Spotlight by CeFEO

What drives family firms to invest in young ventures?

External Corporate Venturing in Family Firms: Understanding the Role of Financial Slack and Risk-Taking

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INTRODUCTION

Family firms often exhibit risk-averse behavior, particularly when it comes to high-stakes investments in external ventures, as these initiatives challenge the family's desire to maintain socioemotional wealth (SEW) — the emotional value associated with family ownership. This study addresses a critical question: What factors might prompt family firms to engage in ECV despite inherent risks? With external corporate venturing, family firms can gain access to new markets and innovate, but this requires balancing their economic goals with nonfinancial priorities.

WHAT WE STUDIED

To understand the proclivity of family firms toward ECV, this research draws on the behavioral agency model, which highlights SEW as a major influence on family decision-making. The study applies a dataset of 12,320 firm-year observations from 2,548 European firms spanning 2011 to 2018. It examines whether organizational contingencies, such as financial slack (resources beyond immediate needs) and prior engagement in high-risk activities, influence family firms' willingness to take part in ECV.

KEY INSIGHTS

1. Family Firms' Risk Aversion and SEW

Family firms tend to prioritize SEW, often avoiding investments that could threaten their control or reputation. This behavior aligns with the behavioral agency model, where the primary reference point is the preservation of nonfinancial values, causing family firms to engage less in ECV compared to nonfamily firms.

2. Financial Slack Mitigates Risk Perception

When family firms have substantial financial slack, they are more inclined toward ECV. The availability of excess resources eases concerns about SEW loss, allowing these firms to explore new ventures without the immediate pressure of economic performance.

3. High Risk-Taking Experiences Encourage ECV

Previous high-risk experiences also positively influence family firms' propensity for ECV. Such ventures may normalize risk, leading family firms to adapt to uncertain investment landscapes and reduce the anticipated SEW loss.

TAKEAWAYS

1. Recognize SEW's Role in Family Firms' Investment Decisions

Family business owners and managers should consider the impact of SEW preservation on their risk attitudes. Awareness of SEW's influence could help family firms navigate the emotional and strategic aspects of venturing investments.

2. Leverage Financial Slack Wisely

Family firms with substantial financial resources should view these as opportunities to diversify and grow through external corporate venturing. Resource abundance reduces SEW-related fears, creating a more flexible approach to innovation.

3. Cultivate a Risk-Tolerant Culture

For family businesses accustomed to high-risk decisions, the accumulated experience may ease entry into new ventures. Leaders can foster a risk-aware

environment that mitigates SEW concerns, especially when past experiences have shown resilience in risky endeavors.

IMPACT

This study highlights that while family firms are typically more conservative in their investment choices, favorable organizational contexts—like financial slack and past risk-taking—can change this attitude. As family firms encounter increasingly dynamic and complex markets, the findings encourage family business leaders to reassess their reference points under specific conditions that support ECV engagement.

RECOMMENDATIONS

Family business advisors should emphasize the importance of monitoring organizational contingencies like financial slack and risk history. Encouraging family firms to develop a strategic approach to ECV under favorable conditions may lead to sustained growth and innovation.

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