The Relationship Between Socioemotional and Financial Wealth: Re-visiting Family Firm Decision Making

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The relationship between socioemotional and financial wealth

Re-visiting family firm decision making

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Abstract

Purpose – A growing volume of family firm literature has argued that the preservation of family socioemotional wealth takes precedence over the pursuit of financial goals. The purpose of this paper is to develop a conceptual framework that builds knowledge regarding the two-way relationship between socioemotional and financial forms of wealth, to develop a more complete theory of wealth concerns that may inform family firm decision-making.

Design/methodology/approach – The authors conceptually examine contingencies affecting the relationship between financial and socioemotional wealth (in both causal directions).

Findings – The authors predict when one form of wealth (socioemotional/financial) is likely to dominate the other (financial/socioemotional) in the family firm’s strategic decisions.

Originality/value – The paper advances knowledge on the two-way relationship between socioemotional and financial forms of wealth providing a platform for further development in the nascent field of family business research, including our understanding of family firm decisions regarding control and influence over the family business, environmental policy, altruism toward family members, R&D, accounting choices and corporate diversification.

Keywords Family firm, Socioemotional wealth, Financial wealth

Paper type Research paper

Resumen

Propósito – Un volumen creciente de trabajos sobre empresas familiares ha defendido que preservar la riqueza socio-emocional de la familia prevalece sobre el objetivo de perseguir resultados financieros. Nuestro propósito es desarrollar un marco conceptual que avance el conocimiento sobre la relación bidireccional entre la riqueza socio-emocional y la financiera, para de este modo desarrollar una teoría más completa que informe sobre los procesos de toma de decisiones en las empresas familiares.

Diseño/metodología – Examinamos conceptualmente como diferentes contingencias afectan a la relación entre riqueza financiera y socio-emocional (en ambas direcciones de causalidad).

Resultados – Predecimos cuando una determinada forma de riqueza (socio-emocional/financiera) es probable que domine a la otra (financiera/socio-emocional) en las decisiones estratégicas de las empresas familiares.

Originalidad/valor – El artículo genera conocimiento acerca de las relaciones bidireccionales entre riqueza socio-emocional y financiera, proporcionando una plataforma para el desarrollo del área de
investigación en empresas familiares, incluyendo la comprensión de las decisiones de las empresas familiares relativas al control y la influencia sobre el negocio familiar, su política medioambiental, el altruismo sobre los miembros de la familia, I+D, elecciones contables y diversificación corporativa.

Palabras clave Empresas familiares, Riqueza socio-emocional, Riqueza financiera
Tipo de artículo Trabajo de investigación

Introduction

Family firm decision-making is argued to differ from that of non-family firms due to their prioritizing of socioemotional (non-economic) goals over financial (economic) goals (Gomez-Mejia et al., 2011). For the most part, the literature seems to suggest that the pursuit of socioemotional utilities takes place at the expense of financial gains; yet, paradoxically, several reviews and empirical studies show that if anything, family controlled firms tend to outperform non-family controlled firms (Villalonga and Amit, 2006; Amit and Villalonga, 2014; Van Essen et al., 2011). This invites the possibilities that:

• socioemotional and financial goals may be mutually reinforcing;

• financial goals may be prioritized within family firms more so than family business research has previously acknowledged; or

• some elements of socioemotional wealth (SEW) may be negatively related to financial performance (e.g. nepotism, favoritism), while others are positively related to the achievement financial goals (e.g. greater commitment to firm, long term orientation) and thus the negatives and the positives of SEW in terms of economic outcomes may neutralize each other.

To date, we know little about how financial and socioemotional goals of family firms inter-relate, although once again, most of the literature assumes that the pursuit of SEW translates into suboptimal economic achievement, and thus that SEW gains and
financial gains are inversely related (Miller and Le Breton-Miller, 2014; Schulze and Kellermanns, 2015).

Possibly due to a lack of theoretical attention to how socioemotional and financial goals work in tandem, various mixed findings and contradictions have been revealed by prior family business research when it comes to examining the unique nature of strategic choices by family firms. For instance, family firms have been found to be more aggressive in accounting decisions (Stockmans et al., 2010; Chen et al., 2010); yet, other studies have found family owners to be more conservative in the same decision domain (Ali et al., 2007; Martin et al., 2016). Family owners have been argued to invest less in R&D (Gomez-Mejia et al., 2014); yet, they have also been portrayed as having a longer-term perspective (Miller and Le Breton Miller, 2005) and more “patient capital” (Sirmon and Hitt, 2003), which would seem to support the opposite prediction (Chrisman and Patel, 2012). Our study aims to provide a theoretical platform for family business scholars to re-visit these contradictions.

In sum, we offer a conceptual framework for examining the two-way relationship between socioemotional and financial forms of wealth, including contingencies affecting these relationships. We argue that contingencies affecting the relationship between socioemotional and financial factors are important to understanding heterogeneity in family firm decision-making. We further argue that to understand these contingencies, it is necessary to examine the relationship between various dimensions of family SEW (Berrone et al., 2012; Miller and Le Breton-Miller, 2014; Schulze and Kellermanns, 2015) and financial performance. That is, consistent with research highlighting the need to examine the effects of different sources of SEW (Miller and Le Breton-Miller, 2014; Schulze and Kellermanns, 2015), we build theory regarding how changes in SEW are likely to influence financial wealth (and vice versa) by building on theory that conceptualizes SEW as a multi-dimensional (as opposed to monolithic) construct.

Informed by our framework depicting the relationship between financial and SEW, we offer propositions that allow us to understand when financial or socioemotional factors are likely to dominate in family firm decision-making. Our theory aims to provide a platform for further development in the nascent field of family business research, including our understanding of family firm decisions regarding control and influence over the family business, environmental policy, altruism toward family members, R&D, accounting choices and corporate diversification.

**Family firm decision-making**

Decision-making processes that shape firm strategy have long been a focus of management and corporate governance research. In their seminal development of the behavioral theory of the firm, Cyert and March (1963) describe the complex inter-relationship of the various decision makers and units within a firm, which ultimately molds the firm’s decisions and strategic direction. This raises the controversial question of where to focus when examining decisions that ultimately manifest in the firm’s observable strategic choices. One stream of literature has explored the role of the top management teams (TMTs) and thus managerial discretion in shaping the strategic direction of the firm (Finkelstein and Hambrick, 1990). However, the idea that equity ownership results in influence and discretion in firm decision-making also has a long history in the management literature. In recent years, the family business literature has continued this tradition by focusing on the influence of
family principals over firm decisions through management and board representation (Schulze et al., 2003; Anderson and Reeb, 2004; Gomez-Mejia et al., 2007; Cruz et al., 2010; Miller et al., 2010; Berrone et al., 2010).

Emerging from this literature has been an intriguing picture of what sets the family firm apart from their non-family counterparts. The utilities guiding family firm decision-making were first examined in detail by Kets de Vries (1993) in a psychological study of family owners’ goals and prioritizations. Kets de Vries revealed that family owners prioritize goals related to the family’s affective needs over financial goals. That is, non-economic utilities were found to take priority over the economic utilities that had previously been assumed – within strategic management literature – to be the overriding priority across all business forms. The non-economic utilities related to family members’ social status, self-esteem and self-concept are argued to derive from the status and standing of their family’s firm (Westhead et al., 2001). Thus, the family is argued to enhance and preserve this non-economic utility – more recently referred to as a family’s SEW – in the context of behavioral agency theory (Gómez-Mejía et al., 2007, 2010, 2011; Berrone et al., 2010; Chrisman and Patel, 2012).

SEW is said to derive from a number of sources, including satisfying the needs of affect and intimacy (Kepner, 1983; Sharma, 2004), preserving the family dynasty (Casson, 1999; Berrone et al., 2012), caring for family members (Schulze et al., 2003; Westhead and Howorth, 2006) and enjoying the exercise of authority (Schulze et al., 2003). Various family firm decisions are purportedly influenced by the goal of preserving SEW, such as investment in environmental safeguards (Berrone et al., 2010), earnings management (Stockmans et al., 2010) and financial independence (Gomez-Mejia et al., 2007).

Socioemotional and financial wealth
While the caveat has been offered that family firms do not ignore the financial aspect of decisions that are motivated by preservation of family SEW, the relationship between financial performance and SEW is yet to be explicitly included in theorizing regarding family firm decision-making. The prevailing paradigm is well articulated by Berrone et al. (2010, p. 89):

The foregoing discussion is not meant to imply that family firms are self-sacrificial, pay exclusive attention to SEW, and/or ignore financial issues. Our key point is that when family interests predominate, firms are more likely to bear the cost and uncertainty involved in pursuing environment-friendly policies, driven by a belief that such a risk is counterbalanced by noneconomic utilities rather than the potential for current or future financial gains.

The above quote suggests family firms are cognizant of financial issues, yet assumes that concern for non-economic utilities will dominate in any calculus that weighs one against the other. Further, the quote also typifies the view often implicit in family firm research that:

- SEW and financial wealth are independent constructs;
- pursuit of SEW may compromise financial wealth; and
- the pursuit of financial wealth is prone to diminish the family’s SEW endowment.

We contend that this view greatly simplifies the complex relationship between socioemotional and financial outcomes and the family firm decision-making process.
We now examine this relationship between socioemotional and financial outcomes in greater detail by examining how one affects the other, by drawing upon various dimensions of SEW and the possibility that causality works in both directions. We first examine the causal effect of financial performance upon family SEW before later examining the reverse causal effect (of family SEW upon financial wealth).

Effect of financial performance upon socioemotional wealth

Negative effect of financial decline upon socioemotional wealth. Previous research has drawn attention to the loss of SEW that is associated with poor financial performance, such as the complete loss of SEW that would be associated with organizational failure (Gomez-Mejia et al., 2007). We now examine in further detail how financial performance is likely to influence family SEW. First, financial difficulties lead to a breakdown in trust between the firm and its stakeholders and with it loss of reputation for those who are associated with the family, such as equity owners and their executives (Gillespie and Dietz, 2009). Second, negative media publicity that may result from declining performance has deleterious reputational effects for the firm that is the subject of this publicity (Fombrun and Shanley, 1990). Below, we argue that the extent to which trust between the family firm and its stakeholders is broken – and family reputation damaged – due to poor performance is likely to be subject to boundary conditions. Specifically, we will argue that reputational damage to the family is likely to be dependent upon:

- the negative impact of declining family firm performance for the firm’s stakeholders; and
- the stakeholders’ perception of the degree to which actors within the failed firm were directly responsible for the failure and hence the harm inflicted upon the firm’s stakeholders (Gillespie and Dietz, 2009).

Regarding the degree of harm experienced by the firm’s stakeholders, drawing on studies that have argued that family relationships – or ties with the community – are a source of family SEW (Berrone et al., 2010; Cennamo et al., 2012; Gillespie and Dietz, 2009), if many stakeholders are negatively affected due to a family firm’s financial problems, the loss of reputation (and associated loss of family SEW) is likely to be more severe. Negative effects on stakeholders include employees who have lost their jobs, suppliers who have lost business or not have their invoices paid, creditors and minority equity shareholders who have lost money and other business partners who relied on the family firm. Given the actions of other firms in the focal firm’s networks can influence the focal firm’s reputation (Dacin et al., 1999), the harm inflicted upon other stakeholders of family firms may not only be financial, given their reputation may be tainted if they were also perceived as a partner or close associate of a struggling family firm.

By contrast to the situation where the family is perceived to have been negligent or careless, if the family owners are seen as innocent victims of an exogenous event, there is likely to be less reputation damage due to performance decline. For example, a family firm that has failed due to a natural disaster destroying their factory is likely to suffer less reputation damage relative to a family firm that has failed due to a fraud within the family firm. Similarly, if the family firm has suffered due to macroeconomic events but is perceived to have stood by their employees and suppliers despite financial hardship,
reputation damage – and the associated loss of family SEW along this dimension – is likely to be less severe.

The negative socioemotional effect of declining performance is not likely to be restricted to the reputational dimension of family SEW. Declining performance may necessitate the infusion of external capital (debt or equity) or the recruitment of external expertise to assist in navigating the business difficulties, meaning that family SEW associated with control or influence may suffer (Berrone et al., 2012). Also, declining performance means that family owners may have fewer resources to devote to SEW enhancing activities such as pollution prevention (Berrone et al., 2010) and community development projects (Gomez-Mejia et al., 2011). Similarly, the ability to pass a prosperous business on to the next generation (dynastic succession) could be negatively affected as performance declines. Thus, we offer the following proposition:

P1. Declines in financial performance will be associated with declines in family SEW.

Positive effect of financial performance upon socioemotional wealth. While poor financial performance is prone to negatively impact family SEW, the converse argument is that higher financial performance is likely to have a positive SEW effect for the family. We begin with the proposition that improvements in family firm financial performance are likely to be have a positive influence upon SEW, which we will follow with contingencies illustrating boundary conditions for this proposition.

The potential for enhanced family SEW due to superior firm performance upon SEW has been generally overlooked by prior family business research (Gomez-Mejia et al., 2011). Strong performance leading to expansion of the firm and/or positive publicity is likely to enhance the firm’s reputation and thus family owners’ SEW (Hammond and Slocum, 1996). This is because a firm’s reputation is closely tied to stakeholder perceptions of how well the firm is being managed (Hammond and Slocum, 1996). A further explanation for the positive relationship between firm performance and reputation is that higher performance generates slack, which in turn provides the cash necessary for socially responsible investments (Hammond and Slocum, 1996).

The same way that the relationship between poor financial performance and SEW is likely to be moderated by the negative implications for stakeholders and blame attributed to the family owners, we argue that the enhancement effect upon SEW due to superior financial performance is also likely to be dependent upon how the family firm’s performance positively influences stakeholders. Enhancements in SEW are more likely if the superior performance leads to greater generosity and munificence toward the firms’ stakeholders. For instance, customer satisfaction is positively related to firm reputation (Athanassopoulos, 2000), meaning that if the firm is more generous with its customers as a result of its financial success, reputation and therefore family SEW will benefit (Berrone et al., 2012).

By contrast to the situation where customers benefit from family firm financial success, if the firm’s success is perceived to be achieved at the expense of firm stakeholders, family SEW may not be enhanced but damaged. This derives from the relationship between corporate social performance (CSP) and family reputation (Berrone et al., 2010). For instance, if the family owns a supermarket and has achieved their success through reducing the profitability and wellbeing of their suppliers, family SEW will not benefit, given performance improvements will be accompanied by reputational
damage. Said differently, if financial performance is achieved at the expense of CSP, the family is likely to incur SEW losses (Berrone et al., 2010; Cennamo et al., 2012).

Rising performance is also likely to reduce the firm’s reliance on external capital (debt or equity), increasing family control presently or the probability of loss of control in the future (Chrisman and Patel, 2012; Gomez-Mejia et al., 2007). Similarly, strong financial performance will improve the firm’s resource slack that may be necessary to hire more staff (Huselid, 1995); as a result, family involvement could be increased through hiring additional family members. Stronger cash flow will also improve the probability that the firm will survive long enough to be passed on to the next generation.

Finally, financial performance is more likely to positively related to firm reputation where the performance is attributed to the superior management skills of the family, as opposed to exogenous factors such as an attractive industry, a booming economy or chance (Flanagan and O’Shaughnessy, 2005). Thus, when it is clear that the family has outperformed due to the talents of the family owners, there standing in the community is more likely to be enhanced.

In short, for all the reasons noted above, financial success should enhance family SEW. Thus:

\[ P2a. \] Increases in financial performance will be associated with increases in family SEW.

However, based on the preceding discussion, we summarize contingencies associated with the relationship between increasing financial performance and family SEW by offering the following propositions:

\[ P2b. \] The positive influence of financial performance upon family SEW will be lower (higher) if the firm’s stakeholders have experienced some form of harm (benefit) as a result.

\[ P2c. \] The positive influence of financial performance upon family SEW will be greater where changes in financial performance lead to greater involvement and control by the family.

\[ P2d. \] The positive influence of financial performance upon family SEW will be greater when the owner family is closer to passing the firm to the next family generation.

\[ P2e. \] The positive influence of financial performance upon family SEW will be greater where changes in financial performance are believed to be attributed to the skills of family members in managing and directing the firm.

**Extreme performance and socioemotional wealth.** Building upon the above propositions, we further suggest that the effect of performance upon SEW will be stronger in situations where performance changes are more extreme, such as performance declines leading to bankruptcy in the negative instance or industry leading performance in the positive case. Crises attract negative media attention, which in turn is likely to negatively influence firm reputation (Fombrun and Shanley, 1990). By extension, less extreme performance declines that are not considered a crisis is less likely to attract media attention. In terms of the control and dynastic succession dimensions of family SEW, extreme negative performance – such as cash flow issues leading to bankruptcy –
is more likely to threaten continuance of family involvement, whereas slight declines in performance pose less of a threat. We therefore theorize that minor changes in financial performance in the mid-range of what is considered to be acceptable performance are less likely to influence the family firm’s SEW. This is because the reputational, control and dynastic succession dimensions of SEW are all less likely to be affected if there are only small changes in performance that are unlikely to change perceptions of management ability, improve the capital position to change reliance on outsiders or the probability of handing the firm to the next generation, as discussed above. Thus, we propose that the aforementioned effect of financial performance upon SEW is most likely to be observed at the extreme ends of the performance spectrum:

\[ P3. \text{ The effect of financial performance upon family firm SEW is likely to be stronger at the more extreme ends of the performance spectrum.} \]

Having examined the relationship between financial and SEW by examining causality of financial factors upon SEW, we now examine causality in the reverse; that is, we examine the influence of socioemotional factors upon financial performance and wealth. As opposed to our theorizing above, we predict different relationships contingent on the SEW dimension in question, and therefore we break this next section into the different SEW dimensions.

Effect of socioemotional wealth dimensions upon financial performance
Miller and Le Breton-Miller (2014) have outlined the importance of identifying the source of SEW. In an initial attempt to address this issue, based on a review of the literature, Berrone et al. (2012) advance the idea that socioemotional factors motivating family firm behaviors derive from the following SEW sources (referred to as the FIBER model):

- family control and influence;
- family identification with the firm;
- binding social ties;
- emotional attachment; and
- renewal of family bonds through dynastic succession.

That is, instead of considering SEW as a monolithic construct, Berrone et al. argue that it is likely that these socioemotional dimensions may be discernable and could influence family behaviors and outcomes differently. We organize the following discussion by analyzing the impact of each of these dimensions of the FIBER model upon financial performance.

Family control and influence. The family control and influence dimension of SEW is likely to have negative performance effects. This was exhibited in a study of Spanish Olive Mills where the choice to join a cooperative had financial benefits but was likely to be shunned by family owners due to the perceived loss of control associated with joining the cooperative (Gomez-Mejia et al., 2007). The choice to not expand the firm due to the fear of losing control to outsiders – necessary to provide the capital and skills associated with expansion – could also come at a financial cost (Chrisman and Patel, 2012). For instance, they may not invest in the R&D necessary to defend against competitor technological advancement or to perpetuate competitive advantage associated with
technology (Chua et al., 2015). The reluctance to give up control is likely to lead to less innovation (Gomez-Mejia et al., 2014), lower internationalization (Gomez-Mejia et al., 2010), fewer professional managers at the top (Cruz et al., 2010) and greater entrenchment of family managers (Gomez-Mejia et al., 2001), all of which should have a negative impact on performance. Thus:

**P4.** Family SEW associated with a desire to maintain family control will be negatively related to firm performance.

**Family identification with the firm.** The extent to which a firm’s employees identify with the firm and its objectives (similar to the concept of employee engagement) has been positively associated with task performance (Carmeli et al., 2007). The logic being that firms engaged with the mission and the collective goals of the organization are likely to exert greater effort and engage in less unproductive, opportunistic or in the extreme, destructive behaviors. For instance, family owners are argued to extract greater output from R&D than non-family firms (Duran et al., 2015). This suggests that enhancements in this dimension of SEW – family identification with and emotional attachment to the firm – are likely to be positively related to firm performance:

**P5.** Family SEW associated with identification with the firm will be positively related to firm performance.

**Binding social ties.** A contingency likely to influence the intensity of the effect of family SEW upon firm performance is family involvement across the business, including the board, TMT and other levels of the business. A reason offered for the decline of family business is altruism in hiring of senior executives, meaning the best people may not be considered for key roles (Villalonga and Amit, 2006; Schulze et al., 2003). Excessive family involvement in the business, an unwillingness to rely on professional managers and the appointment of family members or their associates to the board might lead to overly centralized decisions, lack of fresh ideas and a limited skills set, all of which may lead to the foregoing of growth opportunities. Thus, too much emphasis on maintaining binding social ties within the firm linked to the family owners is likely to have a negative effect upon firm performance:

**P6.** The effect of family owners’ desire to maintain binding social ties within the firm by excluding non-family members from key managerial and board positions is likely to have a negative effect on performance.

**Family emotional attachment to firm.** Because family owners generally see the firm as an extension or an image of themselves, they tend to be deeply concerned about the firm’s reputation (Berrone et al., 2010). Reputation represents an intangible, difficult to imitate resource that allows for the development and leveraging of client relationships, raising of finance (on favorable terms) or influencing regulators (Fombrun and Shanley, 1990; Roberts and Dowling, 2002). Reputation can act as a barrier to entry, inhibiting entry and upward mobility of competitors (Wilson, 1985). Firm reputation may also provide quality signals regarding products and services to customers, allowing firms to charge a premium (Klein and Leffler, 1981; Milgrom and Roberts, 1986). Reputation in terms of corporate social responsibility (CSR) has been argued to positively influence a firm’s financial performance (McGuire et al., 1988). Along similar lines, corporate reputations
have also been demonstrated to allow firms to sustain superior profit outcomes over the longer run (Roberts and Dowling, 2002).

The above brief literature review suggests that reputation is likely to positively influence firm performance. This suggests that higher levels of family SEW associated with the reputational dimension will positively influence firm performance. Thus, we begin this sub-section with the proposition:

*P7a.* Family’s desire to maintain a good firm’s reputation will have a positive effect upon firm performance.

The studies reviewed above also provide the basis for identifying contingencies that affect the strength of the positive relationship between firm reputation and performance. First, regarding reputation as assisting in leveraging client relationships and providing a source of differentiation (Klein and Leffler, 1981; Milgrom and Roberts, 1986), it follows that reputation will be more beneficial in environments where competition is more intense, and it is therefore more difficult to win new clients or charge price premiums. For instance, reputation is likely to be less beneficial in high growth industries with few players relative to industries that are mature or commoditized; in the case of the latter, it is more likely that a source of differentiation – such as firm reputation – will provide market share benefits or allow for price premiums to be charged:

*P7b.* The effect of family owners’ desire to maintain a firm’s reputation upon firm performance will be stronger in more competitive market environments.

The access to capital provided by reputation (Beatty and Ritter, 1986) provides a contingency proposition, given there will be environments when access to capital is more of a problem, such as during periods of economic contraction or in industries that are considered higher risk (due to performance problems such as airlines, or volatility of earnings, such as high technology; Andersen et al., 2007) that traditionally find capital harder to come by. Thus:

*P7c.* The effect of family owners’ desire to maintain a firm’s reputation upon firm performance will be stronger in environments or industries where capital access is more restricted.

The relationship between reputation benefits provided by CSR and firm performance allows us to examine another contingency that influences the benefits of reputation (McGuire et al., 1988). The role of CSR in driving consumer purchasing behavior will vary across product markets and segments (Mohr et al., 2001). Hence, we argue that the performance effect of the family’s reputation driven by CSR will be dependent upon the extent to which CSR drives purchasing decisions in the family’s chosen markets. Thus:

*P7d.* The effect upon firm performance of the family owners’ desire to maintain reputation will be stronger when the firm’s customers value CSR.

*Renewal of family bonds through dynastic succession.* The last source of SEW in the FIBER model proposed by Berrone et al. (2012) – dynastic succession – may have a positive effect on performance at the founder stage, when founders are intent on passing a successful firm to their heirs. However, once the firm enters the post-founder stage, a desire to maintain the firm within the family for future generations may have a negative effect on financial performance. There are two reasons for this. First, founders generally
have a long-term orientation, which tends to shorten when future generations take over
the firm’s helm. Short-term strategies have are considered destructive by management
scholars (Drucker, 1986; Jensen and Murphy, 1990; Laverty, 1996; Marginson and
McAulay, 2008; Mueller and Reardon, 1993; Walsh and Seward, 1990). The converse of
these arguments is that a longer-term approach to business, which tends to characterize
founders’ attending to the firm “as their baby”, will lead to superior financial
performance. Thus, if family firms are focused on preserving SEW through the dynastic
succession of a successful firm, a longer-term approach to business is necessary, but this
is less likely to be the case past the founder stage.

Second, at later stages, identification with the firm and emotional attachment
weakens (which we argued have a positive effect on firm performance). Those who
inherit the firm from the founder may be more prone to harvest the firm’s resources
rather than to work harder to build a successful organization that may be handed down
to what Schulze et al. (2001) refer to as “a cousin consortium”. In one of the more
prominent studies of the relationship between family ownership and firm performance,
Villalonga and Amit (2006) find that family firm performance is likely to be less than
non-family firms in later (past the founder) stages. Thus, the effect of a dynastic motive
on firm performance is likely to turn from positive to negative, as the firm is handed
down from the founder to their heirs:

P8. Family SEW associated with dynastic succession will be positively related to
firm performance at the founder stage and negatively related to firm
performance as the firm moves through subsequent generations.

Pre-domination of socioemotional or financial factors
An important question that has emerged from the family firm literature has been:

Q1. When are socioemotional goals likely to pre-dominate financial goals (Berrone
et al., 2010; Martin et al., 2016; Gomez-Mejia et al., 2015)?

The pursuit of dual emotional and financial goals of family firms has been documented
or alluded to by various family business studies (Berrone et al., 2010; Chrisman and
Patel, 2012; Distelberg and Sorenson, 2009; Gomez-Mejia et al., 2007). For instance,
family owners are argued to accept greater business risk (and therefore greater risk of
financial losses) to preserve family SEW (Gomez-Mejia et al., 2007). Chrisman and Patel
(2012) make the insightful observation that policies aimed at preserving SEW are less
likely to be pursued when the family owners have failed to achieve performance
aspirations, suggesting that socioemotional and financial wealth goals converge as firm
performance declines. However, family business research continues to lack a conceptual
framework for understanding when and how these goals are likely to overlap or diverge.

Drawing on the above propositions illustrating contingencies influencing the
relationship between these forms of wealth, we could argue that if the contingencies lead
to a strong effect of one (SEW or financial) upon the other, it will be difficult to
disentangle the role of one or the other in influencing the family firm’s decisions. For
instance, if changes in SEW are associated with reputational issues, the socioemotional
and financial factors are indistinguishable in their effect upon family firm
decision-making. Conversely, when the contingencies described above do not play a
role, the socioemotional and financial consequences are likely to be separately
discernable and their impacts are more likely to be measurable.
By allowing us to anticipate when financial and SEW effects are likely to be related, the propositions we have provided above allow us to predict when either the socioemotional or financial influence is likely to predominate family firm decision-making. We have noted above that family firms are loss averse with regard to their stock of SEW and thus will act to preserve or enhance SEW at any opportunity. Yet, we have also noted that the family is likely to be cognizant of the financial consequences of their behaviors, given these are inextricably tied to SEW. It follows that the socioemotional concerns of the family are more likely to predominate financial concerns when the socioemotional consequences of their decisions are not expected to have a negative financial impact. Similarly, the family firm is likely to pursue financial goals when those goals are not expected to have a negative socioemotional impact:

**P9a.** Family firm decision-making will be directed at enhancing SEW when the choices being considered are neutral in terms of financial wealth.

**P9b.** Family firm decision-making will be directed at enhancing financial wealth when the choices being considered are neutral in terms of SEW.

**Mixed gambles and dual wealth concerns**

Implicit in much of the family business research (Berrone et al., 2010; Cruz et al., 2010) is that the first-order SEW preservation effect (for instance as a result of greater family control or reputation) of a family firm’s strategic choices will be large enough to over-ride concerns regarding a negative second-order effect upon SEW due to negative financial effects of these decisions. For instance, it has been suggested that family firms diversify less than non-family firms (Gomez-Mejia et al., 2010) and under-invest in R&D relative to non-family firms (Chrisman and Patel, 2012). The theoretical logic for this research, based on behavioral agency model (BAM)’s predictions with regard to individuals choosing to avoid losses of existing endowments of SEW, has been that family owners are:

- intent on preserving family control – and therefore family SEW – by avoiding decisions that expand the firm or bring in outsiders; and
- will do so despite the additional potential financial downside created by these decisions.

Given that our framework allows estimates of the socioemotional consequences of the financial downside of strategic decisions by family firms, we provide a basis for comparing the prospective socioemotional upside with the downside of family firm decisions; for instance, family owners could weigh the socioemotional control benefits against the socioemotional negatives created by potential financial losses triggered by the decision to hire a family CEO. The possibility of gain, as well as loss outcomes (for family SEW in family firm decision-making) in the family’s decision-making process, invites a mixed gamble approach to analyzing family owners’ decision-making. A mixed gamble is a decision with uncertain outcomes where there is the possibility of both gain and loss outcomes; the mixed gamble contrasts from simple gambles with only gain or only loss outcomes (Bromiley, 2009; Gomez-Mejia et al., 2014). While the mixed gamble approach to analyzing family firm decision-making has been used in family business research (Gomez-Mejia et al., 2014), our theory outlining prospective SEW gains and losses due to changes in financial wealth provides a foundation for using...
this logic more broadly in family business research. An example of this logic applied to family business research is that family firms may proceed with R&D if they anticipate that under-investing in R&D could yield socioemotional gains that are more than 2.5 times greater than the prospective socioemotional losses, based on the logic that potential gains must be at least 2.5 times greater than potential losses to entice individuals to proceed with the gamble (Kühberger, 1998). Hence:

\[ P10. \text{ Family firms will proceed with strategic decisions that preserve or enhance family SEW when the prospective SEW gains exceed the prospective SEW losses by a large enough multiple to justify the decision.} \]

Discussion and conclusions

Family firm decision-making has been the focus of a large volume of research activity, with the importance of this endeavor justified by the ubiquity of the family firm throughout the global economy. This research stream has benefited greatly from the socioemotional perspective, arguing that family firms are loss averse with regard to this non-economic form of family firm wealth (Berrone et al., 2010; Chrisman and Patel, 2012; Gomez-Mejia et al., 2007, 2010, 2014, 2010; Martin et al., 2016; Stockmans et al., 2010). The literature has featured many examples of family firm decision predictions relative to non-family firms – such as whether to invest in R&D (Chrisman and Patel, 2012), pursue diversification strategies (Gomez-Mejia et al., 2010), engage in earnings management (Stockmans et al., 2010) or choose an environmentally friendly policy (Berrone et al., 2010). The common theme across these studies has been the family owners goal of preserving family SEW, which is used to explain why the aforementioned behaviors differ from the non-family firm.

The aforementioned research examining the unique nature of family firm decision-making has acknowledged that there may be negative financial implications of preserving family SEW (Gomez-Mejia et al., 2007); however, the family business literature has also raised the possibility that family firms may see overlap of financial and socioeconomic goals, which have also been noted in this literature (Berrone et al., 2010; Gomez-Mejia et al., 2007; Stockmans et al., 2010). What this literature has lacked has been a reconciliation of these perspectives. That is, we lack a strong conceptual understanding of when family owners must trade-off conflicting financial and socioemotional goals versus family owners must pursue financial goals to preserve SEW. We have aimed to provide such a framework by examining a variety of dimensions of family SEW (Berrone et al., 2012) and the contexts in which each of these may relate to – positively or negatively – financial performance, in both causal directions. Thus, our theoretical insights have benefited greatly from conceiving of SEW as something other than a monolithic construct.

An implication of our propositions outlining positive relationships between financial and socioemotional goals is that family firms may pursue financial goals to increase family SEW; this refines the dominant theoretical perspective within family firm research suggesting that family owners’ primary concern is to preserve (minimize losses in) SEW (drawing upon behavioral decision theory’s concept of loss aversion, used by BAM). Our proposal to use a mixed gamble approach to analyzing family owners’ decision-making – in combination with our framework that allows for estimations of second-order SEW losses that may result from financial downside to SEW preservation...
(or enhancement) decisions – provides a foundation for re-visiting predictions regarding family decision-making (and how it is likely to differ from non-family firm decisions).

Finally, we have provided a theoretical basis challenging the assumption – implicit in much of the family business research (Berrone et al., 2010; Cruz et al., 2010) that the first-order SEW preservation effect (for instance as a result of greater family control or reputation) of a family firm’s strategic choices will exceed a negative second-order effect upon SEW due to negative financial effects of these decisions. For instance, it has been suggested that family firms diversify less than non-family firms (Gomez-Mejia et al., 2010) and under-invest in R&D relative to non-family firms (Chrisman and Patel, 2012). The theoretical logic for this research, based on BAM’s predictions with regard to individuals choosing to avoid losses of existing endowments of SEW, has been that family owners are:

• intent on preserving family control – and therefore family SEW – by avoiding decisions that expand the firm or bring in outsiders; and

• will do so despite the additional potential financial downside created by these decisions.

Our theory provides a framework for analyzing the socioemotional consequences of the downside, which can then be weighed against the first-order socioemotional benefits of the decision when predicting whether the family will proceed with the decision (or not).

Our framework implies that family owners may prioritize financial goals where the socioemotional benefits of those financial goals – such as the benefits of R&D, diversification or earnings management – are perceived as outweighing socioemotional costs. Similarly, family firms may sometimes choose not to pursue SEW preservation strategies where the second-order negative socioemotional effect – created by the financial implications of that strategy negatively affecting family SEW – of attempts to maintain control or family involvement are expected to be too great. For instance, the Walton family in the USA has incurred significant reputational damage as a result of some of the policies used by the firm to achieve the cost advantage that has been the key to their firm’s financial success. If one could predict the reputational impact of those cost reduction policies, the family may have taken greater care to place boundaries around the operational approaches used to achieve a low-cost position and financial success.

Practical implications
Previous guidance provided to family firm practitioners and other family firm stakeholders – including external investors weighing the decision to invest (or not) in family firms – has underlined the role of family owners’ loss aversion toward SEW in family firm decision-making. We refine that guidance by encouraging family owners or other stakeholders interested in predicting family firm behaviors to be cognizant of the potential influence for:

• financial performance to positively influence family SEW (and vice versa); and

• family socioemotional motives to positively influence financial performance.

Our theory reminds the family owners of the value in considering the potential for SEW gains that may flow from decisions aimed at achieving financial goals, highlighting the potential for socioemotional goals to be reinforcing of financial goals. That is, we provide a theoretical foundation for family owners or other family firm stakeholders to predict when
financial goals are likely to be given priority by family owners. Further, our theory encourages the family owners to be mindful of the potential for SEW gains – that might flow from financial performance – as opposed to being solely preoccupied with the potential for losses of SEW.

Conclusion

Our theory provides a framework for analyzing how financial wealth and SEW are likely to inter-relate to enhance predictive validity when applying BAM or the concept of mixed gambles to family firm decision-making. We have drawn upon the various dimensions of SEW to develop theory regarding contingencies likely to influence the strength of the socioemotional-financial relationship. Our theory implies that the family firm may consider financial goals a priority where they are consistent with socioemotional enhancement. Thus, we have emphasized that family owners are likely to not only be prescient regarding SEW losses as implied by much of the family socioemotional literature. The SEW gains may be due to:

- first-order consequences of the decisions – such as maintaining family control or the enjoyment of altruism toward family members; or
- the increased reputation, control, identification with the firm or dynastic succession due to better performance outcomes.

References


Further reading


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