, we seek to contribute to the literature by linking family firms and internal SC in a way that is consistent with Arregle et al. (2007) who suggest that intra-group characteristics have a high potential to affect SC in different forms; we study whether there are differences in the process of internal SC generation between the family members' group and non-family members' group, and how these differences affect innovation. From an internal SC perspective, the innovation process requires the participation of not only family members but also of non-family members due to the coexistence of the different roles of each group at family firms. Second, we intend to develop a new model to assess the internal SC-innovation link in family firms. For this purpose, we distinguish between family SC, which arises from the family group, and non-family SC, which arises from the non-family group. Thus, we explore family firm heterogeneity by focusing on these two groups; we explore how both family and non-family SC impact innovation. Finally, we seek to contribute to future research supporting arguments that indicate that internal SC facilitates innovation by developing an empirically grounded theoretical framework. Arregle et al. (2007) and Pearson, Carr, and Shaw (2008) approached internal SC in family firms from a conceptual perspective. Salvato and Melin's (2008) work performed within-case analysis aimed at reaching a deeper understanding of the relationship between internal SC and value creation at each individual family firm, taking into account only family SC.

This study, to best of our knowledge, is the first empirical study that focuses not only on family SC, but also on non-family SC in family firms, exploring new lines of research. Using a sample of 172 Spanish family firms, our findings provide strong evidence that illustrates the essential role that these two distinctive groups play in this process in family firms. Spain provides an interesting laboratory to examine such firms since this country features a high ownership concentration and a predominance of family-controlled firms (La Porta, Lopez de Silanes, & Shleifer, 1999).

The rest of this paper is organised as follows. After the introduction, we provide the theoretical background of the SC concept and its dimensions in the context of family firms. The third section provides a framework for the empirical analysis and explains the influence of family SC and non-family SC on innovation. The fourth section discusses the data selection procedures, research methods, and presents our findings. Finally, the fifth section offers some conclusions and discusses the implications for management theory and practice, and identifies aspects that merit further investigation.

## Theoretical background

The importance of SC as a determinant of organisational innovation has received important attention over the last few years (e.g., Arregle et al., 2007; Pearson et al., 2008; Salvato & Melin, 2008). In the organisational literature, SC has been generally perceived as the resources that can be derived from a personal network or a set of ties to achieve specific goals (Alguezaui & Filieri, 2010). Several scholars propose that SC involves the relationships between individuals or groups working in the organisation (internal SC) and between the organisation and external parties (external SC); and it provides valuable learning resources and facilitates the development of a distinctive knowledge base which may be essential to generating innovations and creating value (Adler & Kwon, 2002; Nahapiet & Ghoshal, 1998; Yli-Renko, Autio, & Tontti, 2002).

Innovation is an expensive, uncertain, and risky business process that depends on productive knowledge exchange between people with different critical points of view and a variety of professional backgrounds (Griffin & Hauser, 1996). Moreover, to be successful it requires a collection of advanced capabilities and competences (Cassia, De Massis, & Pizzurno, 2012). From an internal perspective, the interchange of ideas and knowledge, and certain relationships between group members contribute to the firm's ability to identify and develop innovative opportunities that could not be identified and developed otherwise. Thus, greater internal communication, coordination, and cooperation contribute to enable people to act collectively and to promote learning, knowledge, and innovation (Subramaniam & Youndt, 2005; Tsai & Huang, 2008; Tsai & Ghoshal, 1998).

As referenced by Coleman (1990), Nahapiet and Ghoshal (1998), and Tsai and Ghoshal (1998), the concept of SC encompasses social interaction, network ties, trusted relationships, and value systems that facilitate creativity within the group context. Nahapiet and Ghoshal (1998) assert that network ties provide access to resources, constitute a valuable source of information, and reduce the amount of time required to gather such information. SC enables organisations to either reinforce or transform their prevailing knowledge (Subramaniam & Youndt, 2005) and reflects the value of relationships (Nahapiet & Ghoshal, 1998). According to Nahapiet (2008), SC is a factor that provides access to other resources. In this way, SC is increasingly being considered a valuable intangible asset for firms since it provides an idiosyncratic and unique network of relationships (Alguezaui & Filieri, 2010).

The internal SC view focuses on internal linkages among individuals and groups within a collective, including those that contribute to cohesiveness and foster collective action (Acquaah, 2011; Adler & Kwon, 2002). From an internal firm perspective, SC is concerned with the relationships across all organisational levels (Leana & Van Buren, 1999). Nahapiet and Ghoshal (1998) propose a conceptual framework for analysing SC dimensions at the firm level, in which they define SC as 'the sum of the actual and potential resources embedded with, available through and derived from the network of relationships possessed by an individual or social unit' (p. 243). They identify three interrelated internal SC dimensions: structural, relational, and cognitive.