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The relationship between entrepreneurial orientation and firm performance: Influence of family governance

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A B S T R A C T

A growing number of recent studies highlight an avenue of entrepreneurship in family business. Previous studies have examined the relationship between entrepreneurial orientation (EO) and firm performance, and generate inconsistent results probably due to the omission of the moderating role of family governance. To explicitly address this gap, this study investigates how entrepreneurial orientation (EO) influences firm performance in the contingencies of family and nonfamily firms by considering the influence of family governance. Built on agency theory and stewardship theory, the empirical findings of this study show that EO is positively associated with the concurrent and sustaining performance of firms, and such positive relationships are particularly strong when family ownership is combined with active family management and control; while in passive family governance, the EO-performance relationship becomes insignificant. These findings suggest that the potential advantages of EO can be better realized in family firms because active family governance alleviates agency problems and facilitates stewardship within firms when family CEOs, family top management, family chairpersons, and family directors are in presence.

1. Introduction

Entrepreneurial orientation (EO) is a dimension of strategy-making process related to superior performance of firms (Wiklund & Shepherd, 2005; Wiklund, 1999). In the academic literature, the studies of entrepreneurship are often aggregated with the general research area of family firms (Zahra, Hayton, & Salvato, 2004). Scholars usually view family firms as an important organizational type and a unique context that enhances the performance of entrepreneurially oriented firms (Casillas & Moreno, 2010; Nordqvist & Melin, 2010).

Prior empirical studies have reported different research findings on the association between EO and firm performance (Covin & Slevin, 1989; Tang, 2008; Wiklund, 1999; Zahra, 1991). Most studies find a positive association between EO and performance (Engelen, Gupta, Strenge, & Brettel, 2015; Tang, 2008; Wales , Patel, & Lumpkin, 2013; Wiklund, 1999; Zahra, 1991), while insignificant results are also reported (Covin & Slevin, 1989; Madison , Runyan, & Swinney, 2014; Stam & Elfring, 2008). Such inconsistency might result from the omission of important contingency variables. Scholars argue that some moderating variables should be considered in the EO-firm performance link, such as the internal organization and external environment of firms (Covin & Slevin, 1991; Engelen et al., 2015; Lumpkin & Dess, 1996).

Recently, an emerging line of studies proposes that the EO-performance relationship is contingent on the degree of family governance,[1] specifically, family involvement in ownership, management and control (Casillas & Moreno, 2010; Madison et al., 2014; Sirmon & Hitt, 2003). Given the close relationship between EO and family firms (Cruz & Nordqvist, 2012; Lumpkin, Brigham, & Moss, 2010; Miller & Le Breton-Miller, 2005), whether family governance facilitates or attenuates the EO-performance relationship is a research question that deserves close examination.

Existing studies on family governance are mainly based on agency theory and stewardship theory (Miller & Le Breton-Miller, 2006).

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[1] In the literature, different definitions of family governance exist. Family governance mechanisms range from rather informal family meeting to heavily structured professional bodies such as family offices, family foundations, and family committees (Suess, 2014). Past literatures have identified three types of family governance, including family meeting, family council, and family constitution (Suess, 2014); while other related topics are also widely discussed, such as family involvement in ownership (e.g., Anderson & Reeb, 2003), boards of directors (e.g., Pieper et al., 2008), CEOs, and top management positions (e.g., Villalonga & Amit, 2006). Our study does not aim to cover all aspects of family governance mechanisms, but focus only on family ownership, family management, and family control.

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Although some studies raise concerns on the negative effect of family governance (Naldi, Nordqvist , Sjöberg, & Wiklund, 2007; Schulze, Lubatkin, Dino, & Buchholtz, 2001), most agency theory research suggests a positive influence because agency costs between owners and managerial agents become low when a close alignment exists between the interests of family owners and family managers (Fama & Jensen, 1983; Pieper, Klein, & Jaskiewicz, 2008). Family owners, managers and directors also have better knowledge and information on the company so that the potential free-rider problems and monitoring costs can be reduced (Anderson & Reeb, 2003; Carney, 2005; Miller & Le Breton-Miller, 2006; Villalonga & Amit, 2006). Similar arguments are addressed in the stewardship theory of family firms. Family members tend to have stronger stewardship perceptions than nonfamily members (Davis, Allen, & Hayes, 2010), so they are likely to be intrinsically motivated by high-level needs and act with altruism for the benefit of the firms, especially when the corporate governance structure gives them high authority and discretion (Davis, Schoorman, & Donaldson, 1997; Davis et al., 2010; Pieper et al., 2008). Family top managers and directors also tend to have longer business horizon in decision making, and this may influence their pursuit of first-mover advantages through innovation, proactiveness and risk-taking (Casillas & Moreno, 2010; Zahra et al., 2004; Zellweger & Sieger, 2012).

This study therefore aims to go beyond existing literature by examining the EO-performance relationship when family ownership is combined with active family management and control, specifically when family members serving as CEOs, top management, chairpersons and directors. Moreover, although existing studies have suggested that entrepreneurial actions can help first-movers to acquire both temporary and sustained high performance (Zahra & Covin, 1995) so its effect should be both short-term and long-term in nature (Wiklund, 1999; Zahra & Covin, 1995; Zahra, 1991), empirical evidence so far is still limited. Therefore, this study differs from previous studies by considering both the concurrent and sustaining effects of family governance on the EO-performance link.

Based on data collected from a secondary database and a questionnaire survey from 223 public firms in Taiwan, this study finds that EO indeed is positively associated with the concurrent and sustaining performance of firms, and the positive relationship is more significant when family ownership is combined with family management or control. Specifically, the presence of family top managers, family CEOs, family chairpersons and family directors magnifies the positive association between EO and performance; while in nonfamily firms the influence is insignificant. Similar results are found in both the concurrent and sustaining performance of firms, largely supporting the agency theory and stewardship perspective of family firms.

2. Theoretical background and hypotheses

Over the past two decades, a growing amount of research has integrated the areas of EO and family firms (Casillas & Moreno, 2010; Lumpkin et al., 2010; Nordqvist & Melin, 2010; Zahra, 1991). However, earlier studies seldom examine how the association between EO and firm performance is influenced by family governance. This section reviews literature on the relationship between EO and firm performance. Possible influence of family governance on the EO-performance relationship is then discussed, with hypotheses developed accordingly.

2.1. EO and firm performance

EO has been described as reflecting a firm's inclination toward entrepreneurial activities (Lumpkin & Dess, 1996; Wiklund & Shepherd, 2005; Zahra, 1991). EO refers to a posture or disposition toward the processes, practices and decision-making activities that lead to new entry, involving the intentions of a firm to grasp new market opportunities in a dynamic process (Lumpkin & Dess, 1996). Miller (1983) argues that an entrepreneurial firm is willing to engage in the innovation of products and technological processes, to provide proactive innovations to pursue first-mover advantages, and to undertake risky ventures. EO is thus a combination of at least three dimensions: innovation, proactiveness, and risk-taking (Lumpkin & Dess, 1996; Wiklund & Shepherd, 2005).

Researchers often view EO as an independent variable that creates or sustains firm performance. The positive influence of EO on performance is related to the first-mover advantages and the tendency to take advantages of emerging opportunities implied by EO (Wiklund, 1999). Specifically, innovation keeps firms ahead of their competitors and gains competitive advantages; proactiveness gives firms the ability to present new products/services to the market ahead of competitors (Wiklund, 1999); while risky strategies lead to high mean performance in the long term even though some projects fail while others succeed in the short term (Wiklund & Shephard, 2005). All these lead to improved financial results for firms.

The positive influences of EO on firm performance have been found in different country and industry settings. For example, based on the data of *Fortune* 500 manufacturing firms, Zahra (1991) finds that EO is positively associated with financial performance of firms. Wiklund (1999) study on small Swedish companies and Tang (2008) study on Chinese firms also report the same results. Engelen et al. (2015) use data from 790 small- and medium-sized firms in six countries and find a positive relationship between EO and firm performance. Wales et al. (2013) use a sample of high technology manufacturing firms in the U.S. and find EO as a source of variability in firm performance. All these studies confirm the traditional view of EO.

However, different findings are also reported. Covin and Slevin (1989) find insignificant relationship between EO and performance in U.S. firms. Similar results are reported in Netherlands firms (Stam & Elfring, 2008), and small U. S. firms (Madison et al., 2014). Such inconsistent results imply that the realization of EO's potential benefit might be influenced by certain contextual settings, such as external environment (Wiklund & Shepherd, 2005) and internal organization (Casillas & Moreno, 2010; Naldi et al., 2007; Wiklund & Shepherd, 2005). Some interaction effects might exist in the EO-performance relationship but are seldom examined in existing literature (Wiklund, 1999).

In line with most prior studies, this study predicts a positive EO-performance relationship, and moves further by examining how the EO-performance link is influenced by family governance, specifically, family ownership, management, and control.

Regarding the time periods, some research suggests that actions of innovation, proactiveness, and risk-taking should help first-movers to acquire both temporary and sustained high performance (Wiklund, 1999; Zahra & Covin, 1995; Zahra, 1991). Such arguments are supported by empirical studies. For instance, Wiklund (1999) uses data from small Swedish firms and finds that EO affects performance during an extended period of time, rather than just a "quick fix" where performance is only temporarily affected. Zahra (1991) finds that the positive correlation between EO and performance sustains during three consecutive years. The longitudinal study of Zahra and Covin (1995) also confirms that EO influences performance during each of the five years studied. Therefore, it is hypothesized that,

H1. EO is positively associated with firm performance.

H2. EO is positively associated with sustaining firm performance.

2.2. Moderating role of family ownership and management

In traditional family business literature, the concept of family firms includes family ownership, management, and control (Villalonga & Amit, 2006). Prior studies have found that the advantages of family firms in mitigating agency problems are more likely to be realized when family ownership is combined with active family