FAMILY FIRMS AND INNOVATION: THE ROLE OF VENTURED START-UPS

Lai, Alessandro[1]; Panfilo, Silvia[2]; Stacchezzini, Riccardo[3]

[1]Dept. of Business Administration, University of Verona, Verona, Italy

[2]Dept. of Management, University of Ca' Foscari, Venice, Italy

[3] Dept. of Business Administration, University of Verona, Verona, Italy

ABSTRACT

Technological innovation can be defined as the set of activities through which a firm conceives, designs, manufactures, and introduces a new product, technology, system or technique (Freeman, 1976). It can take place according to different strategies: through internal R&D and by mean of external knowledge acquisition (Cassiman and Veugelers, 2006).

Extant studies are predominantly focused on the analysis of the "internal perspective", while there is a research gap on how firms can reach technological innovation by mean of venture capital initiatives (Dushnitsky and Lenox, 2005).

The present paper aims to fill this gap by focusing on how family small and medium entities (SMEs) may develop technological innovations by creating ventured start-ups. In other words by focusing on how the open innovation in SMEs stream of literature (Chesbrough, 2003; Van de Vrande *et al.*, 2009; Lee *et al.*, 2010) is applied by the peculiar category of family firms through equity investments in start-ups. In particular, considering the previous studies which identified the family firms' peculiar characteristics in terms of processes like corporate governance (Randoy and Goel, 2003), internationalization (Zahra, 2003), entrepreneurship (Naldi *et al.*, 2007) and financing (Romano *et al.*, 2001), the research investigates how the family firm's ownership structure affects its technological innovation activities and outcomes (Hoskisson *et al*., 2002).

The research draws on the concepts of exploration and exploitation developed by March (1991): exploration is *"experimentation with new alternatives having returns that are uncertain, distant and often negative"*, while exploitation is the *"refinement and extension of existing competencies, technologies and paradigms exhibiting returns that are positive, proximate and predictable"*. These concepts are central for technological innovation (Atuahene-Gima, 2005): Yalcinkaya *et al.* (2007) found that exploitation is negatively associated with the degree of innovation, while exploration is positively influences the degree of innovation.

The research question of the paper is as follows: how can family SMEs manage the innovation processes by balancing exploration and exploitation?

To answer to this research question, the paper considers the extant research on entrepreneurship and venture capital initiatives and verifies how, in a family business context, these initiatives bringing into

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the governance structure directors and managers with high technological skills favor the overall technological innovation of the company.

The research is based on a case study analysis developed through semi-structured interviews to the managers of the start-up and to the family entrepreneur who invested in the start-up. To better understand the case, the analysis is based also on non-participative observations about the production processes in the start-up and in the family business: we investigate interactions among managers in their decision-making about technological innovations.

The company on which the case study is developed is a 4th generation Italian medium enterprise in the textile sector. This company has an equity investment in a start-up aiming to produce new technological products and participates to "AdottUp", the project that Confindustria (i.e. the General Confederation of Italian Industry) is developing to support SMEs in the process of "adopting" a start-up.

The paper contributes to emerging management literature on technological innovation developed by family firms (De Massis *et al.*, 2012) by showing that a family firm – as a center of exploitation activities – through an equity investment in a startup – playing as the headquarter of innovation activities – can reach an equilibrium creating innovations while maintaining traditions. In this respect we extend the exploration-exploitation framework developed by March (1991) analyzing the under-investigated interaction among governance and technology. The research has also practical implications as it offers empirical insights to entrepreneurs that aim to innovate without compromising core values and sustainability of their firms. Nevertheless analyzing a single case study of a medium size family business adopting this innovation can be considered a limitation. Previous research has indeed shown that there is a great deal of difference in the innovation strategies of small and larger firms (e.g. Acs and Audretsch, 1990) .

Keywords*: innovation, start-ups, family business, SMEs, case study*

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