

## Why do some family firms take more risks than others?

*Navigating the balance between preserving tradition and embracing risk to secure long-term success*

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Family businesses are often viewed as reluctant to take risks, largely because they must balance financial imperatives with a deep emotional attachment to their enterprise. Unlike non-family firms, which focus primarily on financial returns, family firms are driven by both economic and socioemotional wealth. This means they prioritize aspects such as family reputation, legacy, and control over the company. The desire to protect these non-financial benefits can result in risk-averse behavior, as family owners may be unwilling to jeopardize their influence and status for uncertain financial gains. However, this view does not fully capture the diversity of risk-taking behaviors within family firms. Some family businesses actively engage in bold strategic moves, invest in innovation, and pursue ambitious expansion plans. Others maintain a cautious approach, favoring stability over disruptive change.

This research introduces a novel perspective by proposing that the **implicit beliefs of family business owners**, shaped by key organizational characteristics, determine their willingness to take risks. The study builds on the **Socioemotional Wealth (SEW) framework**, which explains how family firms prioritize emotional and identity-related goals, and integrates it with **Implicit Theories**, a psychological concept that describes how individuals interpret reality. Those with an **entity mindset** see their business as inherently fixed and resistant to change, while those with an **incremental mindset** perceive it as flexible and capable of adaptation. The research suggests that the strength of SEW in a family firm influences whether owners adopt an entity or incremental perspective,

which in turn shapes their strategic risk-taking behavior.

### WHAT WE STUDIED

This study leverages **Socioemotional Wealth (SEW) theory**, which posits that family firms make strategic choices based on both financial and non-financial considerations. SEW encompasses factors such as family control, identity, reputation, and intergenerational succession. The more a family firm prioritizes these socioemotional benefits, the less likely it is to engage in decisions that could threaten them. However, SEW alone does not fully explain why some family firms are more risk-averse than others. To address this gap, the study incorporates **Implicit Theories**, which refer to the cognitive frameworks individuals use to interpret reality. Implicit Theories suggest that individuals develop different perspectives on change and stability:

- Those with an **entity mindset** believe that core characteristics of their business, such as its structure, values, and competitive position, are largely fixed and unchangeable. As a result, they are less inclined to take risks, as they perceive little benefit in attempting to alter something that is inherently stable.
- Those with an **incremental mindset** see their business as dynamic and malleable, believing that change and adaptation can lead to positive outcomes. These individuals are more open to taking strategic risks, as they perceive uncertainty as an opportunity rather than a threat.

The study theorizes that SEW intensity—how strongly a family firm prioritizes socioemotional goals—determines which of these mindsets dominates. Four organizational characteristics influence this dynamic: the **salience of family identity versus business identity**, the **founder's imprint on the firm's values and decision-making**, the **stage of generational ownership**, and the **firm's historical trajectory of success or failure**.

## KEY INSIGHTS

A firm's identity plays a crucial role in shaping its approach to risk. Family firms that emphasize **family identity over business identity** tend to exhibit a higher intensity of SEW, as they are deeply invested in preserving traditions and maintaining family control. In such firms, owners are more likely to adopt an **entity mindset**, resisting strategic changes that could disrupt their established legacy. By contrast, family firms that prioritize **business identity** over family heritage are more open to transformation and innovation. Their leaders recognize the need to adapt to external market forces and are thus more inclined to take calculated risks.

Another key factor influencing risk-taking is the extent to which a **founder's imprint** remains embedded in the company's culture and decision-making processes. When a family firm is still guided by the values and strategies of its founder, it is more likely to adhere to traditional approaches and avoid deviations from the original business model. This reinforces an entity-oriented perspective, where change is viewed as unnecessary or even detrimental. However, as the firm transitions to later generations of ownership, the founder's influence begins to wane, allowing new decision-makers to explore alternative strategies and adopt a more incremental approach.

The **generational stage** of a family business also shapes its risk preferences. First-generation family firms, where ownership and control are concentrated within a single founding family, tend to exhibit strong SEW intensity and an entity mindset, making them less likely to engage in high-risk strategic moves. As ownership transitions to later generations, however, the emotional attachment to the business often diminishes. With more diverse perspectives emerging among family shareholders, there is a greater willingness to experiment with new business strategies, leading to an increased likelihood of risk-taking.

A family firm's **historical trajectory of success or failure** further influences its risk orientation. Firms that have experienced a long history of success tend to reinforce the belief that their existing strategies are

effective, reducing the perceived need for change. These firms develop an entity mindset, prioritizing stability and continuity. In contrast, family firms that have faced financial difficulties or market disruptions may become more receptive to change, recognizing that their survival depends on adaptation. In such cases, they shift toward an incremental mindset, embracing risk as a necessary response to external pressures.

## TAKEAWAYS

This study provides a deeper understanding of why some family firms are risk-averse while others embrace uncertainty. It highlights the importance of **cognitive framing** in strategic decision-making, emphasizing that risk preferences are not solely driven by financial considerations but are also shaped by deeply ingrained psychological perspectives. By recognizing the influence of implicit theories, family business leaders can take a more proactive approach to balancing tradition with innovation.

For practitioners, these findings suggest that **periodic reassessments of risk orientation** can help family firms adapt to changing market conditions. Family business owners should evaluate whether their current strategic approach aligns with their long-term objectives and consider whether their risk preferences need to evolve over time. Developing a **structured approach to risk management**, where small-scale innovations are tested before committing to major strategic shifts, can help mitigate potential downsides while fostering an environment of adaptability.

Some advises:

### 1. Assess Your Firm's Risk Mindset

Family business leaders should reflect on whether they operate with an entity or incremental mindset. Understanding this can help them make more balanced decisions and avoid knee-jerk reactions based on tradition or fear.

### 2. Balance SEW and Business Goals

Preserving the family legacy is important, but it should not come at the cost of innovation and growth. Leaders should find ways to balance emotional and financial goals when making strategic decisions.

### 3. Be Open to Change Across Generations

Next-generation leaders often bring new perspectives that can help the firm adapt to changing market conditions. Encouraging a culture of learning and adaptation can prevent stagnation.

### 4. Don't Let Past Success Lead to Complacency

While a strong track record can create confidence, it can also lead to rigidity. Business owners should

continually re-evaluate their strategies and embrace calculated risks to stay competitive.

### 5. Use Performance Crises as a Catalyst for Change

Rather than waiting for a financial crisis to force a shift in mindset, family firms should proactively explore strategic opportunities before reaching a breaking point.

### IMPACT

By integrating socioemotional wealth considerations with cognitive perspectives, this research provides valuable insights into how family firms navigate strategic risks. Understanding these dynamics can help family businesses **develop governance structures** that encourage balanced decision-making, ensuring that neither excessive conservatism nor reckless risk-taking

dominates. Advisors and family business consultants can use these insights to guide business families in **crafting adaptive strategies** that respect tradition while embracing necessary change.

### RECOMMENDATIONS

1. Family businesses should foster an adaptive culture by integrating both stability and flexibility in their decision-making.
2. Governance structures should encourage strategic discussions on risk-taking across generations.
3. Education programs for family business leaders should focus on understanding cognitive biases and decision-making tendencies.

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