



MANNHEIM BUSINESS RESEARCH INSIGHTS

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The Family Successor– Firm Performance Relationship

Is a family CEO successor a blessing or a curse?

Family affiliation may be an advantage for a CEO successor, but it is not the only decisive factor for success. Close family relationships can only marginally counterbalance deficits in other CEO attributes.

Family-owned companies represent the vast majority of firms on this planet. They are typically managed over the course of generations, building a social capital of vivid culture and mutual commitment. However, all family-owned companies have to face the topic of succession management one day. They usually aspire intergenerational continuity in leadership and values, which they hope to achieve via installing successors, coming from their own family, to manage the firm.

At the same time, and quite paradoxically, extant management research has frequently and very convincingly documented that choosing a family successor has detrimental effects on firm performance. There is evidence that firms controlled by family successors perform worse in the post-succession phase when compared to firms led by nonfamily successors. However, this finding is again in mismatch with the general literature outside the succession context which attests a positive effect on performance based on family involvement. Clearly, in a puzzling way, these research results do not seem to match.

Assistant Professor of Management Jan-Philipp Ahrens knows about the utmost importance of empirical evidence on the question of whom to choose best as next CEO. He and his co-authors felt that this is not yet the whole story and that there might be more to discover that could help to explain this “enigmatic contradiction” in the literature. How much reliance can be placed on the statement, that family CEO involvement is detrimental to post-succession firm performance? Or have prior empirical studies partially failed to disentangle this phenomenon by confusing the family affiliation of the CEO with other, distinct CEO attributes? To find out, the authors

have put together and examined a unique data set on CEO successions and analyzed 804 CEO successions in nonpublic medium-sized family firms.

Unraveling “family member attributes” from “CEO attributes”

The researchers re-conceptualize CEO succession in family businesses, making the family successor in his/her social constellation and the reciprocal human interactions that constitute this group the focal unit of investigation. Building on social exchange theory and its core ideas of generalized exchange, the norm of reciprocity, as well as extended credit, they create a novel theorem that considers the “family member attribute”. The authors of the study define it as the successor’s affiliation with a family that allows extended access to and the maintenance of family-specific social capital, knowledge, values, and identity while facilitating the intergenerational sustainability of the family firm.

In a second step, Ahrens and his research fellows theorize that successor selection in family-owned firms is different from natural (first best) selection - which affects the other CEO attributes of the selected successor in a systematic manner. Consequently, they implement an empirical conceptualization that separates the family attribute’s performance relation from important distinct CEO attributes affected by altered selection and identified by extant research as drivers of firm performance.

Finally, the authors theorize about the sources of the superiority of the family firm successor. In their eyes, a

“family member attribute” enables the intergenerational transfer of social capital due to the interplay of the norm of reciprocity and the mechanism of “extended credit” that results from generalized exchanges. For instance, if general exchanges of the prior generation have built up a stock of positive social capital with key stakeholders, for instance employees, then due to the extension of credit, members of the family will enjoy this endowment the moment they walk into the firm. This happens because parts of the social capital are transferred to group members, in this case the successor. In the same vein, prior social exchange inside the family allows the family successor to nurture and maintain this transferred social capital in superior ways. For example, in many ways they will know implicit norms and key stakeholders’ expectations. Those two theoretical mechanisms then foster new generalized exchange in the post succession phase that enables superior information flow and enhanced support of the successor while facilitating the transfer of key knowledge. As non-family successors do not have access to these unique mechanisms due to their non-affiliation with the social group, this results in a competitive advantage of being a family successor in a family firm.



The family successor is not necessarily the ideal CEO for the firm

In the end, the team of researchers finds considerable evidence for their theoretical argument. The findings high-

light that a family member attribute is primarily something positive: it is vital for post-succession performance. However, a family affiliation must not be elevated or overestimated: its positive effect is easily overtrumped by other CEO attributes of greater importance, e.g., the findings show that choosing a family heir without CEO-related human capital will result in severe performance declines. Vice versa, the family member attribute’s positive effect can be seen as a small buffer that allows the toleration of marginal deficits in other CEO attributes. If the family pursues family-centered noneconomic goals beyond this buffer by accepting even more deficits of the successor CEO, a trade-off between economic and family goals begins. Indeed, sometimes in family firms economic goals are trumped by family goals, especially in the case of succession.

The work thus strongly emphasizes the necessity of a thoughtful choice of successors. It is important to note that successors do not inherit talent as reliably as property and control rights. The children of gifted founder CEOs are not automatically the next great CEOs. Furthermore, it is not enough to have a family successor. The goal must be to nurture a family successor who is capable of withstanding and winning a succession contest against internal and external competitors.

Ahrens, J.-P., Calabrò, A., Huybrechts, J. und Woywode, M. (2019). *The enigma of the family successor-firm performance relationship: A methodological reflection and reconciliation attempt. Entrepreneurship, Theory and Practice: ET&P*, 43, 437-474.

About Jan-Philipp Ahrens

Jan-Philipp Ahrens is Assistant Professor at the University of Mannheim, Business School, since 2016, from where he also holds a doctoral degree, earned in 2013. He was a visiting scholar at Humboldt University of Berlin and Ludwig Maximilian University of Munich. Jan-Philipp Ahrens serves as reviewer for numerous internationally renowned academic journals. His research on CEOs, human decision, strategy, digitization and family firms has appeared in several A-ranked scientific outlets, was awarded or nominated for awards more than fifteen times, and is regularly featured in public media,

such as Deutschlandfunk, Spiegel Online or Frankfurter Allgemeine Zeitung.

Jan-Philipp Ahrens spent two years abroad at Haileybury Imperial College (Great Britain) and at the Chinese University of Hong-Kong. Furthermore, he gained practical experience as Political Advisor at the German Federal Ministry of Finance in 2013 and 2014 and is practically experienced in family firm leadership and restructuring. He is passionate about teaching Strategic Management, Entrepreneurship, and Family Firm Leadership at B.Sc., M.Sc., Ph.D., and Executive Level.



Photo: Xenia Münsterkötter

Making a First Impression as a Start-Up

Strategies for a successful digital innovation launch

Digital innovations by start-ups need to overcome low initial trust perceptions for their survival. High quality customer ratings, a comprehensive benefit communication, and a revenue model considering privacy concerns are key.

As digitalization continues to advance, consumers increasingly have access to digital innovations – many of them developed by start-ups. Consumers' first perception of these digital innovations and their confidence in the trustworthiness of the start-up gain increasing importance. Innovation is generally subject to uncertainty, and this uncertainty is even greater for a service of a digital nature. More than 90 percent of start-ups that develop digital innovations fail. In practice, this means that start-ups seldom get a second chance and that it is essential to gain the trust of consumers at initial touchpoints.

There is no second chance to make a first impression

Assistant professor Elisa Konya-Baumbach, Professor Sabine Kuester, and a team of fellow Marketing researchers have recognized the significance of the "first impression" for digital innovation start-ups. They conducted five consumer experiments explaining how start-ups can indicate trustworthiness and increase initial trust in order to boost consumer adoption. Their study aims to close an important research gap, as little is known about whether and how business model design strategies can help to improve consumers' initial trust in digital innovations from start-ups. The group of researchers finds three specific design strategies for business models to be effective to overcome low initial trust perceptions and to increase adoption of digital innova-

tions. Accordingly, they have three recommendations that digital innovation start-ups should put into practice.

Three practical advices to increase initial trust

First, the study by Konya-Baumbach and her fellow researchers points out the meaning of customer ratings. The results show that positive customer ratings have a significant impact on the initial trust perception and adoption intention of customers – regardless of their total amount. Hence, quality beats quantity: Start-ups should definitely highlight and indicate some positive customer ratings on their website, in app stores, or press releases, rather than investing money to achieve a high number of positive reviews.

Second, when communicating the benefits of their digital innovations, start-ups should bear in mind that some benefits are more helpful than others in increasing initial trust while other benefits are more effective in boosting adoption intention. Start-ups should carefully tailor the communication of benefits to the target audience, depending on their primary goal: encouraging adoption intentions via increased initial trust perceptions or directly. Since start-ups mostly depend on both directly boosting short-term adoption to reach a critical mass of consumers and establishing a sustainable high adoption rate via overcoming low initial trust in the long-term, they might consider communicating both benefits at the same time. As an example, an insurance

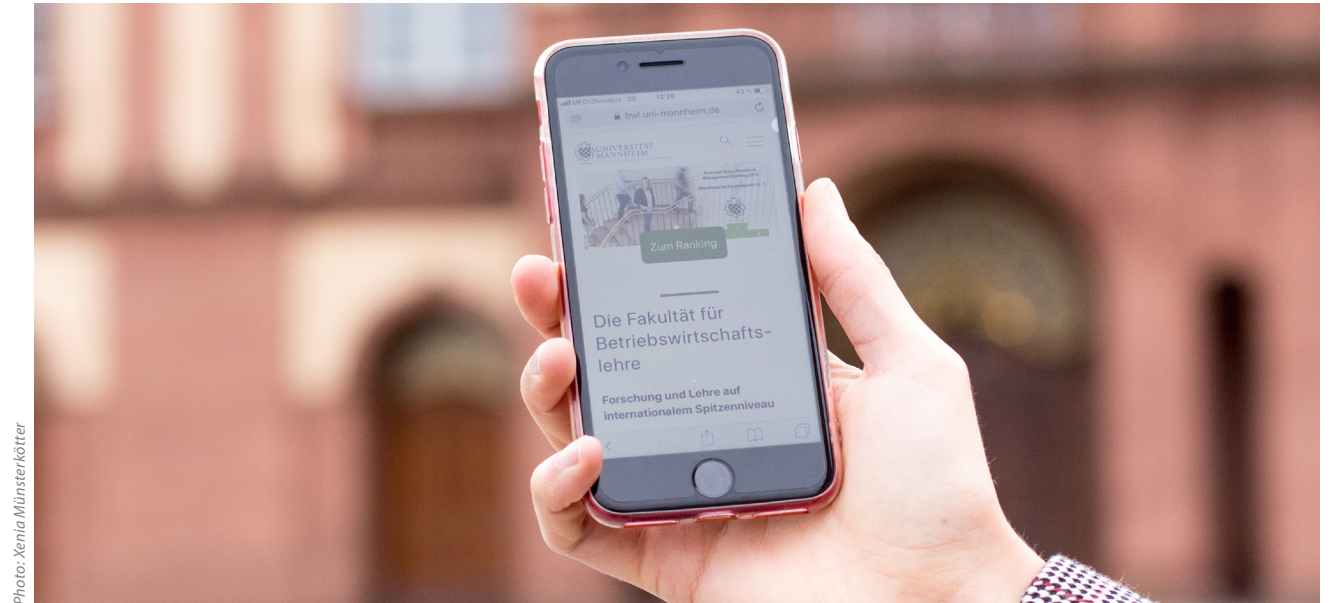
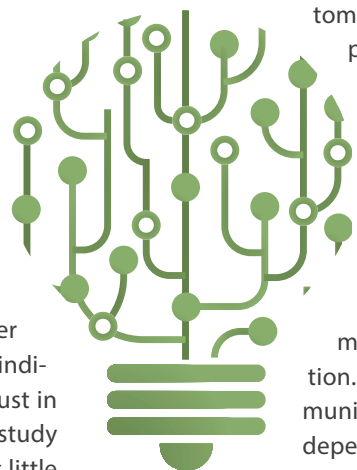


Photo: Xenia Münsterkötter

could promote both original benefits, such as personal service, and digital benefits, such as transparency.

Third, when deciding on a revenue model for their digital innovations, start-ups should be aware that selling their users' data to third parties can permanently damage their trustworthiness. For example, if start-ups consider offering a "free" service option in the realm of a databased revenue model to attract consumers and encourage them to switch to a paid service option, the "free" service option can potentially backfire. By charging a monetary price for their service rather than using consumer data, there will be less privacy concerns with regard to the digital innovation by the start-up. Fewer privacy concerns imply higher initial trust perceptions, which drive digital innovation

adoption rates as compared to charging a "data price". Thus, start-ups should aim to follow a monetary revenue model and, more importantly, should clearly state that they refrain from private data collection and use if the creation of initial trust is the main objective of the start-up. In this case, start-ups should even use their strong privacy policy as a unique selling proposition in their marketing communications, as some successful companies already do in practice.

Konya-Baumbach, E., Schuhmacher, M. C., Kuester, S. und Kuharev, V. (2019). Making a first impression as a start-up: Strategies to overcome low initial trust perceptions in digital innovation adoption. *International Journal of Research in Marketing: IJRM*, 36, 386-400.

About Elisa Konya-Baumbach

Since May 2016, Elisa Konya-Baumbach is an Assistant Professor at Professor Kuester's chair of Marketing & Innovation. She was a visiting scholar at the S. C. Johnson School of Management at Cornell University, USA, in 2017 and at Stern School of Business at New York University, USA, in 2014.

Elisa Konya-Baumbach's research focuses on consumer psychology and behavior

as well as marketing and adoption of digital innovations. She is particularly interested in consumer decision making and innovation adoption. For her dissertation project examining the launch of e-innovations, she won prizes by the Marketing Foundation of the University of Mannheim as well as by the employers' association Suedwestmetall.



Photo: Xenia Münsterkötter

Relating Product Prices to Long-Run Marginal Cost

Evidence from solar photovoltaic modules

To forecast future product prices, it is essential to understand long-run marginal costs and potential changes in cost. An innovative procedure for estimating long-run marginal cost has recently been implemented for the solar photovoltaic industry.

The solar photovoltaic (PV) module industry has experienced unprecedented price declines and rapid output growth in recent years. The corresponding price trajectory has widely been thought to be a learning curve with an 80 percent constant elasticity. Accordingly, prices would fall by 20% every time the cumulative capacity, measured in megawatts (MW), doubles.

Yet, the empirical findings of a study by Stefan Reichelstein, head of the Mannheim Institute for Sustainable Energy Studies (MISES), and his co-author Anshuman Sahoo of the Stanford Graduate School of Business, point to a rate of cost reductions that is faster than suggested by the 80 percent learning curve. In order to estimate the learning curve for solar modules, the authors of the study propose and implement a method for estimating long-term marginal costs based on data obtained from financial statements at the firm-level. Economic theory predicts that in equilibrium competition drives the price of a product to the long-term marginal cost of the product. However, the proper measure of marginal costs is still a matter of considerable debate. The conceptual framework developed in the paper provides a new method for quantifying long-run marginal costs. Such a framework allows the authors to compare a trajectory of cost estimates to actually observed sales prices. The resulting differences are a measure of the extent of disequilibrium in the market at different points in time.

Understanding the dramatic sales prices decline

When applied to the solar PV industry, Reichelstein and Sahoo find a close match between average sales prices and long-run marginal cost for the years 2008-2010. However, from the end of 2011, they conclude that the dramatic decline in the observed sales prices in most of the quarters in 2012-2013 is not compatible with the industry having been in equilibrium. They conclude that the decrease in sales prices for these time periods should be attributed to excessive production capacity rather than to intrinsic cost reductions. The study identifies not only a steeper learning curve than previously estimated, but also derives an estimate for the learning curve that corresponds to core production costs. The latter may be influenced by several factors, including temporary excess capacity. Previous studies on learning curves, in contrast, have sought to infer production costs from observed prices, assuming that the industry is in an equilibrium such that firms will charge normal markups on their production costs.

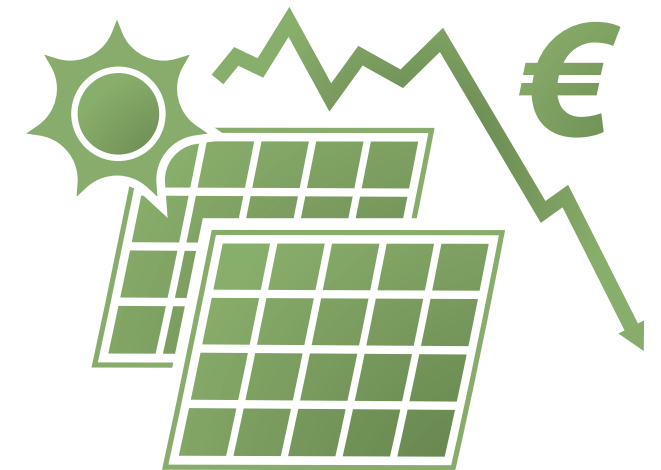
The study by Reichelstein and Sahoo provides a generic model framework for determining long-term marginal cost in a dynamic model of a competitive industry where firms make sequential and overlapping capacity investments and subsequently select their periodic production levels in a competitive manner. The authors then identify a procedure for estimating the long-run marginal cost of a product, based mainly on firm-level financial data.

The resulting insights are of direct interests to managers and investors in the solar photovoltaic industry as well as those in other renewable energy industries. In addition, the findings of the study are of interest to governments, including those of Germany and the U.S., which have set cost targets for solar photovoltaic modules and established different policy mechanisms for further supporting this technology.

A reliable forecast of the trajectory of future cost

The methods and findings of this paper have several policy implications. First, the pricing of solar PV modules, in particular from Chinese suppliers, has been legally contested in recent years. The complaint of “dumping” of modules is similar to predatory pricing in domestic price disputes and generally refers to pricing below cost. The study shows that prices in the 2011-2013 window were frequently below the long-run marginal costs at that time. Yet, the long-run marginal cost includes several components that are likely to be considered “sunk” in the short-run. If the relevant cost benchmark in legal disputes is the short-term average variable cost, the measure of core manufacturing costs would provide an upper bound. The study concludes that the firms in the sample have at no point in time charged prices below their core manufacturing costs.

Second, demand for solar PV modules has in the past decade been driven in significant part by public policy support in the form of feed-in-tariffs, investment tax credits and renewable energy portfolio standards. As solar system prices have dropped rapidly in recent years, governments in many countries have reduced these subsidies.



One of the key questions in the ongoing debate is the magnitude of tax credits and/or feed-in tariffs required to sustain the deployment of solar PV. The debate about these subsidies must be informed by predictions about the continuation of the recently observed cost reductions. The present study can inform regulators on this question.

Finally, the study provides broader insights about the long-term positioning of renewable energy. The results show that prices will continue to fall as the use of solar PV modules increases, which in turn provides an incentive for increased use and thus for further price declines. Considering that solar PV is still in the relatively early stages of large-scale global deployment, the study suggests continued benefits from this reinforcing cycle in the long-run.

Reichelstein, S. und Sahoo, A. (2018). Relating product prices to long-run marginal cost: Evidence from solar photovoltaic modules. Contemporary Accounting Research, 35, 1464-1498.

About Stefan Reichelstein

Prof. Stefan J. Reichelstein holds an endowed chair in business administration at the University of Mannheim. During the past 30 years he held positions at several leading international universities, including Berkeley and Stanford. In light of his research accomplishments, he received honorary doctorates from the University of Mannheim in Germany and the University of Fribourg in Switzerland, as well as honorary professorships from

the University of Vienna and the Technical University of Munich. At the University of Mannheim, Prof. Reichelstein has been tasked with building up the Mannheim Institute for Sustainable Energy Studies (MISES). This new institute addresses economic aspects of the transition to a decarbonized energy economy, with a particular focus on timeliness and cost effectiveness.



Photo: Felix Zeiffer



IMPRINT

Publisher:
University of Mannheim
Business School
L 5, 5
68131 Mannheim
www.bwl.uni-mannheim.de

Responsible
Professor Dr. Stefan Ruenzi

Concept/Editing
Dr. Liane Weitert

Design
Keren Deng



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