STRATEGIC DYNAMICS AND CORPORATE GOVERNANCE EFFECTIVENESS IN A FAMILY FIRM

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Abstract

This paper employs a case-study approach to address linkages between corporate governance and a firm's strategic dynamics. It investigates a family firm which moved from a state of crisis to a renewed growth and profitability stage to analyze how establishing appropriate governance practices may contribute to strategic renewal and value creation. Creating an effective system of corporate governance is a crucial task for all firms, requiring an appropriate balance between accountability and entrepreneurial dimensions to carry out the firm's strategies. Data reveal how corporate governance variations over time may help a family firm to move through its organizational life cycle, by creating an appropriate fit with the evolving strategic needs.

Keywords: Corporate Governance, Strategic Dynamics, Family Firm, Value Creation

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1. Introduction

Although corporate governance is increasingly recognized as a critical organizational factor influencing the firm's performance and long term survival, the corporate governance debate, over the last few decades, has been distinguished by the prevalence of the agency perspective with a main focus on the accountability dimension (Filatotchev, 2007; Ingley and Van Der Valt, 2005). Much attention has been devoted to mechanisms ensuring monitoring and control to protect owners from managerial opportunism, but resources and knowledge roles have been underestimated. Nevertheless, the enterprise dimension of corporate governance may become relevant for increasing strategic flexibility and promoting long term growth through differing stages of a firm's life cycle (Filatotchev and Toms, 2003). Substantial efforts have been directed towards large and mature public companies, mainly consistent with the U.S. experience, concentrating on a static theorising of the principal-agent perspective (Filatotchev *et al.*, 2006), while little attention is given to family firms, even if they are largely represented around the world (Westhead *et al.*, 2001). Family firms share some dimensions common to non-family firms (Sharma, 2004), but their governance issues may become potentially more complex than in non-family firms, given the interwoven systems of ownership, management and family (Westhead *et al.* 2001; Chua *et al.* 2003).

Many family firms deal with several challenges to their long term value creation efforts and the establishment of an effective corporate governance system is a crucial task they face (Steier, 2001). The organizational value creating attributes are embedded in the firms' system of corporate governance on the basis of differing incentives, authority structures and norms of accountability (Carney, 2005). Investigating how family members exert their governance role to influence the practice of strategy may provide useful explanation on the topic of value creation over time in a family firm (Sharma *et al.*, 1997).

This paper addresses the effectiveness of the corporate governance practices in terms of fit with the emerging strategic needs. On the basis of a case-study approach, it explores key contingencies affecting the integration between the firm's strategic dynamics and the corporate governance practices along the firm's organizational life cycle. It investigates the case of a family firm which shifted, over the last years, from a state of crisis to growth and then went public, while still remaining controlled by a small number of families. It represents interesting evidence of a strategic transition and its reciprocal interplay with the corporate governance system.

We extend previous research by examining how corporate governance mechanisms work and interact, then providing support or obstacles to the firm's strategic behaviour. Addressing the topic, this study seeks to identify which variables are relevant to explain how the corporate governance practices and strategic dynamics were integrated, providing an effective support to the strategic transition of the firm examined.

This paper aims to extend previous research providing several contributions. First, responding to criticisms to well established, but universal perspectives on corporate governance, it contextualizes the analysis to a family firm, trying to bridge corporate governance literature with family business research specificities. Second, it addresses, in an integrated view, emerging changes in corporate governance practices according to the firm's strategic dynamics to develop a dynamic and process perspective. In this way, it contributes to better understanding conditions influencing the effectiveness of corporate governance. Third, it focuses how the corporate governance mechanisms may be differently managed to fit with the strategic needs arising from the firm's organizational life cycle. In a dynamic view, it will investigate how a family firm may overcome strategic transitions by appropriately rebalancing its corporate governance system.The study is structured as follows. The following section will shortly introduce the study's main theoretical constructs and some missing links in explaining relationships between corporate governance effectiveness and strategic dynamics in a family firm. Then, the study's longitudinal research design, data collection and data analysis will be described. In the following sections, after a brief description of the case study, a specific statement will be delineated on the basis of the case analysis linking it to the results of previous studies. Finally, in the discussion section, the broader implications of this study will be outlined.

2. Theoretical framework

The entrepreneurial dimension of corporate governance and value creation.

Corporate governance effectiveness stems from an appropriate fit with the firm's strategic requirements, balancing accountability and enterprise dimensions to carry out the firm's strategies (Filatotchev *et al.*, 2006). Firms commonly vary their strategic orientation passing through different stages of their life cycle and these changes may require appropriate adaptations in corporate governance established practices (Zahra and Filatotchev, 2004; Gedajlovic *et al*, 2004; Huse and Zattoni, 2008).

Differing perspectives have addressed how family firms deal with strategic challenges, hence attaining value creation or failing to do so. Agency theorists emphasize that due to retaining both ownership and control, and because of their intra-familial altruistic relationships, family firms are exempt from agency costs (Fama and Jensen, 1983). Goal congruence among family members and informal control pressures will reduce the need to monitor behaviour or outcomes, making formal governance arrangements unnecessary or counterproductive (Jensen and Meckling, 1976). In contrast, other studies in the agency tradition have emphasized several potential inefficiencies which may lead to value reduction in the context of family firms (Schulze *et al.*, 2001).

Well established approaches focusing the accountability dimension of corporate governance, mainly rooted in the agency perspective, are increasingly subjected to criticism (Keasey and Wright, 1993; Huse, 2005; Filatotchev, 2007). Agency theory has shortcomings when considering entrepreneurial firms pursuing growth which emphasizes crucial requirements of knowledge and resources. Even if accountability has been the main focus in corporate governance research, along the firm's life cycle the value creation dimension may become relevant, in accordance with the firm's strategic dynamics (Zahra and Filatotchev, 2004; Filatotchev, *et al.*, 2006).

Corporate entrepreneurship involves the activities referring to corporate venturing, strategic renewal and innovation (Sharma and Chrisman, 1999), providing potential means for revitalizing established companies and developing value creation. Corporate governance may sustain value creation by influencing the organization-environment interdependences (Filatotchev and Nakajima, 2010). Value creation refers both to opportunities recognition in the external environment and to their exploitation by the development of sustainable competitive advantages (Adner and Helfat, 2003). Identifying opportunities is a key value creation activity, but firms subsequently incapable of exploiting them may waste their potential. However, firms not engaged in seeking new opportunities, even if this has competitive advantages, may risk a reduction over time of their value creation or of their current wealth, depending on changes in their environment (Alvarez and Barney, 2004). Thus, the effectiveness of corporate governance stems from how managers and directors strategically choose corporate governance practices to deal with environmental pressures (Aguilera *et al.*, 2008) Competitive advantages are built upon the possession of valuable, rare, imperfectly imitable and non replaceable resources idiosyncratic to the firm (Barney, 1991) and well known drivers may be new products or new processes creating performance differences among firms (Danneels, 2002). Absorptive capacity is recognized as a key resource to develop value creation resulting from relationships with external entities that can promote access to and control of resources and assimilation of knowledge. Among the firm's resources, knowledge is the most likely to lead to enduring success because it is socially complex and difficult to imitate (Barney, 1991). Entrepreneurial strategies may then pursue value creation by leveraging the existing knowledge base, recombining and extending existing knowledge and importing new knowledge (Kazanjian *et al.*, 2002). However, required knowledge could be obtained changing the composition or decision making processes of board of directors (Zahra *et al.,* 2009:249). Knowledge is most critical in technology-based firms, because generating and exploiting knowledge requires that knowledge to be continually replenished. Given that the acquisition and exploitation of knowledge are mainly an outcome of social processes, absorptive capacity may become a critical antecedent for the long term survival and profitability of technology based firms. However a neglected topic in previous research refers to how family related social interactions may influence the family firm's capability to develop a dynamic strategic adaptation (Salvato and Melin, 2008, Sirmon and Hitt, 2003).

Absorptive capacity is a dynamic capability, referring to knowledge creation and utilization, which increases a firm's ability to gain and sustain a competitive advantage (Zahra and George, 2002). The ability to access and absorb knowledge influences the firm's effort to value creation, but the level of prior related knowledge characterizing a firm moderates its potential identification and utilization of external knowledge (Cohen and Levinthal, 1990). It has relevant implications, even if neglected in previous research, for firms going through a transition from a start-up phase to a more professional management stage along their organizational life cycle which requires the building and the development of differing capabilities (Zahra *et al.,* 2009). An appropriate identification of knowledge residing outside the firm and the capacity to absorb it into new processes develops innovation and opportunities recognition, (Cohen and Levinthal, 1990; Zahra and George, 2002) and the ability to successfully employ such knowledge for market purposes promotes opportunities exploitation (Tsai, 2001).

Furthermore, in addition to the firm's resource base, organizational and strategic processes are also relevant to promote the manipulation of resources into value creating strategies (Salvato and Melin, 2008). Individuals holding power positions, such as senior managers or board members, can play a role in the development of capabilities by undertaking specific initiatives and establishing organizational routines. Dynamic capabilities allow firms to renew competencies and to strategically arrange and bundle organizational resources, skills and routines required to develop value creation facing the evolving competitive conditions. They have been the focus of an increasing body of research, but few cases of analysis have addressed the processes inside organization and how corporate governance practices may influence their development.

3. Methodology

3.1 Research Design

We followed a case-study research strategy (Yin, 1994) to identify contingencies affecting relationships between changes in the strategic orientation and corporate governance practices in the context of a family firm. In selecting research sites, the goal is to identify available cases that are likely to replicate or extend theory, rather than randomize (Eisenhardt, 1989), and that are promising to provide rich empirical data on the investigated phenomenon, based on a plurality of data sources (Yin, 1994). Accordingly, the case of RCF was selected because it provides a meaningful experience of a strategic transition from crisis to renewed growth and a radical change in the corporate governance practices. Furthermore, it is controlled by a dominant coalition of three families where two members from each family serve on the board or have a managerial position at a higher level. Thus this case is appropriate for exploring the mutual interplay between strategic dynamics and the potential adaptation of corporate governance structures and processes in a family firm. This design enabled to identify salient constructs and their constituent components (Yin, 1994).

3.2 Data Collection

Data were collected through personal interviews and secondary sources (newspapers, articles from magazines, internal company documents, annual reports, notes and letters to the investors, company press releases, the company website and so forth). Aiming to investigate the research topic in depth, the case study was conducted relying on interviews with several people in the organization to represent different perspectives (Myers, 2009). Interviews were the primary source of data and informants at different levels of the corporate governance system were met to yield a more accurate analysis (Yin, 1994). Semi-structured interviews were conducted separately with individuals representing ownership, board members and managers.

At first, the key informants were identified, as individuals having the most information about our specific topics of interest in the organization and with decision making authority or influence in the corporate governance and strategy topics. The key people were both initiators of the firm's process of change and are currently involved in the boardroom and/or in managerial roles. Interviews were also extended to all individuals proved as having significant information because of their lead positions in the organization or in the change process under analysis (Myers, 2009).

Interviews were conducted during several formal and informal meetings having an average length of two and half hours. The interviews were audio-recorded and transcribed after each meeting.

Interviews were organized in two parts. Initially respondents told their story on the evolution of the firm's strategies and on the characteristics and functioning of the corporate governance system along the years considered. The research focused on the threshold from crisis to growth, but further data regarding the previous history of the firm were acquired for a better interpretation and contextualization of events and roles of the people involved holding key positions. Open-ended questions were asked (i.e. overview of the family business' history, crucial events referring to the firm's strategic behaviour and changes, information about the corporate governance practices and their variations over time, the involvement of families members) without specifying to the interviewee the constructs of interest in the research project, with the aim of avoiding influencing their answers.

During the interviews, probing questions were asked to obtain more details on the topics discussed and to triangulate the data acquired (Yin, 1994). In the second part of the interviews, structured questions were asked in order to investigate the role played over time by specific corporate governance practices (i.e. ownership identity, board composition, board tasks), their interplay and potential complementarities or substitution effects. The aim was to investigate the outcome of the established governance arrangements as a whole and the following degree of effectiveness in supporting the firm's strategic needs throughout different stages of its life cycle. Secondary sources allowed to build longitudinal accounts both of the firm's strategic dynamics and of intervening variations in the corporate governance structure. They allowed to identify critical events, potential links and contribute to build up a description of the organization and of its history (Bryman and Bell, 2007).

3.3 Data Analysis

Data analysis was guided by theoretical concepts regarding the entrepreneurial dimensions of corporate governance and an iterative cycle of analytic induction and deduction was employed (Eisenhardt, 1989). Data were triangulated among respondents and from secondary sources, such as published and unpublished documents. The data collected were stored in a data base specifically designed for the task of structuring and clarifying information and then was carried out a recursive iteration between data and theoretical constructs (Bryman and Bell, 2007). In a first phase, each construct was addressed separately and then were explored emerging relationships among the identified constructs. Interview transcripts, observations and secondary data were carefully read to identify and refine patterns. During the data analysis memos were generated and then matched to refine theoretical understanding (Yin, 1994). The emerging theoretical constructs developed by the memos were compared to the evidence for evaluating their fit with data in an iterative process (Yin, 1994; Eisenhardt, 1989), often generating new and more fine grained memos which became the basis for the presentation of the research findings.

To check the credibility of the interpretation of data, confirmation was asked from respondents on an ongoing basis. Then findings were presented to peers to ensure the validity of the analysis and theory building during several informal and formal meetings.

4. Case description

RCF was founded in 1949 in Northern Italy, by three technicians who left their former employment as a result of post-war restructuring. It made its mark in the public sound and professional audio system market thanks to the quality and technological sophistication of its products. The company manufactured and sold professional microphones, amplifiers and loudspeakers. Yet, despite its growing reputation, RCF suffered from a chronic lack of capital that, in times of crisis, put the company under extreme pressure and led to frequent changes to its governance structure.

In 1982, as a consequence of the financial difficulties the company had been experiencing for a number of years, one of its suppliers purchased a majority share in a far-reaching organisational shift which saw one of its own managers take over an operational role in RCF with the task of overhauling its commercial division. At the same time, Mr. Macchiaverna, a consultant with the new buyer, took on a consultancy role at RCF too.

The company in the early 90s branched out into the loudspeaker market. Until then, the store of know-how built up in the fields of amplifiers and loudspeakers had never been applied to in-house products, serving instead in the supply of components for finished product manufacturers. In 1995, the company was at a standstill again because of an awkwardly high number of partners and their lack of cohesion, which made it impossible to define a clear strategy and led to stalemate and decisional inconsistency.

That year, in a bid to overcome the managerial problems the company was facing, the majority coalition offered a 22% share to Mr. Arturo Vicari, an engineer with a proven track-record in sound systems and the owner of a company involved in high frequency electronic design for the music market, named A&B . Mr.Vicari became the new CEO, but he came into the company on the condition that he would have free rein in the running of operations. Despite having a share of only 22%, he demanded, and obtained, a shareholder's agreement that would protect him from interference by the other partners on the board of directors.

He provided the leadership the company needed by defining clear goals and strategies and he quickly gained superior performance. By 1998, the company had reached a turnover of around 80 billion lire, where in 1995, the figure at the close of the year was around the 45 billion mark.

Mr. Vicari believed that in order to consolidate its success, the company needed to expand the group internationally through M&A operations, but the other partners did not agree. Thus, Mr.Vicari started looking round for a buyer for the company.

A potential buyer was found a few months later, in the new year, in the shape of a company which was a world leader in mixer design. Its success was founded on a philosophy similar to that of RCF, namely producing innovative high quality products at affordable prices and not exclusively for the specialist market.

The purchase was completed by June 1998 and Mr.Vicari kept his position as CEO for a few months longer in order to ease the transition.

Yet, what should have been a successful merger failed to yield the desired results, and, after an auspicious start, the company' profitability began to drop, until, in 2003, it collapsed entirely.

There were many reasons for the failure, but they were mainly connected with the unbridgeable divide between an almost entirely American governance and top management on the one hand, and the rest of the company, particularly the board of directors, on the other.

In their efforts to amalgamate the company into the rest of the group, the new owner lost sight of the potential that was specific to RCF, particularly its trademark. Indeed, most RCF products were sold under the new owner trade name, with the result that the name of RCF gradually disappeared from the market.

R&D was experiencing problems, too. Although there was no lack of resources and skills, there was no guiding hand to direct the work of technicians and researchers.

The company's finances continued to deteriorated, until, during the course of 2003, the management of the group gradually came to the realisation that production in Italy had become unviable. On 6 December 2003, the company was put into liquidation and the judicial arrangement with creditors followed soon thereafter.

At that point, Mr.Morlini, one of the majority shareholders of the pre-Mackie era who had stayed on throughout the intervening years, called upon Mr.Vicari and Mr.Macchiaverna to take part in a re-purchasing operation.

At the start of 2004, with the completion of a complex operation to repurchase RCF, Mr.Vicari, Mr.Macchiaverna and Mr.Morlini were ready to start rebuilding the company. The ownership was divided in the following way: Vicari 50%, Macchiaverna 30% and Morlini 20%. The board of directors consisted of Mr.Macchiaverna as President, Mr.Vicari as CEO and Mr.Morlini as CFO. Although they were all members of the board of directors, each had clearly defined tasks and areas of responsibility in which they enjoyed full autonomy and the complete trust of the other members: Mr.Vicari was to take care of management, Morlini of administration and finance and Mr.Macchiaverna of tax and M&A matters.

The company's revival was sustained by the people working in RCF. The return of the previous CEO, the averted threat of redundancy, the challenge of rebuilding a company from scratch sparked immediate commitment in the workers who had been selected to stay on for this new adventure. Mr. Vicari had continued to work in the sector and had never taken his eye off the strategic moves of RCF, and therefore held a clear vision about why things had gone wrong and how to resolve them. His strategy was to upgrade the brand name by developing superior quality products. The R&D work carried out by Mr.Vicari's company over the previous years contributed considerably to making this possible. A&B had invested heavily on electronics applied to sound, digital technology in particular. Nevertheless, the operation was not so straightforward, as rather than simply taking an A&B product and applying to it the RCF brand name, it involved developing a new RCF product using A&B technology. The capacity of RCF's technical department to adapt quickly to new technological solutions was vital in creating new products at extremely short notice.

Success was immediate; the company started working in January and by March it already had a turnover of 2,000,000 euro, a trend it maintained for the entire year, closing the year with revenues to the tune of approximately 24,000,000 euro. On the wave of the success of its new digital products, the company's growth rate remained steady throughout the subsequent two years, reaching a total growth of 40%.

Alongside innovative products and a well-known brand name, RCF's revival owed much to the reputation and network relationships of its new owners, who were able to rally all the company's stakeholders in the effort to relaunch the business.

One final element in the revival of RCF was the speed at which the top management made the decisions that enabled the organisation to re-orient itself along the lines set out by its leader and achieve results within a time-frame that until that moment had been not predictable. The trust that existed between the partners was fundamental and allowed each one of them to commit fully to the task in hand without fear of interference from the others.

In 2006, encouraged by growing sales and excellent profitability, the company decided to make another quality leap and float itself on the Italian stock market. Mr.Vicari revived his intention of expanding rapidly by making acquisitions, but this time he received the full backing of the other members of the board. The stock market seemed to be the most effective way of putting together the necessary capital and giving the group solidity and continuity.

RCF's listing reflected the management philosophy of its owners-directors. A new company was set up to purchase RCF and A&B shares and make a public offering. The decision to float the group leader and to leave the bulk of production to the subordinate companies made it possible to adopt an extremely agile management model for the operative companies.

5. Propositions

Collected data provide evidence on the integration between the established corporate governance structure and the firm's strategic dynamics going through its organizational life cycle. The threshold from the state of crisis was characterized by a radical change in the corporate governance structure and processes, which became the starting point for a strategic renewal. After a few years as a subsidiary of a large U.S. company, RCF reverted to a family owned structure in 2005. Initiators of the throwing again were Mr. Macchiaverna, Mr. Vicari and Mr.Morlini and they represent the dominant coalition of families holding the ownership of the firm. They started to run the business in 2003 when the U.S. company controlling RCF declared its failure and began insolvency proceedings. They rented the firm through an agreement outlined in a court authorization which gave them the option to buy the firm within three years, but enabled them to run the business forthwith, without interference from the U.S. company. They became owners in 2005, but they had acted as de facto owners-managers since 2003. The new owners decided to be directly involved in running the business, serving as members of a completely renewed board of directors. Top management team from the U.S. company was substituted by selecting and appointing young, but experienced internal managers with a long tenure in RCF. The aim was to shape a cohesive and proactive team, with high managerial skills, able to address new strategies for overcoming crises by exploiting organizational, but previously neglected resources. These changes underlie a substantial redesign of the corporate governance structure in RCF which allowed the pursuit of new strategies by reconfiguring the resource base and the RCF's strategic positioning to develop value creation. Furthermore, data referring to previous events in the firm's history show that the firm went through recursive stages of crisis and growth, associated with changes in established governance practices which provided help or obstacles to the firm's strategic orientation. Thus, case data led to the following proposition.

> *Proposition 1: Facing strategic thresholds, appropriate changes in the corporate governance structure may facilitate the firm's ability to pursue a strategic renewal and inadequate variations may obstacle its development and its survival.*

In the case we studied, changes in the RCF strategic dynamics were largely conditioned by previous variation in the firm's corporate governance established structure. A previous change in corporate governance allowed going through a crisis that in 2003 led to insolvency. Data show that, among the corporate governance mechanisms, ownership exerted a key role to help transition. The present owners identified key organizational and strategic limitations affecting RCF, then evaluating resources constraints and potential opportunities to recover the business. Furthermore, they addressed strategic goals and a consistent restructuring in corporate governance and organizational processes. They addressed the board functioning and composition, thus deciding to be directly involved in running the business, but clearly shaping specific tasks, with the aim of identifying their appropriate contribution to develop value creation. All of them had previous experience in RCF before the US company acquisition. Mr Macchiaverna as a consultant, Mr. Vicari and Mr. Morlini as owners and director or CEO, but only when the current ownership identity was established were they able to create conditions for such a relevant success. Mr Vicari previously became owner and served as a CEO, from 1995 to 1998, because the lack of shared strategic goals and conflicts regarding power allocation among the current owners required a discontinuity to overcome a strategic stalemate. He realized a fast growth with superior performance, but nonetheless the current owners opposed his further investments projects and strategies to further development. Following conflicts led to the U.S. company take over, and in a few years, to crisis. Data show how ownership, representing the ultimate decision maker, holds a crucial role in addressing the firm's strategic orientation, by its direct involvement or by legitimizing the board or the CEO behaviour. Family firm boards are typically dominated by family directors (Voordeckers, Van Gils & Van den Heuvel, 2007), hence owners may further condition board activities and performance, providing a conclusive help or obstacles for going through organizational life cycle stages. These arguments support the following proposition.

Proposition 2: In a family firm, ownership is the main contingency affecting the firm's long term goals and strategic decision making, thus conditioning its going through organizational life cycle stages

Absorptive capacity exerted a key role in enabling RCF to overcome its crisis and then pursue value creation by developing dynamic capabilities. When the current dominant coalition took over RCF, its products were suffering from technological obsolescence and their market price was much too high, because of inefficiencies, especially arising from its excessive and unjustified size. Working in a sound transmission industry, technological obsolescence was a main concern, also because designing and developing innovation may require two years before realizing a new product. In the previous years, R&D in RCF was not effectively addressed by the U.S. company and even if it maintained high level competences on the electromechanical side, the electronics was inadequate, leading to badly working products. Mr. Vicari identified a key resource for addressing strategic change in digital technology applied to professional loudspeakers, but neither was it currently available in RCF, nor was the required knowledge consistent with internal competences. Hence, absorptive capacity bridged the gap by the acquisition of high technology in digital electronics from an small external company, named A&B and also owned by Mr. Vicari, but previously a rival of RCF. In previous years A&B had developed and realized many highly innovative projects, but it was unable to exploit their potential value, mainly because they lacked a brand name allowing market positioning. Therefore, acquiring some of these projects which provided highly specialized electronics then adapted to RCF loudspeakers, RCF was able realize highly innovative new product in a short time. Consequently, new high level electronic systems were not simply transferred to RCF products, but united with its existing resource base, RCF designed highly innovative products by a well performing adaptation of its specific knowledge in electro-mechanics and the specific knowledge provided from A&B in digital electronics. Designing and realizing its product as a whole, RCF obtained continuously radical innovations ensuring superior performance and competitive advantage. Indeed, with the exception of two players, all its competitors within industry hold internally just one out of two technologies, usually buying the other one, but designing their products on the basis of the internal one. Consequently, their products systematically under-perform if compared with RCF's. Furthermore, due to the well-established partnership with A&B, RCF gain new specific-knowledge, allowing a high rate of unique product innovation continuously sustaining competitive advantage. These arguments support the following proposition.

Proposition 3: In the transition from a state of crisis, absorptive capacity may accelerate changes in the firm's strategic positioning enabling value creation strategies.

When the current dominant coalition took over RCF, with the purpose of overcoming the state of crisis, a radical organizational restructuring was required. The firm's size became redundant when managed by the US company, mainly because of a lack of internal communication and coordination between the US top management and RCF. The brand name was neglected and almost disappeared from the market because RCF was substantially managed as an externalized unit of the holding company. In this way, even the efforts of the R&D activities were unclearly addressed, originating under performing products, but high production costs penalizing the firm's competitive positioning. On the other hand, the RCF management was well skilled and electro-acoustic technology maintained a high level of innovation. Then, when Mr. Vicari started to run the business as the new CEO he first carried out a robust downsizing which allowed resources selection to improve efficiency. Then, on the basis of his previous experience, he addressed commercial management efforts to rebuild access to the market and he directed R&D goals. Developing new, well functioning products was consistent with enhancing the RCF brand name, thus improving its market positioning. New managerial tools and techniques were introduced and increased internal communication allowed sharing knowledge and goals within the firm. New organizational routines were established, increasing both the firm's efficiency and its ability to identify and to exploit new market opportunities, then addressing the development of new products which obtained high success and sustained fast growth. Thus, our data reveal how discontinuity stemming from a new CEO initiated the development of new dynamic capabilities sustaining the firm's value creation. In formal terms:

Proposition 4: In the transition from the state of crisis, a new CEO may promote value creation strategies by renewing the firm's dynamic capabilities.

6. Discussion

The aim of this study was to investigate conditions influencing the effectiveness of the corporate governance practices, according to strategic challenges affecting a family firm when moving through its organizational life cycle. This research addressed the topic by applying corporate governance theories to the context of family firms and responding to recent calls for improved theoretical pluralism and for developing knowledge on contingencies affecting corporate governance mechanisms and processes (Huse, 2005; Filatotchev, 2007). In this way, this research also aimed to provide useful insight from family business research, suggesting extensions or elaborations enriching in return corporate governance theories (Zahra and Sharma, 2004:336).

Findings challenge well established universal perspectives, showing how corporate governance and the firm's strategic behaviour are interlinked, thus suggesting that corporate governance practices should be differently established to fit with the firm's strategic dynamics. The mutual interplay between corporate governance practices and the firm's strategic dynamics are most evident when considering transitions through the organizational life cycle. Changes in the firm's strategic needs enhance evidence on required adaptations in the corporate governance structure and mechanisms to improve conditions for the firm's survival and profitability. Focusing on the threshold from a state of crisis to a renewed growth, as in the case we studied, the necessary radical changes and their impact on the firm's strategic positioning and performance should be most evident.

A first insight emerging from this study is that variations in the established corporate governance practices may represent a powerful antecedent to address strategic change, but their impact depends on the effectiveness of the emergent system of corporate governance as a whole, more than on individual and specific mechanisms. The firm's system of governance refers to an established and reinforcing bundle of authority relations, norms of legitimacy and incentives (Gedajlovic *et al.*, 2004) structuring decision making rules, rights and responsibilities among the key stakeholders involved, as well as their relationships. The resulting system may be appropriate or inadequate to fit with the firm's strategic requirements, but within it individual mechanisms are interdependent, thus originating potential complementarities, substitution effects or conflicts (Rediker and Seth, 1995; Brunninge *et al.*, 2007). In a family firm, the effectiveness of the corporate governance practices may concern settling relationships among the dominant coalition of families holding the firm, as well as their involvement in governance and managerial roles. The case I studied emphasizes the crucial role of ownership when addressing the firm's strategic challenges and it sheds light on ownership as the ultimate decision maker (Carney, 2005), because of the owners preferences which may be consistent or contrasting with the firm's strategic dynamics. Mr. Vicari, as owner and serving as CEO, gets a decisive support to his strategic leadership from the current members of the ownership structure which usually validates his leadership. In his previous experience as owner and CEO in RCF, he also obtained high performance and growth, but because of differing and contrasting preferences among the past owners, he was induced to renounce developing further growth strategies. It may address not a matter of ownership structure, but it refers to ownership composition and its subsequent strategic goals, pointing out implications from the ownership identity on the firm's long term goals.

A further contribution of this study refers to how family specificities may influence those strategic activities enabling a family firm to sustain value creation over time (Salvato and Melin, 2008). The family members absorptive capacity was identified as a prominent source of the firm's competitive advantage, providing a certain resource heterogeneity the firm then developed into dynamic capabilities to realize its value creation strategies. Relationships between members of the dominant coalition of families controlling RCF and external clients and suppliers allowed a fast rebuilding of the firm's commercial network and provided decisive technologies to design high quality products in a short time. Knowledge acquired from clients and suppliers contributed to new products development which may require inputs of relevant complementary knowledge, such as market or design, often possessed by other firms (Danneels, 2002). Furthermore, owners' prior knowledge represented a source of potential absorptive capacity and enabled the firm to increase the depth of relation-specific knowledge, then increasing the potential for further innovative combinations (Zahra and George, 2002).

Absorptive capacity may enable firms facing strategic challenges to combine external knowledge with internal competences, and successfully exploiting them to perform value creation strategies (Hitt *et al.*, 2001; Zahra and George, 2002; Zahra *et al.*, 2009). This study points out how a relevant portion of absorptive capacity may reside in the family members' differing competences and relationships and, because of their involvement in corporate governance roles and processes, they may represent a considerable source or attribute of the competitive advantage embedded in a family firm (Carney, 2005). In the case I studied, as an example, the board, and especially the CEO, addressed the firm's ability to learn how to develop and use new knowledge, creating routines and skills that generated dynamic capabilities, such as realizing continuous innovative products, and applied them quickly to develop value creation (Zahra and George, 2002). Therefore, the development of corporate governance processes and strategic flexibility required by value creation are interlinked, thus suggesting that corporate governance practices may be designed strategically. The development of dynamic capabilities relies on bundling the firm's resource base and linking them to appropriate firm-specific routines reflecting the unique organizational context in which they emerge. Flexibility needed to challenge strategic dynamics may require an appropriate degree of organizational learning, questioning the effectiveness of the corporate governance system to lead to changes necessary to the firm's repositioning. Key actors in the governance system provide differing knowledge and skills and these differences may influence managerial priorities, decision making and, finally, how the firm creates and leverages its capabilities to develop value creation.

7. Conclusions

In this study, I investigated relationships between corporate governance practices and strategic dynamics in the context of family firms. I analyzed the case of RCF, an Italian firm owned by a dominant coalition of families, which shifted over the last years, from crisis to a renewed growth. Its experience represents an interesting example showing how changes in its strategic orientation and in its corporate governance system are integrated, leading to a deeper evaluation of contingencies influencing the effectiveness of a corporate governance system. I identified relevant relationships between corporate governance mechanisms and strategic challenges that are supported by case data, then addressing a process view to challenge the investigated topic.

This study aims to develop knowledge at the intersection of corporate governance and family business research, considering the role of family specificities in the mutual interplay between corporate governance practices and strategic dynamics. This stream of research promises to advance knowledge in a contextual approach to corporate governance, but it also has implications for an appropriate design of corporate governance practices in family firms.

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