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# **Social capital in entrepreneurial family businesses: The role of trust**

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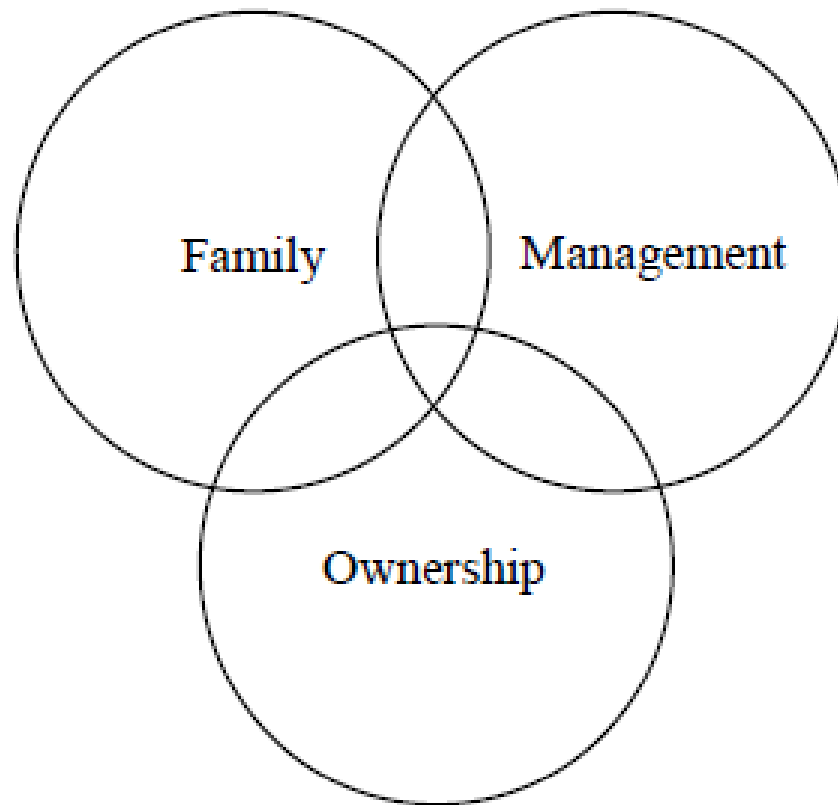
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# Background

- What is social capital (cf., financial and human capital) and how does it influence entrepreneurship and innovation in SMEs?
- Entrepreneurs typically pursue “ambiguous, changing and constructed goals” (Sarasvathy, 2001, p. 244), and often base the processes on unfamiliar and unstable socio-economic relations.
- Trust helps reduce transaction costs in unfamiliar environments, as an “adaptor” or “lubricant” that translates the complex and formal transactional relations into flexible and informal bonds between actors (Puffer *et al.*, 2010).
- Trust, as a relational form of social capital (cf., structural and cognitive forms), is believed to be important source of competitive advantage for SMEs (Arregle et al., 2007).
- What is trust? Its sources and types?
- A “dark side” of trust, or side effects?

# The family business



The three-circle model (Gersick *et al.*, 1997)

# Introduction

- Family businesses (FBs) are an enduring institution for entrepreneurship (Craig *et al.*, 2009), usually with an entrepreneurial culture underpinning family entrepreneurial teams (Discua Cruz *et al.*, 2013).
- By being entrepreneurial, FBs are more likely to sustain growth and performance across generations (Steier, 2007).
- At the intersection of the family system and the business system, FBs engage relations and values from both systems, including the trusting relationships, that yield unique and important influences on entrepreneurship (Shi, 2014).
- Prior studies take a static and single-dimensional view (Sundaramurthy, 2008), claiming that trust, in an unspecified form, is conducive to entrepreneurship in FBs, mainly because trust strengthens relationships in the family (Dyer, 2012).
- However, trust is a dynamic and multi-dimensional notion (Welter, 2012). And there can be a potential “dark side” as high levels of trust may be associated with a “blind faith” (Eddleston *et al.*, 2010, p. 1044).
- Knowledge is demanded on sources and types of trust, and their effects on firm performance.

# Research questions

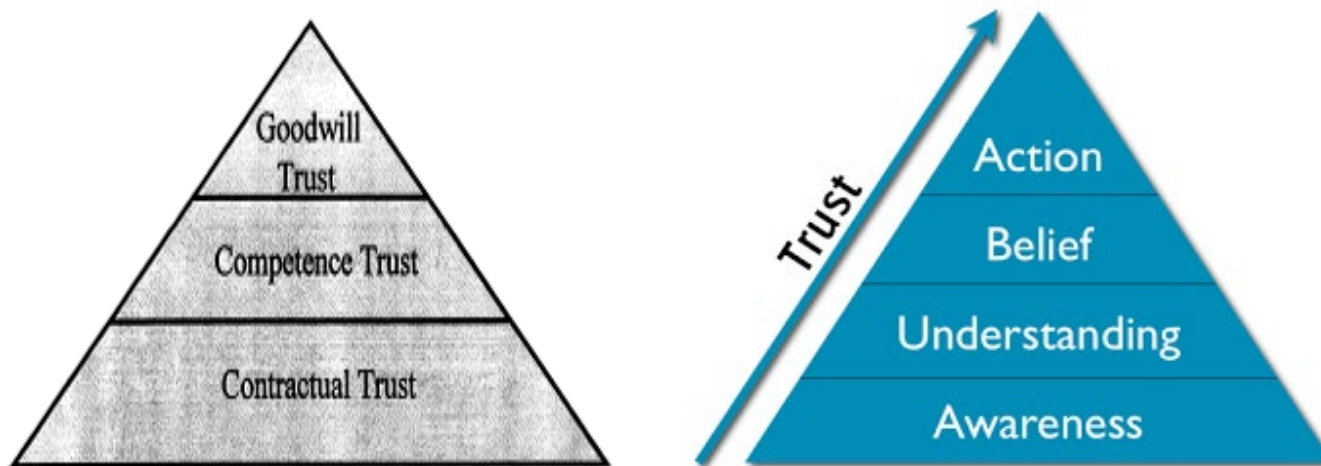
1. Where does trust originate in family businesses?
2. How does trust influence the entrepreneurial processes in family businesses?

# Social capital

- Distinctive from financial capital and human capital
- Embedded in, available through, and derived from networks of relationships and interactivities between individuals or social units (Nahapiet & Ghoshal, 1998), e.g., families and businesses
- Two perspectives of antecedents of social capital:
  - Structural holes (Burt, 1992) that are inherent in a network structure, enabling an individual to broker between unconnected individuals within his or her network;
  - Network closure (Coleman, 1988) that allows for access to information and effective sanctions within the closed network.
- Hence, two aspects in understanding the essence of social capital – *exchange* and *interaction*.

# Trust

- A relational form of social capital
- A psych state comprising intentions to accept vulnerability based on positive expectations of others' intention or behaviour (Sitkin et al., 1998)
- Dynamic, evolutionary, and strengthened as interaction increases; hence a 3-stage framework - calculus-based, knowledge-based, identification-based (Lewicki & Bunker, 1996)
- In reality, the development of trust does not necessarily follow a step-by-step sequence, but is reversible and dependent on circumstances and relations that impact the calculation, knowledge, and identification
- For example, kinship relations often provide a “short-cut” for identification-based trust (Lane, 1998), with little to no calculus- or knowledge-based trust as prerequisites
- Focus shifted to the level of trust (interpersonal, organisational, institutional) and source of trust (goodwill, competence, contractual) (Fukuyama, 1995; Lane, 1998; Lui, 2009; Sako, 1992)



# Trust and entrepreneurship

- Literature focuses on the positive effects, facilitating entrepreneurial performance, e.g., reducing transaction costs in unfamiliar environments, mobilising through network to access resources and opportunities
- Potential “dark side”, e.g., it may impose mental conformity on all actors in the network (Dana & Morris, 2007), locking actors within the loyalty relationship (Prause et al., 2013) away from openness and newness (cf., Granovetter, 1973, 1985)

## Trust in family businesses

- Family ties form a ground for goodwill trust, which serves “as an organizing principle for family firms” (Eddleston *et al.*, 2010, p. 1044):
  - form the entrepreneurial teams (Discua Cruz *et al.*, 2013)
  - play a critical role in strategic decision-making, networking, relationship building, resource acquisition and organisation, opportunity creation and exploitation (Shi, 2014).
- There is a flip side too:
  - Groupthink – members restricted to existing networks
  - Centre of gravity/power – incompetent (but trusted) leader
  - Family conflicts – distrust, ongoing socioemotional costs (cf., SEW)

# Methodology and methods

## Exploratory nature

- Qualitative, case-study approach
- Semi-structured interview, observation, and document inspection
- Eight Chinese FB SMEs, 2<sup>nd</sup> generation, manufacturing

Company	From	Industry	Workforce	SOM's age at succession	SOM's siblings	Founder retired for
CHE92	1992	Chemical manufacturing, financing	1,000	24	1 younger sister	Lifestyle
HIT02	2002	High-tech R&D and manufacturing, real estate	250	28	1 elder brother	Lifestyle
MAC83	1983	Machinery manufacturing	90	32	2 elder sisters	Lifestyle
MAC90	1990	Machinery manufacturing	70	36	1 younger brother	Lifestyle
MAC94	1994	Machinery manufacturing, retailing	120	30	Nil	Other business
MAC95	1995	Machinery manufacturing	160	27	2 elder siblings	Lifestyle
TEX90	1990	Textile manufacturing	110	28	Nil	Other business
TEX92	1992	Textile manufacturing	180	31	1 younger brother	Health

## Findings: Levels and sources of trust

- Organisational structure nuanced by family ownership and management, providing an unstable ground for trust to develop at a more collective level
- Interpersonal trust as a critical and indispensable resource that either “facilitated” or “promoted” opportunity creation and exploitation
- Two common effects on entrepreneurial processes:
  - OMs freed from routine and miscellaneous operations, to concentrate on strategic development and entrepreneurial venturing (via power delegation, mostly implicit)
  - OMs connected to sources of necessary resources for opportunity creation and exploitation (via networking and relationship building)
- Individual competence and interpersonal goodwill constituted the most reliable and durable source of trust, while contractual trust was emerging and marginal
- “Bloody is thicker than water” vs. “*Good* blood is thicker than water”

## Findings: Patterns of trusting relationships

- Employment is neither the only nor most important indication; the existence of a “second person” (cf., deputy or delegate) in all case companies, who deeply involved and influence decision-making and operations

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Business	Position of “2nd person”	Relation to SOM	Explicit/implicit appointment
CHE92	Deputy Manager	Uncle	Implicit
HIT02	Senior Advisor	Father's deputy in 1st generation	Implicit
MAC83	Line Manager	Brother-in-law	Implicit
MAC90	Not an employee	Wife	Implicit
MAC94	Not an employee	Husband	Implicit
MAC95	Founder	Father	Explicit
TEX90	Founder	Father	Explicit
TEX92	Deputy Manager	Father's line manager in 1st generation	Explicit

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- Three pattern types observed:
  - Kinship goodwill
  - Kinship goodwill + individual competence
  - Kinship goodwill + contractual commitment

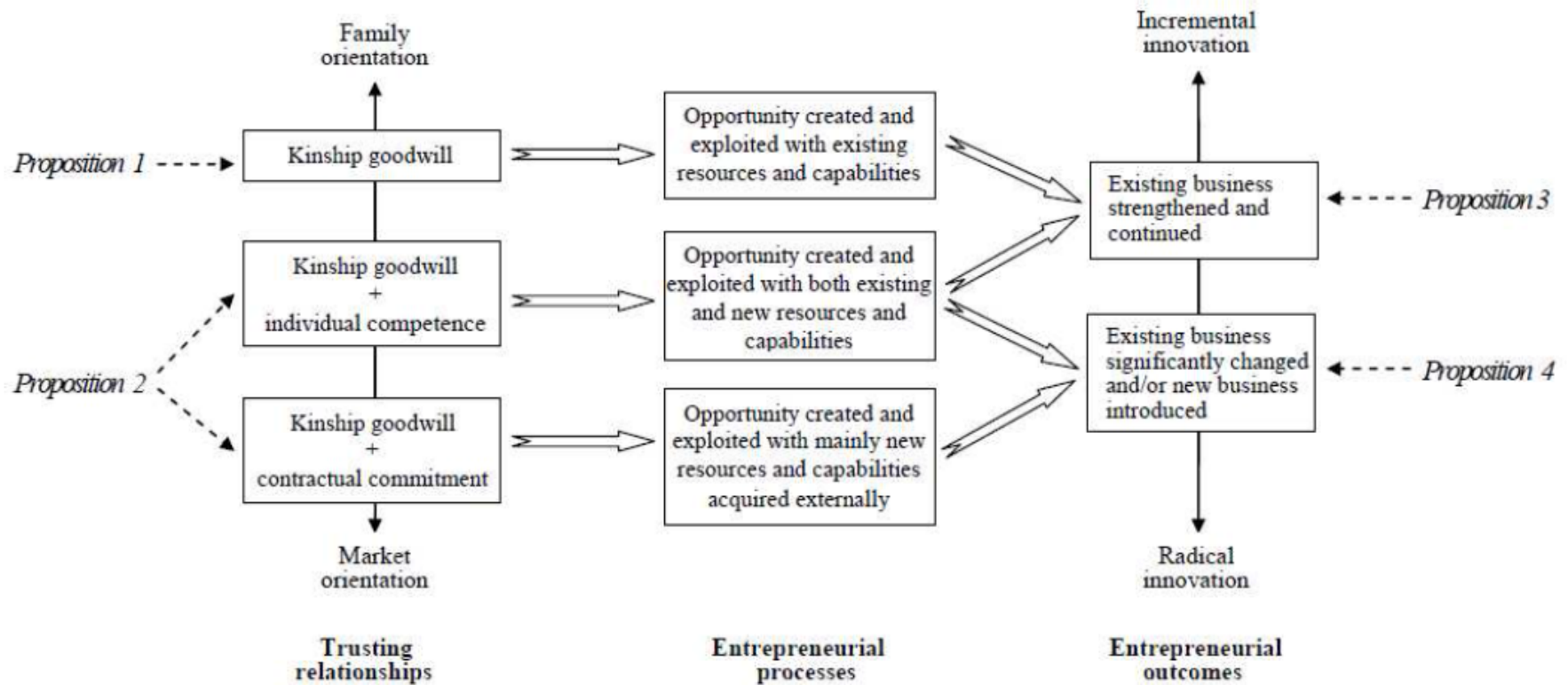
# Findings: Effects of trust on entrepreneurship

- Schumpeterian approach to understand innovations as entrepreneurial outcomes in established FBs (cf., new venture creation)
  - source of opportunity,
  - resource acquisition and deployment, and
  - nature of innovations produced
- When trusting relationships were mainly structured around kinship goodwill (MAC95, TEX90), a family-focused value orientation tended to be more likely to guide entrepreneurial processes, where
  - Opportunities perceived and created internally
  - To strengthen existing business and improve firm performance without radical changes
- Combination of competence and goodwill trust (CHE92, MAC83, MAC90, MAC94) enabled reaching out for external opportunities and resources
  - less emphasis on maintaining existing business
  - more open to information from the market than internal practices
- When trust was formed mainly on the basis of individual competence (HITo2, TEX92), with little consideration of kinship goodwill
  - mostly market-oriented approach
  - the only pattern where contractual trust was perceived

## Findings: The potential “dark side” of trust

- A typical “strong tie effect” (cf., Granovetter, 1973) in opportunity recognition and exploitation (e.g., MAC95, TEX90)
- Trust based on overestimated competence (e.g., MAC83) – excessive trust in individual competence led to extra cost and may have misguided the entrepreneurial process (cf., Welter, 2012)
- Role-specific competence trust (i.e., little affect-based goodwill) required coordination across positions, which was potentially costly (e.g., HITo2, TEX92)
- Knowledge transfer to outsiders was difficult given a lack of goodwill, which undermined altruism

# Conceptual model and propositions



P1. Trust in small to medium-sized Chinese FBs is mainly constructed at the interpersonal level, on the basis of kinship relationships.

P2. Trust in Chinese FBs starts to progress to less kinship-based types.

P3. Goodwill trust is associated with a greater family orientation, and leads the entrepreneurial processes to incremental innovations.

P4. Contractual trust is associated with a greater market orientation, and leads the entrepreneurial processes to radical innovations.

# Contributions and implications

- Theorisation of trust as a relational form of social capital - we identified patterns of trusting relationships and argue trust is a dynamic construct developing in different patterns from different sources, and resulting in different outcomes.
- Insights to trust in Chinese FBs – individual competence and contractual commitment documented as emerging sources.
- Documented “side effects” of trust on entrepreneurship and innovation – exclusive reliance on trustees rejects opportunities from remote and less trusted sources; unrealistic over-estimate of trustees’ competence resulted in extra costs.
- Practical implications for OM s and policy-makers.

# Limitations and future research

- Interview processes: local business norm and cultural concerns
- Translation
- Generalisability
- There might be more patterns, a need of larger-size studies
- Intergenerational differences
- The “dark side” of trust, and social capital, on innovation and entrepreneurship
- International comparative studies

*Thank You*

*Gracias*

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ありがとうございます