Article

Retrenchment Strategies and Family Involvement: The Role of Survival Risk

Family Business Review
1–18

DOI: 10.1177/0894486518794605
journals.sagepub.com/home/fbr
SAGE

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Abstract

This article analyzes retrenchment strategies that family businesses adopt during periods of crisis. From a socioemotional wealth perspective, we propose that the influence of family board members and family CEOs on retrenchment depends on survival risk. We collected empirical data from companies on the Spanish Stock Exchange (2008-2012). Our findings reveal that family involvement intensifies retrenchment when performance is declining, and that retrenchment intensifies when survival is at risk. We also demonstrate that family firms are able to implement retrenchment measures when required to improve their performance.

Keywords

retrenchment strategy, SEW, family director, family CEO

Introduction

In the wake of the recent global crisis, there has been a marked worldwide increase in the frequency of credit bid processes and company closures. Failure is a significant phenomenon, particularly in hostile environments or in the event of economic and financial crises (Dowel, Shackell, & Stuart, 2011; Mellahi & Wilkinson, 2004). Business failure has a proclivity to be preceded by a phase of decline, during which firms lose their competitive advantage as a result of both external factors—economic recession, technical obsolescence, production inefficiencies, and so on—and internal factors—insufficient management skills, internal conflict, inflexible organizational structures, and so on (Pearce & Robbins, 2008). Previous research has attempted to explicate the development of the processes that restructure or change a firm's direction, using terminology such as *turnaround strategies* (Barker & Duhaime, 1997; Hambrick & Schecter, 1983; Pearce & Robbins, 2008) or *corporate restructuring* (McKinley & Scherer, 2000). These processes are implemented through a series of measures designed to reverse this trend so that the firm is able, after a period of time, to guarantee its survival while regaining and maintaining positive outcomes (Robbins & Pearce, 1992).

There is general consensus that there are two key phases in these processes (Pearce & Robbins, 1993, 1994): (a) the retrenchment phase and (b) the recovery phase. The first phase involves the adoption of measures in numerous internal areas of the firm, such as controlling cash flow by reducing current expenditure, principally in relation to employees (Hambrick & Schecter, 1983; Robbins & Pearce, 1992). It also involves rationalizing product lines through divestment procedures and replacing members of the governing bodies (e.g., the management team, board of directors, etc.). The second phase involves reorienting the firm to pursue enhanced long-term performance. This often requires a new entrepreneurial aptitude to be developed in order to empower the company to sustain its strategy in this new context (Pearce & Robbins, 1994; Revilla, Pérez-Luño, & Nieto, 2016).

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Retrenchment is a critical phase in a restructuring strategy when difficult decisions must be taken and implemented. Robbins and Pearce (1992) stated, "The most expeditious road to turnaround strategy begins with a sustained retrenchment response" (p. 304). Furthermore, the way in which the retrenchment phase is developed plays a critically important role in determining the probability of successful turnaround (Pearce & Robbins, 1993). Previous research has indicated that firm ownership structure influences the development of turnaround and retrenchment strategies, principally through corporate governance (Daily & Dalton, 1994; Elloumi & Gueyie, 2001). More specifically, research has proposed that family ownership has an impact on the firm's turnaround strategies and potential exit strategy (DeTienne & Chirico, 2013). For example, Cater and Schwab (2008) applied an inductive approach to their research into some of the family characteristics that explain turnaround strategies in established small family businesses. They found that the implementation of retrenchment strategies in family businesses is moderated by eight variables: strong ties to the family business, replacement candidates, consensus orientation, informal management systems, internal orientation, integration of nonfamily employment, altruistic motives, and long-term goal orientation. Corbetta and Salvato (2012) posited that the more family members who are involved in family firms (the *cousin consortium*), the more likely the firm is to pursue exit strategies in terms of sale or asset liquidation. They argue that this is due to a phenomenon to which the authors refer as *generational drift*—a progressive decay of family members' affective commitment to the firm. DeTienne and Chirico (2013) therefore proposed that in later generations, when socioemotional wealth (SEW) has dissipated (Gómez-Mejía, Haynes, Nuñez-Nickel, Jacobson, & Moyano-Fuentes, 2007) and the performance threshold is elevated (Gimeno, Folta, Cooper, & Woo, 1997), a more dispersed ownership structure is associated with a greater likelihood of a cessation-based exit strategy. However, with a very limited number of exceptions (see Cater & Schwab, 2008), there has been a dearth of empirical research into family firms' development of retrenchment strategies as a reaction to declining performance and as a means to circumvent failure and exit.

Wennberg and DeTienne (2014) identified two specific aspects of retrenchment strategies in family businesses that warrant further research investigation. First, family businesses consider not only the financial implications but also SEW in their decision-making processes (Gómez-Mejía, Nuñez-Nickel, & Gutierrez, 2001) based on their proximity to failure and the potential loss of SEW. Second, there are specific and idiosyncratic characteristics of the governance structures of family businesses that affect their management processes (Watkins-Fassler, Fernández-Pérez, & Rodríguez-Ariza, 2016). This articel focuses on retrenchment strategies in family businesses, following the line of research that started with DeTienne and Chirico (2013). These authors suggested that SEW influences exit strategies in family firms through their performance threshold: "the level of performance below which controlling organizational constituents will act to dissolve the firm" (Revilla et al., 2016, p. 367). Our research proceeds on the assumption that the family firm has elected not to exit, and the question therefore is how to instigate a turnaround using a retrenchment strategy. Certain characteristics of family businesses may affect how they address declining performance and execute retrenchment strategies in their attempts to avoid an exit. Although declining performance may damage SEW in family businesses, retrenchment strategies can also have a negative impact, whereby inadequate management by family decision makers is apparent and the reputation and social capital of the family and its business systems are eroded. Our article proposes that this response to declining performance will differ according to whether or not the firm's survival is at risk. We argue that when survival is not in jeopardy, family involvement will entail a lower level of retrenchment to avoid damage to family social ties and family reputation. However, when the decline is strong enough to threaten a firm's survival, family involvement will intensify the retrenchment strategy in order to safeguard SEW (Gómez-Mejía et al., 2007). Our articel perceives declining performance and survival risk as different concepts. While they are correlated in the long term, there are a number of reasons why they are not necessarily correlated in the short term, including financial structure, ownership structure, and financial costs (Bruton, Ahlstrom, & Wan, 2003).

In this article, we therefore address the following research question: In the context of a crisis and confronted with a deterioration in performance, how does family involvement influence the intensity of retrenchment strategies? We investigate the role of family decision makers in the retrenchment strategy with

consideration of the family's involvement on the board of directors and the role of a family CEO. In doing so, we identify two distinct mechanisms that potentially moderate how family firms address their retrenchment strategies, depending on whether or not firm survival is in danger (Gómez-Mejía et al., 2007; Gómez-Mejía, Makri, & Kintana, 2010). The core objective of our article, therefore, is to augment current understandings of retrenchment strategies in family businesses in the context of a period of crisis.

This study aims to make the following contributions: First, we aim to facilitate the advancement of different theoretical frameworks by enriching current academic debates relating to the retrenchment literature, corporate governance, and the SEW perspective. We will advance the literature on retrenchment by including aspects that are not necessarily rational or financial (e.g., SEW) while providing the literature on family firms with examples of explicit risk as a context for decision-making processes. Second, based on SEW perspectives, we make proposals relating to how family members' involvement on boards affects turnaround strategies that are intended to avoid the potential risk of exit. Third, we propose that, in the case of family businesses, these dangers to firm survival exert a moderating effect on the intrinsic relationship between diminishing performance and turnaround strategies. Our research clearly demonstrates how a threat to survival determines the way in which a family firm responds to declining performance, and considers that performance deterioration and survival risk are not inevitably associated in the short term, thus supporting our proposals from the SEW perspective. Our findings indicate that survival risk changes the context in which family businesses make decisions when confronted with declining performance.

Theoretical Background

Existing theories have provided some insights into how family firms manage a decline in performance and potential failure. As Revilla et al. (2016) suggested, failure and exit in family businesses depend not only on financial performance but also on noneconomic objectives. The SEW perspective accentuates the importance of emotions, social capital, and noneconomic goals, especially when survival is threatened by declining performance (Chrisman & Patel, 2012; Kammerlander, 2016). Gómez-Mejía et al. (2007) applied the term *socioemotional wealth* to nonfinancial facets of the firm that meet the family's affective requirements, such as identity, the ability to exercise family influence, and the perpetuation of the family dynasty (p. 106). Conversely, Berrone, Cruz, and Gómez-Mejía (2012) conceptualized SEW as the stock of affect-related value that a family derives from its governing position in a particular firm. Wilson, Wright, and Scholes (2013) maintained that family firm ownership is significantly associated with firm survival, which suggests that through the board, the family contributes different types of resources to support the firm's survival. Haynes, Walker, Rowe, and Hong (1999) contended that family firms have the capacity to share resources between the family and the business in order to certify the firm's long-term existence. A number of studies also state that owner-managers with substantial emotional attachments to their business evade the prospect of their resources transmogrifying out of the family's control, even when an exit would represent the most advantageous option from an economic standpoint (Dehlen, Zellweger, Kammerlander, & Halter, 2014; Gimeno et al., 1997; Zellweger, Kellermanns, Chrisman, & Chua, 2012). The SEW literature assumes that family firms consider the circumvention of a potential loss of SEW as the primary reference point to an exit (Gómez-Mejía et al., 2007). There is an assumption that family businesses possess the aptitude to survive at subordinate performance levels compared with their nonfamily counterparts. Hence, to preserve SEW, family firms undertake less retrenchment (e.g., layoffs) when their survival is anticipated. In other words, family businesses demonstrate a lower performance threshold (the performance below which the organization's controlling constituents will act to dissolve the firm) than nonfamily firms (DeTienne & Chirico, 2013; Gimeno et al., 1997). However, the same objective—safeguarding SEW—motivates family businesses to implement intensive retrenchment when their longevity is under threat.

The SEW perspective has been developed as an extension of behavioral agency theory (Wiseman & Gómez-Mejía, 1998). According to this theory, firms make decisions based on the judgment of the dominant principal, and in family businesses, the point of reference is the preservation of the owning family's SEW (Gómez-Mejía et al., 2007). Accordingly, any danger to SEW indicates that the family is in "loss mode" and will consequently make strategic decisions that will bypass these latent SEW losses (Gómez-Mejía et al., 2010). This perspective facilitates an understanding of how

these businesses respond during periods of decline: Retrenchment processes in family-controlled businesses are oriented toward protecting maximum SEW (i.e., minimizing the loss of SEW).

While family firms do not invariably have the same level of SEW (DeTienne & Chirico, 2013), family-controlled businesses facing a diminution in performance formulate their own context that can simultaneously promote and hinder the acceptance of a retrenchment strategy. First, any risk that affects the firm's survival has special repercussions when the firm is identified with a particular family, given that the failure of the business has an adverse implication on the family's emotions (Shepherd, Wiklund, & Haynie, 2009) and reputation (DeTienne & Cardon, 2012; DeTienne & Chirico, 2013). Second, family-managed businesses have a tendency to trust the management of their board of directors and many implement only low-level monitoring and regulatory mechanisms (Cruz, Gómez-Mejía, & Becerra, 2010). In other words, family decision makers are more preoccupied with the impact of SEW than are those in family firms that are managed by a nonfamily CEO (DeTienne & Chirico, 2013). This essentially releases family board members from their responsibility when performance outcomes are poor (Gómez-Mejía et al., 2001). Consequently, the dimensions of SEW generate a different point of reference for family businesses, giving preference to family owners' value perceptions and organizational behaviour (Zellweger & Dehlen, 2012). Third, when performance is deficient, family-controlled firms have a proclivity to implement nontraumatic measures that will ostensibly affect internal relationships (between family and employees) and external relationships (with clients, local institutions, etc.), which delays the enactment of retrenchment measures (Berrone et al., 2012). Fourth, family firms often have more flexible and centralized management structures, in addition to coherent organizational structures, that enable them to adopt entrepreneurial and reactive measures more efficiently (Salvato & Melin, 2008). Finally, where there are elevated levels of SEW, the firm is much less disposed to select to exit when confronted with poor economic performance, and more disposed to implement more intense retrenchment strategies (DeTienne & Chirico, 2013).

Family firms with high levels of SEW are characterized by their owners' identification with the firm and aspiration to remain in the business over time, progressing from one generation to the next (Gersick, Davis, Hampton, & Lansberg, 1997). Thus, when a firm experiences a deterioration in performance, the family directors and shareholders are inclined to evaluate the extent to which this deterioration poses a genuine risk to the longevity of the family business (Shepherd & Haynie, 2011). Their interpretation will determine whether or not certain retrenchment policies are executed and how quickly and intensively this takes place, bearing in mind that some retrenchment measures could negatively affect SEW (Gómez-Mejía et al., 2001). According to D. Miller and Le Breton-Miller (2005), family firms endeavor to establish a cohort of talented, motivated, and devoted employees working to enhance the firm's performance for its future. It is therefore anticipated that family firms will be less inclined than nonfamily firms to dismiss employees when there is a decrease in performance.

Finally, in their study of stewardship in family-owned businesses, D. Miller, Le Breton-Miller, and Scholnick (2008) proposed a stewardship over customer relationships. This stewardship alludes to the fact that family businesses are "especially pre-occupied with creating customer loyalty – moving from a transactional link with customers towards a broader, more enduring relationship" (D. Miller et al., 2008, p. 56). In this dimension, it is presumed that family firms will be reluctant to roll out retrenchment measures in response to a decline in performance. Retrenchment strategies entail the internal and external recognition of declining performance, deteriorating relationships among family members and employees (D. Miller et al., 2008), and damage caused to external reputation and social capital (Deephouse & Jaskiewicz, 2013; Salvato & Melin, 2008).

Hypotheses Development

There is strong consensus that SEW influences the way that family decision makers take and implement decisions in family firms (Gómez-Mejía et al., 2007), particularly at times of impaired performance (DeTienne & Chirico, 2013). The SEW literature reveals that the influence of SEW is different when the firm's survival is in jeopardy compared to its influence in normal circumstances when the firm's existence is not threatened. Family businesses with higher levels of SEW will avoid any potential risk during periods of good economic outcomes. However, they will be very proactive and take more risky decisions when they are in loss mode; that is, when the firm's survival is threatened (Chrisman &

Patel, 2012). This asymmetrical behavior has been found in relation to a number of strategic decisions, such as diversification (Gómez-Mejía et al., 2010), the adoption of new technologies, research and development (R&D) investment (Chrisman & Patel, 2012), the internationalization process (Arregle, Naldi, Nordqvist, & Hitt, 2012), and closely linked to our research, exit strategies (DeTienne & Chirico, 2013). Following this line of reasoning, we analyze the effect of family members' involvement at the strategic decision level when the family business is confronted with a decline in performance. In this article, we focus on retrenchment strategy, considering exit as an undesirable consequence of poor performance (failure). Our research complements DeTienne and Chirico's (2013) study by focusing on exit strategies in family businesses.

We will consider two different types of family members' involvement in strategic decisions: family involvement on the board of directors and the role of a family CEO. Family involvement on the board of directors has been extensively used to measure the level of overlap between the family and the firm (Revilla et al., 2016). The corporate governance literature considers that family involvement on the board is a means by which it can germinate ownership control through strategic decisions. Schulze, Lubatkin, and Dino (2003) emphasize the importance of the CEO's power in the decision-making process. Recent research into exit strategies in family businesses underscores the role of the CEO (see DeTienne and Chirico, 2013), and the literature clearly suggests that the effect of family management is contingent on who occupies the CEO position (Morck, Shleifer, & Vishny, 1988). When the CEO holds a significant share of the power, the asymmetry of information (Gómez-Mejía et al., 2001) allows them to interpret and justify the decline in performance to the other stakeholders while not disclosing their management failings. In summary, our hypotheses combine the influence of family board membership and the family CEO in two potential contexts: when the firm's survival is threatened, and when it is not.

Retrenchment When Firm Survival Is Not at Risk

The extent of the family's involvement—either by participating on the board or by assuming the role of CEO—is imperative for comprehending how family firms react to a decline in performance (Wilson et al., 2013). The SEW perspective proposes that family businesses maintain strong links with both internal agents (workers, members of the owning family, etc.) and external agents (clients, institutions, professional associations, etc.). Internal links inspire altruistic relationships, trust, and nonopportunistic behaviors (Dehlen et al., 2014; DeTienne, 2010), while external links authenticate the reputation and image of the firm and the family (Deephouse & Jaskiewicz, 2013; D. Miller et al., 2008). These aspects are indicative of three key reasons why the greater involvement of family members on a firm's board of directors or as the CEO diminishes the prospect of traumatic measures that require retrenchment strategies such as cost reductions or divestments.

The first reason lies in how family and nonfamily businesses interpret poor results (Wennberg, Wiklund, DeTienne, & Cardon, 2010). Family members' involvement promotes a sense that they are fulfilling the role of steward (J. H. Davis, Schoorman, & Donaldson, 1997), given their common objectives, collaboration, and nonopportunistic conduct (Chrisman, Chua, Kellermanns, & Chang, 2007). Family involvement bolsters confidence in management (Cruz et al., 2010) and indicates that fewer monitoring and control mechanisms have to be implemented (Cruz et al., 2010; Gómez-Mejía et al., 2001) in comparison to nonfamily businesses or family businesses with low family involvement on the board. In this context, a decline in profits is often attributed to causes external to the firm's management, thereby evading the dismissal of family board members or the family CEO (Gómez-Mejía et al., 2001). Therefore, family directors and the family CEO might exhibit a biased perception of the firm's performance (Zellweger & Dehlen, 2012).

A second reason is the reluctance of family businesses to adopt drastic measures that might affect internal and external relations (Wennberg, Wiklund, Hellerstedt, & Nordqvist, 2011). Such turnaround strategies undermine the trust relationship between family members and nonfamily employees (Le Breton-Miller, Miller, & Lester, 2011; D. Miller et al., 2008) and have negative connotations for how clients and suppliers, local institutions, and so on perceive the firm (Kammerlander, 2016). When performance is in decline, active family members (those involved in the company) might safeguard SEW by concealing negative news and unfavorable data from customers, employees, and other owners in an attempt to protect the firm's reputation (Wennberg et al., 2010). Although

this characteristic is not exclusive to family directors and CEOs, they are more motivated to adopt it than their nonfamily counterparts. This is primarily because active family members are accountable for the preservation of SEW, which affects not only the staff within the firm but also all associated family members (D. Miller et al., 2008). This is contextually significant, as family relationships are more enduring than those of a professional nature. Additionally, the reputation of the family firm affects the entire family, as opposed to merely those involved in the business. This occurs predominantly when there is a link between the firm's name or trademark and the family name (Salvato & Melin, 2008). For example, DeTienne and Chirico (2013) argue that a family CEO has a tendency to meet and satisfy the family's desires, thereby circumventing decisions that might denote a threat to the family's SEW.

The third reason is that deciding on retrenchment strategies requires a problem to be recognized in full view of internal and external stakeholders, which in turn can impair the family firm's social capital and reputation (Berrone et al., 2012; Gómez-Mejía et al., 2007). Retrenchment decisions could be perceived as a signifier of the firm's poor management and failure, with a negative impact on the reputation of the family business, including stigmatization (Ucbasaran, Shepherd, & Lockett, 2013). This impairment is even more consequential when the firm bears the family name, as the reputation of the firm will be transferred to the family itself, as previously stated. The family directors and CEO will operate as defenders of the family's reputation, rebuffing any board decisions that may negatively affect its social capital and emotional legacy (Jaskiewicz, Combs, & Rau, 2015).

In summary, the literature suggests that, with the prospect of declining performance, family firms try to avoid retrenchment strategies because they require the family members involved in the business to acknowledge poor performance, which in turn may impede SEW (reputation, internal and external social capital, etc.).

Hypothesis 1: *When a firm experiences a decline in its performance that does not threaten its survival, the relationship between decline and the intensity of the retrenchment strategy will be moderated by (a) family involvement on the board and (b) the presence of a family CEO. Specifically, when firm survival is not threatened, the relationship between decline and retrenchment strategy will be attenuated by (a) a higher family involvement on the board and (b) a family CEO.*

Retrenchment When Firm Survival Is at Risk

The SEW perspective recognizes that long-term orientation and the firm's aspiration to progress to the next generation is one of the mainstays of family firms (Berrone et al., 2012; D. Miller et al., 2008). These firms often attempt to avoid any facet that threatens their continued survival. Family businesses adopt differentiated points of reference compared to nonfamily firms in respect of performance and prioritize the circumvention of a potential loss of SEW (Gómez-Mejía et al., 2007). Using SEW as a reference point, family businesses place a high value on sustaining family control with respect to accepting poor performance. DeTienne and Chirico (2013) advise that underperforming family firms are inclined to survive predominantly due to motivational aspects (DeTienne, Shepherd, & De Castro, 2008), leading them to accept a lower performance threshold. Exit is "the very last option" for a family business, given its direct effects on SEW. As Shepherd et al. (2009) attest, despite a certain level of financial distress, family businesses will evade or postpone business failure.

Business failure is more than a professional failure for family businesses; it is, to a certain extent, a family failure, which affects its internal and external reputation. Family businesses will thus be hesitant to close the business (Revilla et al., 2016), and when faced with this situation, the family directors and CEO feel obligated to take actions that will save the firm and its legacy (Jaskiewicz et al., 2015; Lumpkin & Brigham, 2011). In such cases, the family's involvement evidently benefits the effectiveness of retrenchment strategies, given its members' altruism (Schulze et al., 2003) and the speed with which decisions can be taken. Only when the decline in performance is so pronounced that it endangers the firm's survival will the CEOs be likely to appreciate that their stewardship role requires them to operationalize retrenchment measures to preserve SEW (Kammerlander, 2016; Zellweger et al., 2012).

The stewardship role of the family CEO carries the responsibility of ensuring the continuity of the firm. When confronted with declining performance, therefore, an authoritative CEO can manage intensive

retrenchment measures when firm existence is threatened, using the leadership position to take difficult decisions. As De Massis, Kotlar, Campopiano, and Cassia (2013) stated, a family CEO may be able to use his or her power and managerial discretion to manage the goal conflicts among family members, whereas non-family CEOs may be more tempted to accommodate some groups of family members at the expense of other groups (p. 174). If retrenchment measures are not integrated, then the family business could be at risk, which would categorically affect SEW. In view of this, we propose the following hypothesis:

> **Hypothesis 2:** *When a firm experiences a decline in its performance that threatens its survival, the relationship between decline and the intensity of the retrenchment strategy will be moderated by (a) family involvement on the board and (b) the presence of a family CEO. Specifically, when firm survival is threatened, the relationship between decline and retrenchment strategy will be intensified by (a) a higher family involvement on the board and (b) a family CEO.*

Methodology

Sample

This empirical study is based on firms listed on the Spanish Stock Exchange during the period from 2008 to 2012. This was a period of one of the world's greatest economic crises, which had a significant and enduring impact in Spain. The country went into recession twice during this period, and the value of its stock market fell by more than 45%. The sample comprises 126 companies that were listed for at least 2 consecutive years during this time frame (109 firms were listed for the duration of the 5-year period, while 15 companies exited and 2 companies entered the stock exchange during this time). Four companies that departed the stock exchange subsequently filed for bankruptcy. The data we gathered from these companies relate to their finances and boards of directors for each of the 5 years of the study. We also collected data from preceding years (2006 and 2007) to calculate the rate of growth/decline of several financial indicators. A total of 599 observations (firm-years) were conducted from an unbalanced panel of 126 firms throughout the 5-year period.

Variables

Dependent Variable. The dependent variable is the intensity of the retrenchment strategy, measured by the decline in firms' assets and costs over 2 consecutive years. Our retrenchment variables were operationalized in line with the measures that are most frequently enacted in retrenchment research (Barker & Mone, 1994; Lim, Celly, Morse, & Rowe, 2013; Morrow, Johnson, & Busenitz, 2004; Robbins & Pearce, 1992). Retrenchment is the deliberate reduction of assets and/or costs as a means of increasing profits (Lim et al., 2013) and is one of the most debated topics in turnaround research, given previous studies' mixed evidence regarding its value (Barker & Mone, 1994; Castrogiovanni & Bruton, 2000; Lim et al., 2013; Pearce & Robbins, 1993). Studies have found two types of retrenchment: cost and asset. Cost retrenchment involves the net reduction of costs, such as those incurred by selling, general, and administrative expenses, R&D, interest payments, salaries, and stock options (Lim et al., 2013; Morrow et al., 2004; Robbins & Pearce, 1992). Asset retrenchment involves the net reduction of assets. Plant closures, equity divestment, and the disposal of property or equipment are a few examples of this type of retrenchment, which tends to be implemented in more extreme situations than cost retrenchment (Pearce & Robbins, 1993).

Asset and cost retrenchment are the two main retrenchment strategies available to a business when performance is waning (Lim et al., 2013; Morrow et al., 2004). Asset retrenchment was calculated as the percentage change in the firm's total assets from one year to the next, and cost retrenchment as the percentage change in the cost of selling, general, and administrative expenses over 2 consecutive years. We did not consider any other cost categories (e.g., R&D costs, inventory, etc.) because this information was not available for the majority of firms in the sample. In our study, we found both measures to be highly correlated (correlation = .853, $p < .001$), and so we standardized both variables to calculate their average, obtaining a single variable, after checking the reliability of the measure (Cronbach's $\alpha = .704$). To assist with the interpretation of the results, we used the inverse indicator so that the greater the value, the greater the retrenchment intensity adopted by the firm.

Independent and Moderator variables. We used four independent and moderator variables:

1. *Decline*: In line with the literature, we consider a firm to be in a state of decline when its economic performance (return on assets) has dropped in 2 consecutive years, reaching a negative level (Barker, Patterson, & Mueller, 2001; Lim et al., 2013). We assigned firms a value of 1 if they were in decline and 0 if they were not.
2. *Survival risk*: Measured using the Altman *Z*-score, which measures a company's risk of bankruptcy (Altman, 1968; Barker et al., 2001). Altman's *Z*-score has been widely used in the retrenchment literature (Barbero, Di Pietro, & Chiang, 2017; Barker & Duhaime, 1997; Bruton et al., 2003; Chen & Hambrick, 2012). The measure is also used in a professional context by banks and investment funds, given its bankruptcy predicting power. The *Z*-score is calculated using five synthetic ratios weighted by fixed coefficients. As the *Z*-score drops below 3, the risk of the firm going bankrupt becomes more apparent. A *Z*-score below 1.8 denotes that the firm faces a considerable risk of bankruptcy in the next 2 years (Altman, 1968). The measure is used in both older and more recent retrenchment studies to control for a firm's level of distress (Barker & Duhaime, 1997; Chen & Hambrick, 2012).
3. *Family board member*: First we considered ownership control, identifying the main owner from information provided in the companies' annual reports and Sabi (a broader version of Amadeus for Spain and Portugal, distributed by Bureau van Dijk, which provides online information on over 850,000 Spanish firms, taken from the annual reports lodged with the Mercantile Registers). Following the proposal of the European Family Business Group and the board of the Family Business Network, we considered a firm to be family-controlled when a single person or family held more than 5% (individually) or 25% (family group) of the firm. For family-controlled businesses, we calculated how many board directors belonged to the controlling family: a ratio of family directors and the total number of board members, as seen in previous literature (Revilla et al., 2016). For nonfamily businesses, we assigned family board members a value of 0.
4. *Family CEO*: A "dummy" variable was applied, where 1 indicates that the CEO is a family member and 0 indicates that (a) the CEO is not a member of the family controlling the company or (b) that the company is not considered to be family- controlled.

Control Variables. We used the following control variables, measuring: (a) the size of the companies using the log of assets; (b) the age of the firm as the difference between the year of our study and the foundation year in logarithmic form. We also considered two financial variables as a control, given their potential influence on retrenchment strategies; (c) leverage, in the form of the ratio of long-term debt to total assets (Lim et al., 2013); (d) cash flow, in logarithmic form (Pearce & Robbins, 1993), as an indicator of financial liquidity; (e) the firm's sector, controlled through four dummy variables, identifying five main sectors: energy, manufacturing, construction, finance, and other services; and (f) ownership concentration, given its potential influence on family business performance (De Massis, Frattini, Pizzurno, & Cassia, 2015). This last variable was measured using the Herfindahl index of the ownership structure, by calculating the total sum of the squared fraction of shares held by shareholders. The Herfindahl index has been used extensively in previous research to measure entropy and the concentration of phenomena such as diversification (D. J. Miller, 2004), market diversity (Hitt, Bierman, Shimizu, & Kochhar, 2001), or ownership concentration (Li, Wang, & Deng, 2008). This index rises as ownership concentration increases and falls as ownership becomes more dispersed.

Statistical Models

We adopted the panel data approach, based on dynamic models that use lagged dependent and independent variables as explanatory variables. As mentioned in our Methodology section, our panel data refer to 599 observations from 126 firms over the 5-year period from 2008 to 2012. We determined the lag for the dependent variable by comparing the mean square error of the model with the first-order lagged dependent variable to that of the second- and third-order lagged models, finding no differences between them. Given the potential risk of endogeneity, we used the generalized method of moments. This statistical estimator is suitable for cases with endogenous variables and potential reverse causality (Jean, Deng, Kim, & Yuan, 2016; Yi, Wang, & Kafouros, 2013).

Table 1. Descriptive and Correlation Matrix.

	M	*SD*	Retrenchment	Size	Age	ROA	Leverage	Cash flow	Decline	Altman *Z*-score	Ownership dispersion	Family CEO
Retrenchment	0.032	0.703	1.000									
Size	3.205	9.583	−.013	1.000								
Age	40.43	27.04	−.003	.228***	1.000							
ROA	0.830	18.43	.002	.124**	.052	1.000						
Leverage	0.325	2.058	.035	−.272***	−.161**	.246***	1.000					
Cash flow	0.161	0.615	−.021	.765***	.213***	.264***	−.156**	1.000				
Decline	0.406	0.490	−.025	−.009	−.025	−.038	−.012	−.198***	1.000			
Altman *Z*-score	1.769	1.856	.095*	−.151***	−.144**	.474***	.614***	−.156**	−.007	1.000		
Ownership concentration	0.414	0.282	−.036	.063	.043	.018	−.047	.129*	−.047	.008	1.000	
Family CEO	0.389	0.503	.085*	−.104*	−.011	−.023	−.123*	−.105*	−.008	−.001	.426***	1.000
Family board membership	0.238	0.213	.063	−.143*	.121	−.072	.019	−.054	−.153*	.049	.141*	.403***

Note. ROA = return on assets.
*$p < .05$. **$p < .01$. ***$p < .001$.

Results

Table 1 summarizes the descriptive statistics and correlations between the variables used in our analyses, and the main results are summarized in Table 2. We have presented eight models: Models 1 to 4 represent the effect of family involvement on the board on the retrenchment strategy, Models 1 and 2 when survival is not at risk, and Models 3 and 4 when survival is at risk. In the same way, the last four models illustrate the effect of the family CEO on retrenchment; Models 5 and 6 when firm survival is not at risk and Models 7 and 8 when survival is threatened. In each pair of models, the first model includes only the direct effect, while the second model integrates the interaction effect. We have used level 1.8 of the Altman *Z*-score as the threshold for splitting the models with regard to survival risk, as has been well-established in the literature (Altman, 1968; Barbero et al., 2017; Bruton et al., 2003; Chen & Hambrick, 2012). As we expected, firm survival (Altman *Z*-score) and decline are not correlated when they are considered contemporaneous variables or only have a 1-year lag. Firms can suffer from declining performance during some years without the danger of failure, and vice versa, due to the nature of the financial structure (debt, leverage, etc.). As Bruton et al. (2003) stated, "Z-scores are best used to predict the firms that will face insolvency over the next 2 years," while "turnaround firms may continue on a pattern of decline and performance below their industry peers for many years without facing immediate bankruptcy" (p. 539). We selected a robust method to estimate generalized method of moments regression models, adopting the Sargan test to identify any overidentifying restrictions for all models. To control for potential multicollinearity, we ran the Arellano-Bond test (abond). The results (Table 2) reveal that there is no multicollinearity.

As we established earlier, Models 1 to 4 estimate the effect of family members' involvement on the board on the retrenchment strategy. In this case, the direct effects are significant in Model 1 ($B = -2.3515$; $p < .05$) and Model 3 ($B = -1.5052$; $p < .10$), showing that family involvement has a negative effect on retrenchment, that is independent of the threat to the firm's survival. These models also signify that declining performance has a positive effect on retrenchment intensity, as we proposed in the Theoretical Background section ($B = 0.1158$, $p < .05$; $B = 0.2330$, $p < .001$). When the effect of the interaction between family involvement and decline is included, the results show a positive and significant joint influence in both Model 2 ($B = 0.6689$; $p < .05$) and Model 4 ($B = 1.3132$; $p < .05$), while the negative direct effect of family involvement and the positive direct effect of decline remain significant. These results show that irrespective of the survival risk, family involvement positively moderates the negative effect of declining performance on retrenchment strategy. In other words, our results demonstrate that when a firm is confronted with a decline in performance, retrenchment measures are more intense when family involvement is elevated; this is consistent with Hypothesis 2a but not with Hypothesis 1a.

Table 2. Regression Results. Dependent Variable: Retrenchment.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8
Independent variables	Low survival risk		High survival risk		Low survival risk		High survival risk	
Decline	0.1158* (0.0961)	0.3602*** (0.0817)	0.2330*** (0.0412)	0.6058** (0.1940)	0.0465*** (0.0113)	0.0906*** (0.0230)	0.2649*** (0.0130)	0.4464*** (0.0261)
Family board membership	−2.3515* (1.1772)	−1.3241† (0.8531)	−1.5052† (0.9450)	−1.5976† (2.5543)				
Family board membership × Decline		0.6689* (0.3077)		1.3132* (0.6747)				
Family CEO					0.6005 (0.4223)	0. 5307 (0.0484)	0.4826*** (0.0540)	0.7535*** (0.3699)
Family CEO × Decline						0.1254*** (0.0370)		0.3327*** (0.0365)
Retrenchment ($t-1$)	−0.3192** (0.0073)	−0.2988* (0.0105)	−0.1982** (0.0081)	−0.1920* (0.0102)	−0.3102** (0.0097)	−0.3321* (0.0102)	−0.2017** (0.0121)	−0.2102* (0.0142)
Size	0.1192 (0.0743)	0.1110 (0.0623)	0.0548 (0.0432)	0.0437 (0.0324)	0.1210 (0.0719)	0.1192 (0.0695)	0.0538 (0.0439)	0.0602 (0.0595)
Age	0.4837** (0.1982)	0.6451** (0.2219)	0.3981* (0.1102)	0.288 (0.1293)	0.5543** (0.2109)	0.6327** (0.2227)	0.3395* (0.1186)	0.2390 (0.1321)
Ownership concentration	−1.2732 (0.1092)	−1.1991 (0.2234)	−0.3982† (1.0918)	−0.9831† (1.1201)	−1.4532 (0.1632)	−1.3211 (0.2102)	−0.4219† (0.6635)	−0.5431† (0.2387)
ROA	0.0129† (0.0192)	0.0018 (0.0121)	0.0012 (0.0015)	−0.0011 (0.0013)	0.0035† (0.0021)	0.0033† (0.0023)	0.0019 (0.0012)	−0.0018 (0.0017)
ROA ($t-1$)	−0.0081 (0.0051)	−0.0100 (0.0882)	−0.0175* (0.0191)	−0.0151 (0.0182)	−0.0031 (0.0011)	−0.0042 (0.0012)	−0.0042* (0.0010)	−0.0073 (0.0010)
Leverage	−0.2192** (0.0633)	−0.3921** (0.0726)	−0.2983*** (0.0382)	−0.2539*** (0.0298)	−0.2538** (0.0650)	−0.2883** (0.0583)	−0.2983*** (0.0792)	−0.3209*** (0.0667)
Leverage ($t-1$)	0.2211** (0.0981)	0.3287** (0.1432)	0.0738 (0.0788)	0.0772 (0.0672)	0.2473** (0.0714)	0.2873** (0.0889)	0.0518 (0.0432)	0.0530 (0.0398)
Cash flow	−0.0028 (0.0192)	−0.0283* (0.0199)	−0.0482** (0.0182)	−0.0398** (0.0163)	−0.0172 (0.0163)	−0.0209* (0.0132)	−0.0566** (0.0155)	−0.0540** (0.0165)
Cash flow ($t-1$)	0.0192 (0.0288)	0.0549† (0.0210)	0.0773** (0.0203)	0.0822** (0.0212)	0.0273 (0.0219)	0.0599† (0.0435)	0.0872** (0.0133)	0.0821** (0.02985)
Wald chi-square test	24.648***	57.978***	8.295***	9.786***	25.477***	49.730***	10.392***	9.554***
Sargan test (p value)	35.079 (.9653)	34.458 (.9710)	54.266 (.4871)	55.715 (.3368)	32.382 (.9109)	30.388 (.8220)	51.339 (.5109)	54.399 (.4321)
Arellano-bond test (second order)	0.4197	0.4207	0.5439	0.4783	0.4209	0.4177	0.5293	0.4209
No. of instruments	65	66	65	66	65	66	65	66
No. of groups	69	69	78	78	95	95	93	88
No. of observations	289	289	301	301	289	289	301	301

Note. ROA = return on assets.
†$p < .10$. *$p < .05$. **$p < .01$. ***$p < .001$.

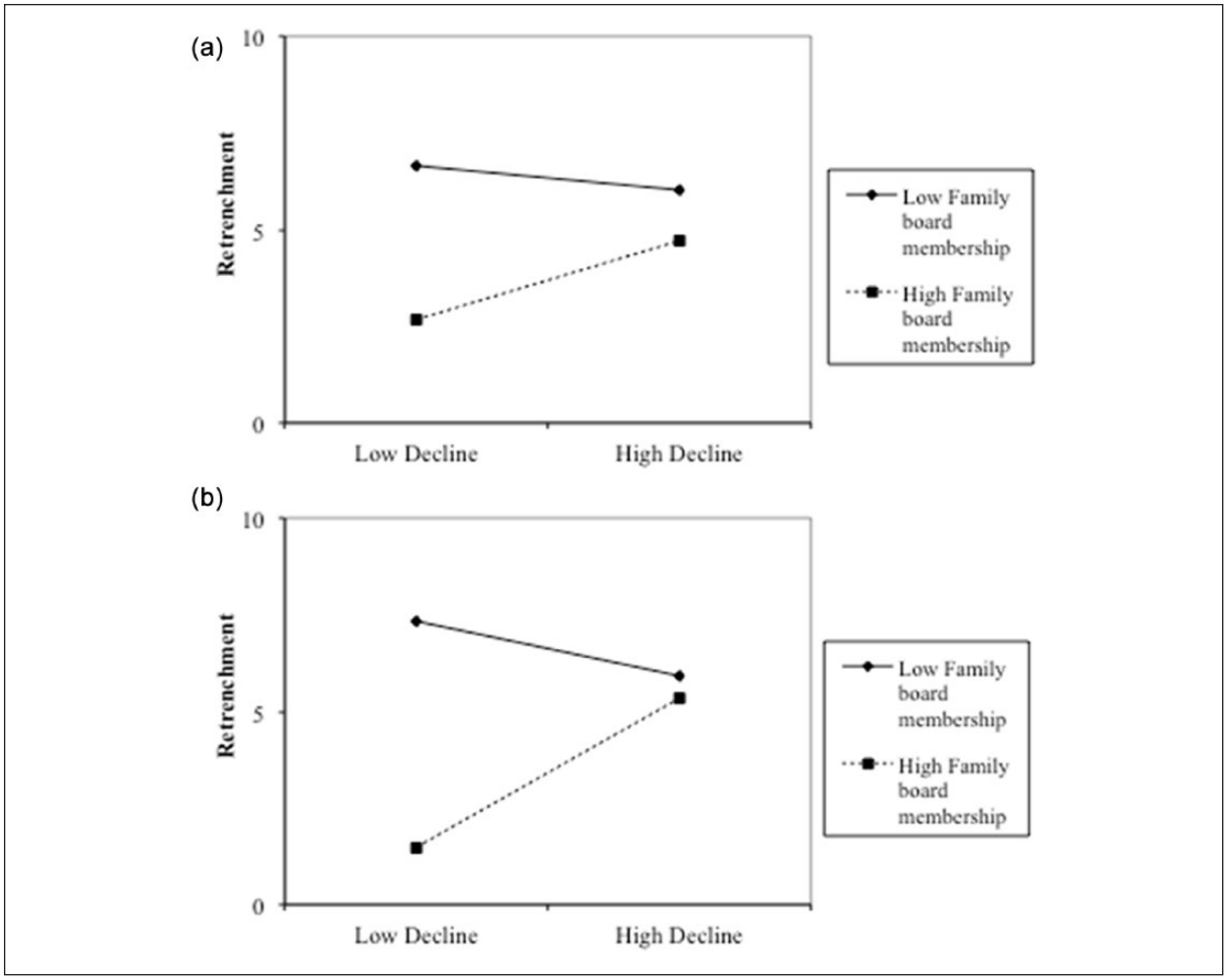

Figure 1. Family board membership × Decline effect on retrenchment: (a) Low risk to survival (Altman *Z*-score > 1.8); (b) High risk to survival (Altman *Z*-score < 1.8).

In relation to the effect of the family CEO, Models 5 and 7 represent the direct effects, while the interaction effects of the family CEO and decline are included in Models 6 and 8. Again, as we expected, the direct effect of declining outcomes on retrenchment strategy is significant and positive (B = 0.0465, $p < .001$; B = 0.2649, $p < .001$). However, the direct effect of the family CEO is significant only when firm survival is at risk—that is, when the *Z*-score is below 1.8 (Model 7: B = 0.4826; $p < .001$)—but not when there is a low threat to survival (Model 5: B = 0.6005; $p > .10$). However, our hypotheses correspond to the joint effect of the family CEO and declining performance in two different contexts: when the firm's survival is threatened and when it is not. These joint effects are set out in Models 6 and 8. The interaction effects are positive and significant in both Model 6 (B = 0.1254; $p < .001$) and Model 8 (B = 0.3327; $p < .001$). These results are consistent with Hypothesis 2b but not with hypothesis 1b. This is because a family CEO intensifies the retrenchment strategy not only when the firm's survival is at risk but also when its survival is not threatened. However, the intensity of the retrenchment measures is more elevated in the former context, as the level of the beta coefficients signifies.

Figures 1 and 2 further illustrate this interaction effects model. Figure 1 characterizes the interaction effect between deteriorating performance and family involvement on the board when firm survival is not in

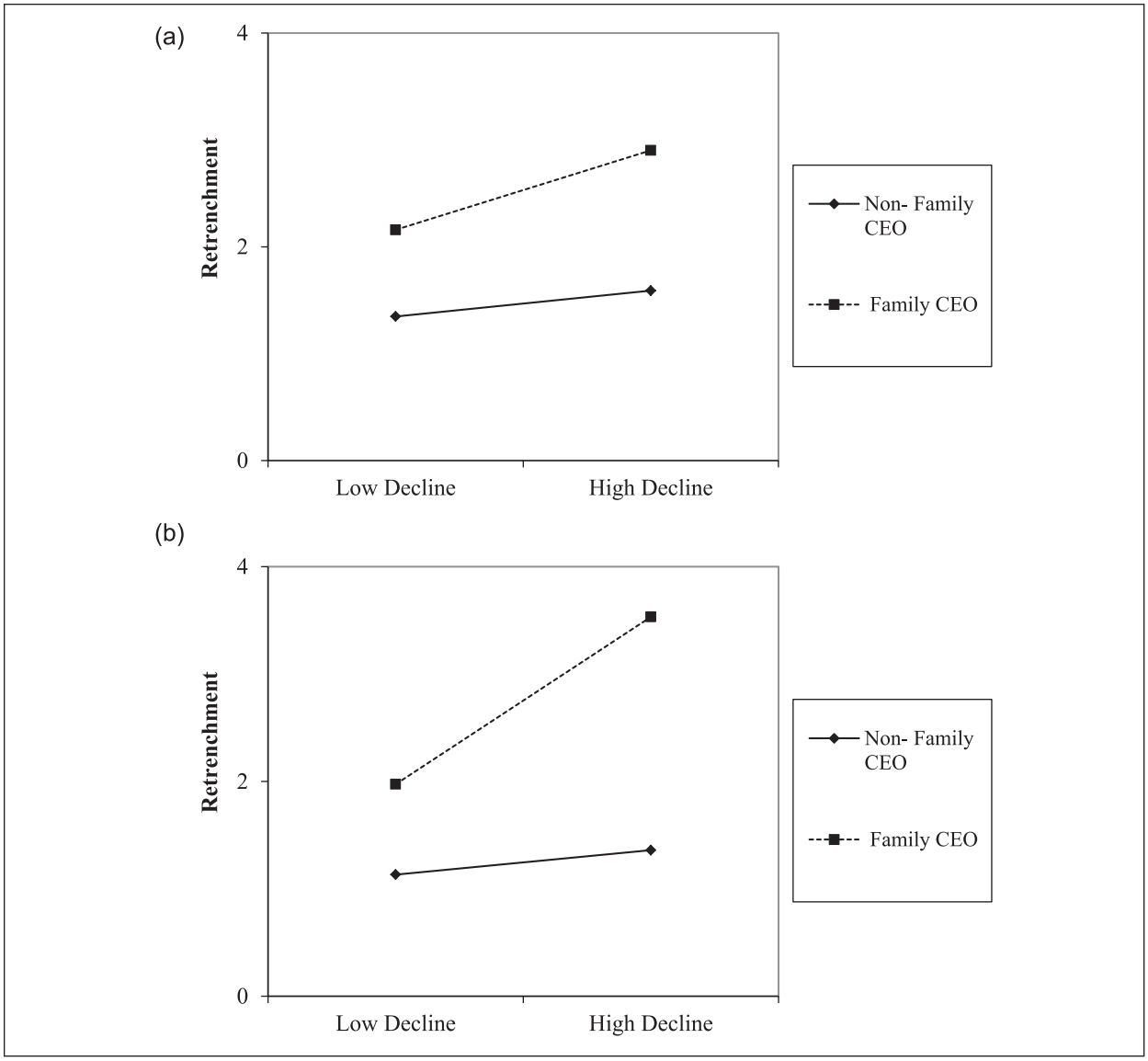

Figure 2. Family CEO × Decline effect on retrenchment: (a) Low risk to survival (Altman *Z*-score > 1.8); (b) High risk to survival (Altman *Z*-score < 1.8).

jeopardy (Figure 1a) and when it is in jeopardy (Figure 1b). As Figures 1a and 1b illustrate, higher family involvement on the board increases the intensity of the retrenchment measures in the context of failing performance, although the absolute level of these measures is lower in firms with higher family involvement. When survival is at risk (Figure 1b), the effect of greater family involvement on the increasing intensity of retrenchment measures is also higher than when survival is not at risk (Figure 1a). The effect is also positive when there is a family CEO, such that their presence increases the intensity of retrenchment measures when performance is waning in both circumstances: when survival is not at risk (Figure 2a) and when it is threatened (Figure 2b). Furthermore, in both scenarios the retrenchment strategy is more intense when the CEO is a member of the owner family than when there is a nonfamily CEO. These results support Hypothesis 2b but not Hypothesis 1b.

Robustness Check

We have tested the robustness of this model in various ways. First, we formulated a three-interaction effect model. We decided against splitting the sample by the Altman *Z*-score variable (survival risk) and instead adopted this variable as a moderator in conjunction with declining outcomes and the family dimensions (family involvement on the board and a family CEO). The results[1] are concurrent with the main findings, revealing (a) the existence of a convergence process in the behavior of firms with both greater and lesser family involvement on the boards when they experience a decline in their performance that may or may not signify a threat to their survival and (b) that when the firm starts to experience a diminution in its results (decline), the fact that the CEO is a member of the owning family stimulates the retrenchment strategy irrespective of whether or not the firm's survival is endangered.

Second, as an additional robustness check, we repeated the models, excluding direct effects when the interaction effects were included and also dismissing the two-way interaction effects when three-way interaction effects were considered. The results of these tests were consistent. We also estimated the interaction effect of family characteristics (family board membership and family CEO) and firm survival risk (Altman Z-score) by splitting the sample by performance (i.e., declining vs. nondeclining), and the outcomes were consistent with the results described above.

Third, we estimated the main models, considering cost and asset retrenchment measures individually. In this case, the results were analogous to those outlined above, with the only difference being the intensity of the effect (slopes) but not the significance or the sign of the beta coefficients.

Discussion

This work analyzes the ways in which firms react to a decline in performance during a period of crisis, when three factors occur simultaneously: There is (a) a decline in performance, (b) a threat to survival, and (c) a family influence on the board of directors, whether through family board membership or through the CEO's membership of the owning family. This study therefore proposes two double hypotheses, distinguishing the type of reaction according to whether or not the firm's survival is threatened, given that the desire for continuity is a fundamental objective of family firms (Revilla et al., 2016).

For the first hypothesis, the results demonstrate that a greater number of family board members increases the intensity of the retrenchment strategies when results are declining regardless of whether survival is threatened. This confirms Hypothesis 2a and rejects Hypothesis 1a. We found that the effect of family board members on the retrenchment strategy is even more pronounced when there is a heightened threat to survival. In other words, family board members always have the effect of intensifying the adjustment measures when performance is failing, and this reaction is more intense when survival is jeopardized. This effect undoubtedly derives from the context of the global financial crisis that started in 2009, in which most firms subjectively considered that their survival was in danger, which resulted in more intense retrenchment. The results therefore illustrate the importance of family involvement in implementing measures that fervently seek to avoid a potential loss of SEW, whether an authentic or a perceived threat, where such a potential loss of SEW might follow the liquidation of the company, or the possibility of the family's ownership share having to be sold (Gómez-Mejía et al., 2007). This result might also be affected by the fact that all of the firms in our study are listed on the stock market. In these firms, the boards of directors comprise a combination of family and nonfamily members, hence mitigating family members' resistance to retrenchment measures.

The results do not support the notion that a greater number of family board members prevents the firm from taking retrenchment measures, either because they fail to recognize low performance or because of their wish to protect the aspects of SEW that are most strongly linked to internal social capital, such as employee relations (D. Miller et al., 2008). The severity of the Spanish economic crisis facilitated a context in which redundancies were perceived as the most favorable option for salvaging most companies. In this environment, retrenchment strategies were considered as more of a means to survive (saving jobs in the long term) than as a short-term technique in which firms were incited to reduce costs and increase profits for owners and shareholders. The more intense reaction of family businesses to the economic recession could be perceived as a sign of the greater stewardship behavior of family board members to preserve SEW in the long term (Gómez-Mejía et al., 2007).

The results also highlight that when the CEO is a member of the owning family, the adoption of retrenchment decisions is more intense when there is a decline in the company's performance, regardless of the threat to the

firm's survival that this implies. Therefore, there is no support for the arguments relating to the reluctance of the family CEO to confront declining results in order to prevent the erosion of certain elements of SEW, particularly those pertaining to employee relations (D. Miller et al., 2008) and other long-term relations with partners and neighboring communities (Berrone et al., 2012). Where there are links to distinct internal and external agents among firms with greater numbers of family board members (Cruz et al., 2010) and where values such as feelings of closeness and interpersonal solidarity prevail in the context of poor results (Uzzi, 1997)—at least in our sample of firms—the presence of a family CEO does not hinder the adoption of difficult decisions such as retrenchment, even though such decisions may have a negative effect on these close agents (particularly on employees and suppliers). Again, these arguments appear to correspond more closely to the increased propensity to introduce this type of measure when there is strong leadership from a family CEO. Similarly, the results support the idea favored by the SEW approach: As the threat to survival increases, the firm's response to safeguard SEW is more intense when the firm is headed by a family CEO.

Contributions and Limitations

This work makes a number of contributions to the understanding of family firms. First, our investigation demonstrates that firms in which the family has a decisive influence on the decision-making process (through its involvement on the board or through a family CEO) are more flexible when they are required to adhere to retrenchment measures to address diminishing performance. This would suggest that these firms are more agile in their decision making (Schulze et al., 2003), given their clear leadership by an individual or through the existence of a majority shareholder. This diverges from nonfamily firms, in which ownership is more dispersed (De Massis et al., 2013). Second, our work supports the role of SEW in relation to potential threats to a firm's survival (Gómez-Mejía et al., 2007; Gómez-Mejía et al., 2010). Thus, when a decline in a firm's performance increases distress or the threat to survival, there is a significant increase in the intensity of the retrenchment measures adopted by family-led firms, specifically those with family involvement on the board of directors or with a family CEO.

Conversely, there is no support for the argument that a family firm will strive to uphold high-quality relations with employees and agents close to the firm (Berrone et al., 2012; D. Miller et al., 2008), even at the cost of sacrificing its economic returns. The results reveal that firms whose decisions are family-led are able to implement retrenchment measures when required to improve their financial results, at least in the case of firms listed on the stock market. Similarly, our research shows that in this type of firm, family board members and/or the presence of a family CEO do not automatically cause a type of "myopia" that creates a distorted view of reality that might preclude the recognition of poor results and inhibit the adoption of retrenchment measures.

However, our results should be considered in context. As our sample only incorporates firms on the stock exchange, this might affect the results and prevent them from being generalized to small, unlisted family firms. A retrenchment strategy is more visible in publicly owned firms than in private and smaller firms, as every stakeholder of public firms has to be informed, and is much more significant for public firms than for private small and medium enterprises. This constitutes a limitation to our work, which should include other types of firms in which much greater discretion is provided to board members and family directors than among publicly traded firms. Another limitation of the study is the national context (Spain) and its time frame (a period of financial crisis from 2008 to 2012), which is not easily transferable to other national contexts or time frames. Finally, the work only considers the intensity of retrenchment measures during a period of poor results but does not consider the time scale of these measures, the decisions taken during subsequent phases of the turnaround process (Pearce & Robbins, 1994; Robbins & Pearce, 1992), or the outcome of the process (exit vs. failure; recovery time; etc.).

These limitations provide direction for new studies. We have already acknowledged the need to extend our research to include other types of firms (unlisted, small and medium enterprises, etc.). Likewise, new investigations should explore in greater depth the types of retrenchment decisions taken beyond the reduction of assets or costs, and the timing of these decisions. Additionally, new models should provide information on supplementary factors correlated to those set out here, such as the particular idiosyncrasies of the ownership structure, the type and influence of different stakeholders, or the characteristics of the owning family (Jaskiewicz, Combs, Shanine, & Kacmar, 2017). Finally, the time factor should be included. The temporal dimension is vital to understanding how the decision-making

process develops in unfavorable conditions. It may be relevant to analyze the speed with which retrenchment decisions are taken by family and nonfamily firms, as well as whether or not the intensity of such decisions is dependent on this speed.

Conclusion

This work contributes to our understanding of how family firms—that is, firms with members of the owning family on the board of directors and/or with a family CEO—behave differently at times of particular difficulty, such as periods of crisis, when businesses are confronted with a deterioration in their performance. The results demonstrate that firms led by members of the owning family react more dynamically, as indicated by the stewardship and SEW approaches. They also reveal that a firm's survival does not need to be under threat to prompt this greater dynamism, but when the threat does exist, the reaction is much more pronounced. Further research is required to advance our understanding of how family businesses behave in comparison to their nonfamily counterparts. Declining performance serves as a useful context for investigating the differences between these two types of firms when approached from the stewardship and SEW perspectives.

Declaration of Conflicting Interests

The author(s) declared no potential conflicts of interest with respect to the research, authorship, and/or publication of this article.

Funding

The author(s) disclosed receipt of the following financial support for the research, authorship, and/or publication of this article: This manuscript has been financed by Santander Family Business Chair of the University of Seville and the Ministry of Economy and Competitiveness (ECO2017-84364-R Project).

Note

1 Detailed results are available from the authors by request.

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