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in memory of Alberto Falck

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"THE IMPACT OF LEADERSHIP CHANGE ON FOREIGN DIRECT INVESTMENTS IN FAMILY BUSINESSES"

Tesi di Laurea di **Marianna Granata**

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This study aims at linking empirically, for the first time in the literature to our knowledge, two phenomena recognized as the most crucial phases experienced by family businesses: leadership change and internationalization.

Leadership change is defined in this research as a succession of the firm's leader, who can be identified as the Chief Executive Officer, the Chairman of the Board of Directors or, in any case, the main decision-maker strongly affecting the company's strategy.

Internationalization is measured by foreign direct investments (FDIs), which are cross-border investments made by a company based in one country into a company operating in another country with the goal of establishing a long lasting interest (10% of the voting power is generally accepted as the threshold for an investment to be considered long lasting). FDIs could be undertaken through greenfield investments – by setting up new plants in the foreign country from scratch –, through brownfield investments – by acquiring an existing foreign enterprise –, or through joint ventures.

This study refers to family businesses as companies in which family members own a significant share of the equity (at least 50% in private firms and at least 25% in public firms) and are therefore able to influence key strategic decisions.

We argue that a change in the family firm's leader is a catalyst for FDIs and we aim at demonstrating it with an empirical analysis. Indeed, the change of leadership has been theoretically identified as one of those critical incidents that can trigger a quick process of internationalization in family businesses, but no study to our knowledge has tested such

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relationship empirically. Moreover, we explore further factors, intervening during the leadership change, which support FDIs.

Particularly, we investigate three research questions: *1) Does a leadership change play a major role in fostering the internationalization of family firms by boosting FDIs?, 2) Do some key factors – the involvement of non-family members in the board of directors, the leader age, the family second generation – influence FDIs?, and 3) Does a change to a non-family versus a family leader have a stronger impact on the growth of FDIs?*

Building on extant family business literature, we predict the following hypotheses:

1) *Family firms experiencing a leadership change will face a higher increase in FDIs compared to those not experiencing it.* Indeed, a change in the company's leader can be an opportunity for strategic renewal that reverberates on a key strategic dimension such as international expansion.

2) *Family firms with Board of Directors involving non-family members at the time of the leadership change will face a higher increase in FDIs.* In fact, non-family members in the Board of Directors can mitigate the weaknesses arising from family dominance and bring substantial managerial resources, thus supporting the internationalization efforts.

3) *Family firms choosing a younger leader will face a higher increase in FDIs compared to those choosing an older leader.* This is due to the consideration that, generally, the younger the leader the stronger the entrepreneurial behavior.

4) *Family firms in their second generation will face a higher increase in FDIs compared to firms in other generational stages.* In fact, the second family generation is generally considered the most likely to revitalize the company's strategy and boost its internationalization process.

5) *Family firms changing to a non-family leader will experience a higher increase in FDIs compared to those changing to a family one.* Indeed, non-family members

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are considered better prepared to manage the complexities derived from internationalization and more willing to implement the related strong structural changes.

We collect data thanks to Bocconi University's Italian Observatory of Family Firms, which monitors the whole population of Italian Family Businesses with turnover over 50 million euro. We use a sample of 1242 Italian family businesses and we analyze the effect of a leadership change taking place between 2008 and 2011 on the increase in the number of FDIs between 2007 and 2012. The increase in the number of FDIs (the response variable of our analysis) is a count variable that follows a Poisson Distribution, therefore we test our hypotheses by performing negative binomial regressions.

The results of the study prove empirical evidence that: *1) A leadership change is a trigger of FDIs, 2) The involvement of non-family members in the BoD positively affects FDIs, and 3) A change to a non-family leader versus a family one is more likely to enhance FDIs.*

On the other hand, our hypotheses concerning the impact of leader age and family generation do not find statistical support.

To understand why leader age is not a predictor of FDIs, we can consider that the positive effects of younger age – such as higher innovation, higher speed, higher reactivity to environmental changes, higher propensity to entrepreneurial risks – could not be able to outweigh the advantages of older age – such as higher experience and expertise, higher power, higher influence, higher reputation, higher motivation to develop the business for the upcoming new generation.

As for the family generation, we have to keep in mind that the transition to the second generation represents a critical momentum because it corresponds to the leadership change between the generation founding the business and the generation inheriting it. Therefore, it is reasonable to assume that the second generation family members could not

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be ready to undertake such a complex move such as FDIs in the immediate years after the leadership change.

In conclusion, we prove empirically that leadership change can boost FDIs, by rejuvenating the family firms' strategic approach and cultural identity and providing new resources to support the internationalization process. This implies that succession in family businesses is not only a difficult barrier to face, but it could actually be a driver for the company to grow internationally.

Moreover, we demonstrate that non-family members are major contributors to family business internationalization: indeed, both involving non-family members in the Board of Directors at the time of the leadership change and appointing a non-family successor as the firm's leader are proved to foster FDIs.

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