THE IMPRINTING EFFECTS OF FAMILY FOUNDERS, ECONOMIC SHOCKS AND INSTITUTIONAL DEVELOPMENT ON FIRM INTERNATIONALIZATION

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ABSTRACT

We show that internationalization is contingent on the interplay between the economic and institutional environments during firm foundation, and the identity of firm founders. We find that family firms are more likely to internationalize if founded in less munificent economic and institutional environments, demonstrating the importance of imprinting effects.

INTRODUCTION

Internationalization is the process by which firms expand beyond domestic markets. Existing theories explain internationalization as arising from firm, market and resource-related factors (Buckley & Casson, 1976; Dunning, 1981). These theories do not, however, adequately examine how conditions at the time of a firm’s foundation affect subsequent internationalization. Since founding conditions imprint firms with characteristics that influence their long-term strategies, actions and performance (Marquis & Tilcsik, 2013; Simsek, Heavey, & Fox, 2014; Stinchcombe, 1965), it is possible that internationalization is partly a manifestation of historical conditions that existed at the time of firm foundation.

We argue that the propensity to internationalize is context specific and varies with founders, and with economic and institutional environments at the time of founding (Chrisman, Chua, & Kellermanns, 2009; Le Breton-Miller & Miller, 2008). The internationalization literature explains foreign expansion as a means for firms to exploit ownership-specific advantages, location-specific efficiencies or host country advantages (Buckley & Casson, 1976; Dunning, 1981). Meanwhile, “born-global” research attributes the early internationalization of young firms to their possession of an innovative culture, knowledge and capabilities (see, Knight & Cavusgil, 2004)) but does not explain the origin of these resources. Hence, these literatures attribute internationalization to contemporaneous forces without evaluating historical influences, particularly at the time of foundation. We address this gap by investigating the impact of initial firm and environmental conditions on internationalization.

We frame our analysis of the imprinting effects of initial conditions by focusing on family firms’ internationalization. We focus on family firms because they are more likely to be embedded with imprints, which are more likely to persist than for non-family firms (Gomez-Mejia, Makri, & Kintana, 2010). We predict that family firms’ founder characteristics, resource
constraints and prioritization of socioemotional wealth at foundation limit their subsequent internationalization, but that this impact is moderated by the economic and institutional environments at the time of foundation. We test our predictions with an unbalanced panel dataset over 19 years (1994 – 2012), evaluating the international expansion of 1,306 listed firms across multiple industries founded between 1994 and 2001 in six East Asian emerging economies.

THEORY AND HYPOTHESES

Imprinting and Family Businesses

Imprinting occurs because founders’ values and priorities, and the resources firms possess at founding influence organizations’ strategies, policies and culture (Eddleston, 2008; Geroski, Mata, & Portugal, 2010; Kriauciunas & Kale, 2006). These imprinting effects are embedded and persist through inertial forces of tradition, policies, ideology, institutionalization and routinization, which determine the norms, premises, “blue prints” and strategies that guide decision making. These in turn, are reinforced when fit with the environment enhances firm survival and growth (Baron, Hannan, & Burton, 1999; Shinkle & Kriauciunas, 2011; Stinchcombe, 1965). Though imprints can change and decay, their persistence in the face of organization evolution and environmental change demonstrates their long term impact (Marquis & Tilcsik, 2013; Perkmann & Spicer, 2014).

Importantly, imprinting is driven by founders’ priorities, preferences and characteristics (Baron et al., 1999; Stinchcombe, 1965) and even environmental effects are imprinted by influencing founders (Johnson, 2007). Variance in founder quality, characteristics and priorities therefore influence the nature of imprinting. Family businesses are particularly influenced by founder characteristics, because of the greater priority they place on preserving socioemotional wealth (Chrisman et al., 2009; Le Breton-Miller & Miller, 2008). The importance that family firms place on non-economic goals is manifested in their prioritization of maintaining ownership and operational control, ensuring continuity of the family business for future generations, and sustaining the image and reputation of the family (Berrone, Cruz, & Gomez-Mejia, 2012; Gomez-Mejia, Cruz, Berrone, & De Castro, 2011). These priorities affect how problems are framed and strategic choices made (Wiseman & Gomez-Mejia, 1998). Indeed, family firms are more likely to preserve socioemotional wealth even at the cost of firm performance (Gomez-Mejia et al., 2011; Gomez-Mejia et al., 2010).

Family Firms and Internationalization

Firms are more likely to internationalize if they have greater ownership-specific advantages relative to foreign competitors (Dunning, 1981). This suggests that resource endowments are a predictor of internationalization. However, the internationalization literature evaluates resources at the time of internationalization, rather than at foundation. For family firms, the decision to internationalize is a particular predicament: though foreign expansion offers opportunities to grow, the process of internationalization challenges these firms’ in areas influenced by their founding characteristics, specifically in their possession of resources and their prioritization of socioemotional wealth. Family firms are likely to face greater constraints on raising resources at foundation than other firms because they often lack the track record, assets or sponsorship of other organizations (Miller, Le Breton-Miller, Lester, & Cannella,
Family firms also face greater managerial constraints as they are often reluctant to incorporate non-family leaders because of increased monitoring costs and the risk of losing control (Gomez-Mejia et al., 2010). Family owners typically have limited social and political ties in foreign markets (Acquaah, 2012) increasing the costs of the liabilities of “foreignness” and “outsidership” in international markets (Johanson & Vahlne, 2009; Zaheer, 1995).

Resource constraints and socioemotional wealth priorities at foundation are especially powerful in imprinting family firms’ structures, operations, cultures and values with qualities that reduce the likelihood of subsequent internationalization. As family members entrench themselves in the organization, family firms experience greater continuity in formal and informal processes than other firms. These family firms therefore experience stronger and more persistent imprints than other firms. These imprints result in family firms adopting strategies that limit resource utilization and that prioritize control over more risky options, reducing the likelihood of internationalization. In contrast, non-family firms are more likely to seek and obtain resources from external stakeholders at the time of founding, even at the cost of reduced ownership and control. Non-family firms may also differ from family firms in balancing profitability, growth and survival, as they are potentially more willing to risk survival for growth and profitability. Hence, non-family firms are less likely to experience strong or persistent imprints that discourage internationalization. For these reasons, we predict that:

**Hypothesis 1**: Family firms are less likely to internationalize than non-family firms.

**Economic Shocks and Internationalization**

Imprinting theory argues that the external environment at the time of founding has lasting effects on firms’ strategic choices, structures and development (Carroll & Hannan, 1989; Stinchcombe, 1965). Environmental imprinting occurs through new firms adopting strategies or practices that fit the environment, resulting in improved performance (Kriauciunas & Kale, 2006). We expect differences in environments, resource availability and imprints to be particularly great for firms founded during economic shocks relative to those founded in non-shock periods. An economic shock is a sudden, substantial and unanticipated change in the macroeconomic environment whose impact spreads beyond specific firms or industries to disrupt multiple sectors of an economy simultaneously (Singh, Mahmood, & Zhu, 2014). Thus, firms founded during economic shocks are established and operate under predominantly severe resource constraints; this in turn attunes them to operate under tight resource constraints and difficult external conditions. Firms with weaker initial resource endowments will face greater difficulties in developing the capabilities needed to achieve subsequent growth and internationalization, compared to firms with superior initial resource endowments. Limited initial resources increase the liability of newness (Stinchcombe, 1965) and lead to higher failure rates over time (Geroski et al., 2010). Imprinting effects derived from resources and environmental conditions may be more persistent than other imprints and are therefore more likely to inhibit a firm’s ability to grow, adapt or learn in future (Geroski et al., 2010; Kriauciunas & Kale, 2006). We expect these effects to influence internationalization, with firms founded during economic shocks being more conservative in investing resources in strategies that are risky or that consume resources extensively, such as international expansion:
Hypothesis 2: Firms founded during economic shocks are less likely to internationalize than firms founded during non-shock periods.

Institutional Environments and Internationalization

Institutions are essential components of the external environment, defining the formal and informal rules that dictate how firms operate (North, 1990). The choices that firms make at foundation, as dictated by the rules of the institutional environment, become imprinted in the routines, structure, development and the strategic conduct of firms (North, 1990; Stinchcombe, 1965). Differences in institutional development manifest themselves in the different types of incentives that govern the way new firms acquire, accumulate and deploy resources; this in turn influences how firms internationalize. More developed institutions impose greater pressures on firms to meet performance norms and enforce regulations more effectively, thereby encouraging a greater focus on firm outcomes from foundation. Consequently, firms founded in a more developed institutional environment are likely to be imprinted with the structures, routines and practices that support the development of superior initial resource endowments, and the subsequent development of capabilities to support internationalization. In contrast, firms founded in a less developed institutional environment will receive weaker initial support, and face weaker incentives and pressures for performance. As a result, firms in these environments are likely to be constrained from developing the capabilities needed to achieve competitive advantage that support internationalization. In general, firms in these environments are likely to have inferior initial resource endowments and face weaker incentives to perform, the imprints of which will influence their subsequent development and internationalization. Hence, we expect that:

Hypothesis 3: Firms founded in less developed institutional environments are less likely to internationalize than firms founded in more developed institutional environments.

Family Firms and Economic Shocks

Gomez-Mejia et al. (2010) found that family firms facing high systematic risks or threats to their performance are more willing to risk socioemotional wealth in favour of economic performance. Extending this logic, we expect that family firms founded during economic shocks are likely to be imprinted with qualities and values that assign relatively high priority to economic goals. Hence, the adverse conditions for firms founded during economic shocks will imprint firms with the need to reduce the risks of geographic concentration to mitigate the threats of economic shocks. Therefore, we predict that family firms founded during economic shocks are more likely to internationalize to achieve geographic diversification than family firms founded outside of economic shocks:

Hypothesis 4: The interaction of family ownership and economic environments will influence internationalization, so that family firms founded during economic shocks are more likely to internationalize than family firms founded during non-shock periods.

Family Firms and Institutional Environments
Hypothesis 3 proposes that firms founded in more developed institutional environments are more likely to internationalize. We expect this to apply to family firms as well, so that the advantages of being founded in a more developed institutional environment will moderate the imprints of family ownership that discourages internationalization. In particular, firms will be more likely to overcome the disadvantages of family ownership with respect to internationalization through more developed institutions providing enhanced access to resources, greater incentives to perform and greater support through intermediaries. In turn, this will increase family firms’ focus on performance, and increase the likelihood that family firms founded in more developed institutional environments will internationalize relative to family firms founded in less developed environments. Therefore, we propose that:

**Hypothesis 5:** The interaction of family ownership and institutional environments will influence internationalization so that family firms founded in more developed institutional environments are more likely to internationalize than family firms founded in less developed institutional environments.

### DATA, MEASURES AND METHOD

We locate our study in six East Asian emerging markets from 1994 to 2012: Hong Kong, Singapore, Taiwan, Malaysia, Thailand and Indonesia. Our sample consists of 1,306 listed firms across multiple industries, founded between 1994 and 2001. We use the date of incorporation as the date of founding because being established as a legal corporation is a clear indication of founders’ intention to maintain the firm as an ongoing entity (Tucker, Singh, & Meinhard, 1990). Our sampling period allows for better demarcation and evaluation of the founding conditions-internationalization relationship across different levels of institutional development during and outside an economy-wide shock (Chakrabarti, Singh, & Mahmood, 2007; Wan & Yiu, 2009).

**Measures**

The dependent variable is the foreign sales ratio, defined as a firm’s foreign sales divided by its total sales for each year. The key explanatory variable for Hypotheses 1 is family founders. We define founders using the following criteria: (1) those identified as founders in at least two public sources (Villalonga & Amit, 2010); (2) the largest shareholders, with at least 10% of ownership at incorporation (Boubakri, Guedhami, & Mishra, 2010; Gomez-Mejia et al., 2010); or (3) those who are officers or directors at the time of the firm’s formal date of incorporation or establishment. We classify a firm as a family firm at founding if it meets three criteria: (1) it was founded by more than one member of a family, who were related by blood or marriage; (2) the founders were officers or directors of the firm; and (3) founders directly or indirectly owned more than 10% of the shares at inception and throughout the duration of the study. Economic shock is an indicator variable which notes if firms were founded during an economic shock, defined as the Asian Economic Crisis of 1997 to 1998. For our institutional environment variable, we draw from Berry, Guillén, & Zhou (2010) to develop a measure of each economy’s state of institutional development using four dimensions: (1) National business systems (Whitley, 1992) measures differences in the administrative, legal and political practices that influence how firms operate within countries; (2) Economic development captures the state of development and openness of each economy; (3) Capital markets measures the impact of financial institutions on
firms’ access to resources and support, which influence firm formation, operations and performance (La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 1998); and (4) Technological development measures the development of technology and innovation as proxies for infrastructure development and overall openness of the economy (Nelson & Rosenberg, 1993). We develop an index of institutional development using these four dimensions. Finally, we use a host of controls including firm (size, age, current ratio, debt ratio, slack, ROA, listing type, diversification), industry dummies; and country (GDP growth rate).

Analyses

Although we observe the entire sample of firms founded between 1994 and 2001, firms may have self-selected to incorporate themselves during the shock, with more risk-oriented founders being more likely to do so. These firms might also be more likely to subsequently internationalize. Thus, formation during the shock is possibly endogenous. We employ 2SLS instrumental variable estimation to correct for this potential endogeneity (Wooldridge, 2010), using country and firm instrumental variables.

RESULTS AND DISCUSSION

We find broad support for our hypotheses and for the importance of founder, economic and institutional imprinting effects on internationalization. We predict that imprints of founding conditions have persistent effects on the likelihood of firms internationalizing and find that family firms (H1); firms that were founded during shocks (H2); and firms that were founded in more developed institutional environment (H3), are less likely to internationalize. We also find that family firms founded in less munificent environments, i.e. during economic shocks (H4) and in less developed institutional environments (H5), are more likely to internationalize. (All results are available from the authors).

We make three theoretical contributions. First, we link and build on the organizational imprinting and internationalization literatures, providing a new perspective and explanation for why firms may expand across borders. By evaluating a combination of firm, economic and institutional imprinting effects, we address calls to examine the complexity of multiple imprints (Johnson, 2007), an aspect that has received little empirical attention (Marquis & Tilcsik, 2013). We show the impact of founding conditions on internationalization, a decision that has largely been attributed to firm and market conditions; this reinforces the importance and persistence of imprinting, the effects of which are under-researched in strategy. Second, we extend the internationalization and family business literatures by improving understanding of how family businesses expand internationally, an understudied issue particularly in emerging economy contexts (Pukall & Calabrò, 2013). Third, we link the internationalization and economic shock literatures. Though economic shocks are an important phenomenon and offer useful theorizing opportunities on the effects of adverse and rapidly changing environments, they have attracted limited attention in strategy research (Agarwal, Barney, Foss, & Klein, 2009; Singh et al., 2014).

REFERENCES AVAILABLE FROM THE AUTHOR(S)