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Exploring the role of psychological ownership towards organizational innovation in family businesses

Abstract

Purpose - The purpose of this study is to understand the interplay between psychological ownership and organizational innovation in family businesses. The research also explored the mediating effect of knowledge transfer alongside the moderating role of governance practices.

Design/methodology/approach - A total of 116 family businesses across India took part in the study. The data was collected with the help of a structured questionnaire supplied to the senior most family member of the firm. The data was analyzed using the moderated mediation model analysis in R.

Findings - The findings indicate that psychological ownership is a key driver of organizational innovation in the family businesses. The transfer of knowledge mediates the relationship between psychological ownership and organizational innovation. Moreover, governance practices of the businesses moderate the association between psychological ownership and knowledge transfer, and its downstream consequences on organizational innovation are also found to be pronounced.

Originality/value - While previous research has explored various aspects of nurturing innovation, the present study explores the effect of psychological ownership in the context of family businesses in India. This study also gives insights on how knowledge transfer and governance practices work together to influence innovation in these businesses.

Keywords - Psychological ownership, Knowledge transfer, Innovation, Governance practice, Family business, Moderated mediation.

Paper Type - Research Paper

Introduction

Family businesses are managed by a single or a small group of close-knit families who shape the actions and culture within these businesses (Ediriweera *et al.*, 2015). Approximately 90% of businesses in the world are either owned or controlled by families which makes family businesses a dominant form of organization globally (Alderson, 2012). With the rise of family businesses, research in this field is also expanding as it is recognized as a crucial area of study. The number of family businesses is on the rise, studies have also been growing as is considered an important area of research (Evert *et al.*, 2016; Rovelli *et al.*, 2022; Xi *et al.*, 2015) Family involvement in business (Rachmawati *et al.*, 2022; Revilla *et al.*, 2016), role of board (Bansal, 2021; Rubino *et al.*, 2017), and firm performance (Pindado and Requejo, 2015; Ratten *et al.*, 2023) are the areas that are given substantial focus in the previous literature on family business, there is a great scope of research in different concepts and contexts. Firms must actively embrace innovation to ensure their survival and sustained value creation (Arekrans *et al.*, 2023; Rubio-Andrés and Abril, 2023). However, family businesses often face difficulty in overcoming their inherent resistance to change to stay relevant in the evolving marketplace (Lorenzo *et al.*, 2022; Steeger and Hoffmann, 2016). The owners have heightened emotional investment and commitment which contribute to increased organizational innovative capacity in family businesses (Goel *et al.*, 2012). Psychological ownership refers to the subjective experience of possession or an internal sense of connection to an object that is independent of legal or formal ownership rights (Pierce and Peck, 2018). The presence of psychological ownership in the context of family businesses fosters the emergence of a stewardship mindset towards the organization's well-being and long-term sustainability (Henssen *et al.*, 2014). Organizational innovation in the family businesses is associated with its research and development (R&D) efforts as well as its capacity to revamp its internal and external arrangements (Broekaert *et al.*, 2016).

The organizational process of knowledge transfer in the family-owned organizations serves as a key mechanism for facilitating the development of a stewardship orientation (Hadjielias *et al.*, 2021). Governance practices are linked to organizational goals, board meetings and routine conduct play a decisive role in making the family businesses effective (Fahd-Sreih and El-Kassar, 2018). The present study aims to examine how psychological ownership shapes the organizational innovation of family businesses. This study also examines the moderating and mediating effects of governance practices and knowledge transfer respectively. The study also draws insights from the agency theory and stewardship theories. Agency theory examines how family businesses with differing objectives can effectively govern the business through contracts, monitoring, and incentive structures to mitigate conflicts of interest in the best interest of the business (Bosse and Phillips, 2016). Whereas, in stewardship theory, trust and shared values are crucial in promoting collaboration and effective decision-making in family businesses (Eddleston *et al.*, 2012). There is a dearth of studies that have studied the domain especially in the context of family businesses in India. The present study seeks to improve knowledge of organizational innovation in family businesses, aiming to fill a notable gap in existing literature and contribute to both theoretical knowledge and practical applications. This area remains underexplored in the Indian context, despite the significant role family businesses play in the country's economy as they constitute 35% of the large businesses in India (Mani, 2021). The proposed research framework is shown in Figure 1.

Figure 1. Research framework

Theoretical Background and Hypotheses Development

Agency theory and stewardship theory

The two prominent theoretical perspectives related to the dynamics of family businesses and their governance structures that have gained attention in the literature are stewardship theory and agency theory. Family businesses face distinctive challenges in terms of governance and agency problems. Agency theory remains a valuable tool for understanding and addressing agency problems in family businesses. According to Jensen and Meckling (1976), agency theory asserts that principals (owners) and agents (managers) have different risk preferences and opinions which often lead to potential conflicts of interest. Family members in management positions may engage in transactions which are beneficial to themselves but detrimental to the business (Chrisman *et al.*, 2012) and resist appointing non-family members in management positions leading to inefficiency and stagnation (Gomez-Mejia *et al.*, 2001). Moreover, favoring family members in terms of employment, promotions, and compensation can demotivate non-family employees and hinder talent acquisition (Mishra and Kapil, 2017). To mitigate these agency problems, family businesses can establish independent boards of directors and professional management teams with clear succession plans which can reduce conflicts of interest (Berrone *et al.*, 2022). The presence of shared value frameworks and communication channels will help to align family interests with firm goals (Kotlar and De Massis, 2013).

Stewardship theory offers a distinct perspective on governance and decision-making in family businesses in contrast with the agency theory. Stewardship theory states that family members act as stewards who are driven by a sense of responsibility and commitment to the well-being and continuity of the business (Davis *et al.*, 1997). It emphasizes the importance of trust and collaboration among family members in decision-making processes (Keay, 2017). According to Anderson and Reeb (2003), stewardship-oriented governance structures in family businesses focus on fostering a sense of shared purpose and responsibility that contribute to the overall effectiveness of the organization. Steward-leaders focus on the long-term sustainability of the business and are inclined to invest in innovative practices in response to changing market conditions (Kellermanns *et al.*, 2008). A study by Chrisman *et al.* (2002), found that stewardship-oriented family firms tend to outperform others in terms of long-term financial stability and adaptability. This highlights the positive impact of stewardship behaviors on overall business outcomes. Despite the positive aspects, stewardship theory acknowledges potential challenges. Sharma *et al.* (1997) identified the risk of agency problems within family businesses, where conflicting interests among family members may undermine stewardship principles.

Researchers have recognized the complementary nature of stewardship and agency theories with each other in understanding the family businesses. While family members may act as stewards, certain agency problems cannot be ignored. A balanced approach that incorporates elements from both theories provides a more effective management of family businesses (Chrisman *et al.*, 2010). Thus, integration of stewardship and agency theory will help the family businesses to adapt according to the prevalent business contexts.

Psychological ownership and organizational innovation

Family businesses contribute significantly to employment and economic growth (Mani, 2021). The understanding of the factors which influence innovation within family businesses is crucial for sustaining their competitive advantage (De Massis *et al.*, 2016). In the context of family-owned business, psychological ownership manifests as the owners' feelings of attachment, control, and responsibility towards their work and the organization as a whole (Pierce and Peck, 2018). Psychological ownership has gained attention in recent years as a potential catalyst for innovation within family businesses. Psychological ownership in family businesses is linked to organizational innovation as it fosters deeper commitment and encourages stakeholders to take risks with innovative ideas (Rau *et al.*, 2019). The presence of high levels of psychological ownership in the organization contributes to successful new product development initiatives (Gray *et al.*, 2020). When individuals feel a personal stake in the success of these family businesses, they are more likely to engage in proactive behaviors that drive innovation (Cennamo *et al.*, 2012). Psychological ownership is also linked to improved financial performance and overall success of family businesses (Sieger *et al.*, 2013). Moreover, a strong sense of psychological ownership in the organization can encourage employees to identify and implement improvements in the business's operations and processes (Avey *et al.*, 2009). In family businesses, when roles and communication are clear, psychological ownership gets strengthened but conflicts or confusion can weaken it (Nicholson and Björnberg, 2008).

Hypothesis 1. Psychological ownership is positively related to organizational innovation in family businesses.

Mediating role of knowledge transfer

In the context of family-owned firms, knowledge sharing is a critical process that facilitates the transfer of tacit and explicit knowledge within an organization (Pittino *et al.*, 2018). Knowledge sharing is the practice of making information accessible to others within the organization to enhance decision-making, foster innovation, and improve overall performance (Gerpott *et al.*, 2020). As the relationships are often deeply rooted in family businesses, this makes the understanding of dynamics of knowledge transfer becomes pivotal (Chirico and Nordqvist, 2010). The process of transferring knowledge through open and transparent communication channels facilitates the exchange of innovative ideas and ensures that the sense of ownership translates into tangible contributions to the organization's innovation efforts (Gedajlovic *et al.*, 2012). The effective sharing of knowledge enhances the ability to adapt to changing environments and fosters a culture of continuous learning in family businesses (Berrone *et al.*, 2022). Pittino *et al.* (2018) found that psychological ownership positively impacts knowledge sharing, which in turn fosters stronger entrepreneurial orientation in family businesses. A sense of psychological ownership in family businesses has a favorable influence on knowledge sharing that creates a conducive environment for innovation and long-term success (Hameed *et al.*, 2019). Knowledge transfer enhances the innovative capabilities of family businesses by promoting a collaborative and open communication environment that contributes to the generation and implementation of innovative ideas (Hernández-Perlines *et al.*, 2019). It is also found that knowledge sharing improves performance through the integration of diverse knowledge bases and fostering strategic decision-making processes that make the family businesses more adaptable and competitive in the market (Sirmon and Hitt, 2003). The transfer of knowledge helps bridge the generation gap by transferring tacit knowledge and experience from senior family members to their successors (Chua *et al.*, 2003). This ensures not only the continuity of the family businesses but also contributes to the development of capable future leaders. Although the majority of studies found the benefits of transferring knowledge in family businesses, challenges also exist. These organizations also struggle to effectively transfer knowledge due to the prevalent trust issues, confidentiality concerns, and resistance to change (Eddleston *et al.*, 2012).

Hypothesis 2. Knowledge transfer mediates the positive relationship between psychological ownership and organizational innovation.

Governance Practices as Moderators

The presence of efficient governance practices helps to direct the positive impacts of psychological ownership towards organizational innovation while maintaining a balance between autonomy and accountability (Ward, 2011). In family businesses, governance practices refer to the systems and policies that govern decision-making and management to navigate the complex relationships between family members and non-family members (Hall and Nordqvist, 2008). The governance mechanisms, such as regular board meetings, and strategic planning, act as moderators for the family businesses towards its long-term objectives (Eddleston *et al.*, 2008). Poletti-Hughes and Williams (2019) opined that the presence of efficient governance practices mitigate the potential conflicts between family priorities and business objectives that leads to improved performance. It is found that family businesses with transparent and decentralized governance practices are more creative and innovative (Scholes *et al.*, 2021). Also, robust governance practices enhance long-term planning and responsible resource management which promote sustainability of family businesses (Berrone *et al.*, 2012). The open communication channels encourage effective governance practices that increase trust and foster collaboration within the family businesses (Hadjielias and Poutziouris, 2015). Effective governance practices establish clearly defined roles and responsibilities which ensure efficient management and hold individuals accountable for their actions (Ward, 2011). These clearly defined policies and procedures prevent favoritism and ensure that non-family employees perceive a fair and equitable working environment which contributes to overall organizational cohesion (Podvorica and Murati, 2023). In other words, effective governance mechanisms can align the diverse interests of family members and other stakeholders that drive collective action towards shared goals (Berrone *et al.*, 2010).

Hypothesis 3. Governance practices moderates the positive relationship between psychological ownership and knowledge transfer in a way that it is stronger when governance practices are low in family businesses.

Hypothesis 4. The indirect relationship between psychological ownership and organizational innovation through knowledge transfer is moderated by governance practices in a way that it is stronger when governance practices are low in family businesses.

Research methodology

Design and participants

This study gathered data from family members involved in the management of family businesses based in India. The questionnaire was mailed to 160 randomly selected firms linked to the Confederation of Indian Industry-Family Business Network India Chapter (CII-FBN). A cover letter along with the questionnaire explained the research aim and assured participants about complete confidentiality. A total of 123 out of 160 invited family businesses responded to the survey, and of those, 116 complete responses were included in the final analysis (response rate = 76.87 %). The questionnaire included demographic questions about respondents and inquiries about the age and size of these family businesses.

Measures

Psychological ownership was assessed with the five-item scale adopted from Pittino *et al.* (2018). An example item was "We perceive the firm as part of the family." The Cronbach's alpha value of the scale was .86. The items were evaluated using a 7-point Likert scale ranging from 1 (strongly disagree) to 7 (strongly agree).

Knowledge transfer was evaluated with the six-item measure adapted from Bartol *et al.* (2009) and an example item was "We readily pass along information that may be helpful to the work of the firm." The Cronbach's alpha value of the scale was .92. The items were evaluated using a 7-point Likert scale ranging from 1 (strongly disagree) to 7 (strongly agree).

Organizational innovation was measured with the three-item scale adapted from Eddleston *et al.* (2008). An example item was "Our firm has spent heavily on research and development." The Cronbach's alpha value of the scale was .89. The items were evaluated using a 7-point Likert scale ranging from 1 (strongly disagree) to 7 (strongly agree).

Governance practices were evaluated with the three-item scale adapted from Fahd-Sreih and El-Kassar (2018). An example item was "Do you hold regularly scheduled meetings with family members involved in the business?" The Cronbach's alpha value of the scale was .84. The items were analyzed using a binary scale ranging from 0 (No) and 1 (Yes).

Data analysis

The statistical software R was used for the comprehensive exploration and interpretation of the dataset (R Core Team, 2021). The gathered data was explored through the application of descriptive statistics, correlation analysis, and moderated mediation analysis. The examination of the moderated mediation model involved the application of the PROCESS macro for R to analyze complex mediation and moderation relationships of the hypothesized model (Hayes, 2020). The PROCESS macro uses bootstrapping technique to estimate effect sizes and test hypotheses without normality assumptions (Hayes, 2020).

Results

Preliminary Analyses

The data used in the study indicated that 37.93% of participants are in the position of either Director or Chairman and the remaining 62.06% occupied senior-level managerial roles. Also, 71.55% of the participants were below 50 years, and 28.45% were above 50 years. The majority (80.17%) of respondents were male, with 75.86% holding a bachelor's degree and 24.13% having a master's degree. Among the participating family businesses, 93.97% had fewer than 100 employees, and 6.03% had more than 100 employees. Table I shows the demographic information of the participants in detail.

Table I. Demographic information (n = 116)

The descriptive statistics and correlation coefficients for all the study variables used in the study are presented in Table II. It is found that all pairwise correlations were statistically significant. A strong positive correlation was found between psychological ownership and both knowledge transfer and organizational innovation (r = .60 and .64, respectively, p < .01). Moreover, knowledge transfer itself was significantly associated with organizational innovation (r = .66, p < .01). Interestingly, a negative but significant correlation was observed between organizational innovation and governance practices (r = -.25, p < .05). Hence, there is a presence of moderate correlations among the variables. The author further assessed potential multicollinearity by examining the variance inflation factor (VIF) values. The VIFs ranged from 1.03 to 1.60 indicating no significant concern for multicollinearity (Kim, 2019).

Table II. Descriptive statistics and inter-correlations

Hypotheses Testing

As can be seen in Table III, psychological ownership had a significant and positive effect on organizational innovation (β = .62, p < .01). Thus, *Hypothesis 1* was supported.

Table III. Overall effect of path coefficient

With regard to the mediation hypothesis (shown in Table IV), the findings showed a significant and positive effect of psychological ownership on knowledge transfer (β = .60, p < .01), which in turn had a significant and positive effect on organizational innovation (β = .40, p < .05). As can be seen in Table IV, the indirect effect of psychological ownership on organizational innovation via knowledge transfer was also significant (β = .25, p < .01). Together, these results support *Hypothesis 2*.

Table IV. Direct and indirect effects of path coefficients (Mediation analysis)

Regarding the moderating role of governance practices on the relationship between psychological ownership and knowledge transfer (shown in Table V), findings showed a significant but negative moderation effect (β = -.15, $p < .05$). Authors further inspected the simple slopes at one SD above and below the mean of the moderator. The results showed that the relationship between psychological ownership and knowledge transfer was weaker at higher levels of governance practices (β = .30, $p < .05$), whereas it was stronger at lower levels of the governance practices (β = .79, $p < .01$). In other words, the association between psychological ownership and knowledge transfer found to be weaker with stronger influence of governance practices as shown in Figure 2. Taken together, these findings support *Hypothesis 3*.

Figure 2. Governance practices as moderator

Table V. Moderation and simple slope estimates

From Table VI, the existence of the statistically significant moderated mediation index, β = -0.07, 95% percentile CI [-0.13, -0.02], provided strong evidence for the moderated mediation model in the study. The results showed that the strength of the indirect effect of psychological ownership on organizational innovation via knowledge transfer was conditional upon governance practices. It was significantly stronger when the degree of governance practices was low compared to when it was average and high. From Table VII**,** results showed a significant a-path from psychological ownership to knowledge transfer, β = 1.12, $p < .01$. There was also significant interaction between knowledge transfer and governance practices for the b-path, β = 1.01, $p < .01$. The direct effect c' from psychological ownership to organizational innovation was also moderated by governance practices, β = 0.37, $p < .01$. Figure 3 shows a clear picture of the complex relationship between the variables. Taken together, *Hypothesis 4* was supported.

Table VI. Conditional direct and indirect effects

Table VII. Summary of results of moderated mediation analysis

Figure 3. Statistical model for moderated mediating effects

Discussion

The present study was conducted to address the need for research integrating psychological ownership with family businesses, with the aim of examining its impact on organizational innovation. This study proposed a blended model with moderated mediation that evaluated the relationship between psychological ownership felt by owners and the organization's innovation levels. The influence of psychological ownership on organizational innovation is hypothesized to be mediated by knowledge transfer. Furthermore, the study considered organizational governance practices to moderate this indirect relationship. The findings aligned with the predicted outcomes that highlighted the significance of psychological ownership as a catalyst for organizational innovation. The present study investigated the positive organizational outcomes of psychological ownership in family businesses which enrich the limited literature available in the Indian context. Psychological ownership promotes innovation in the organization. It also positively influences the transfer of knowledge in the organization, which in turn also affects the degree of innovation in the organization. The present study established knowledge transfer as a key intermediary that elucidates the association between psychological ownership and driving innovation in the organization. The findings of the study align with the results of Avey *et al.* (2009), Gray *et al.* (2020) and Pierce and Peck (2018) where fostering a sense of psychological ownership among the owners lead to improved organizational innovation in specified contextual environments. While most studies have found psychological ownership often fosters creativity and initiative, there are certain conditions that can also hinder its contribution to innovation. Excessive psychological ownership in the organization can lead owners to become overly attached to their own ideas and hinder collaboration which is crucial for innovation (Cocieru *et al.*, 2019). A strong sense of ownership can breed resistance to external feedback or organizational restructuring, even if beneficial for innovation (Pierce *et al.*, 2003). Also, owners with inflated feelings of ownership may prioritize their own pet projects over initiatives aligned with broader organizational goals, leading to inefficient innovation efforts (Cocieru *et al.*, 2019).

The results showed that when there is strong support for innovation from leadership, collaborative culture, and open communication channels, it can mitigate the negative aspects of psychological ownership. The presence of psychological ownership influenced organizational innovation through knowledge transfer with the advent of governance practices. Governance practices have a strong influence on the association between psychological ownership and knowledge transfer in the organization. In the present study, the indirect relationship of psychological ownership with organizational innovation through knowledge transfer was found to be stronger when governance practices have lower influence. This result was overwhelming, given the nature of family businesses in India where strong psychological involvement of owners lead to higher levels of knowledge transfer and innovation in the business. However, when there is too much emphasis on the governance practices, it hampers the knowledge transfer. The characteristics of the findings are such due to the use of a sample size comprising mostly the smaller and medium sized family businesses in India. Psychological ownership drives a sense of autonomy and confidence which encourages individuals to experiment with new ideas and knowledge combinations (Pierce *et al.*, 2018). They feel responsible for the success of their "owned" tasks or ideas that lead to a greater willingness to share knowledge with others to improve them. In other words, psychological ownership positively influenced knowledge sharing, which in turn significantly enhanced innovative behavior in complex management systems (Mahsud *et al.*, 2022). Although psychological ownership is a key driver of knowledge transfer, its effectiveness depends on the context. Governance practices play a crucial role in shaping this context by establishing rules and procedures that guide knowledge sharing behavior in organizations (Szulanski *et al.*, 2003). The presence of rigid rules and procedures hinder knowledge transfer by creating bureaucratic hurdles and discouraging informal communication. However, a moderate level of formalization can create a structured environment that facilitates knowledge exchange (Easterby-Smith *et al.*, 1999). Open communication and information sharing build trust and result in knowledge transfer. A lack of transparency often creates uncertainty and hinder collaboration (Alshwayat *et al.*, 2021).

Theoretical and practical implications

This study addresses a critical research gap and offers valuable insights for both theory and practice through its focus on family businesses in India. This study examines the need for synergizing diverse viewpoints to achieve organizational innovation in this context (Yin *et al.*, 2023; Zahra *et al.*, 2004). It actively explores the connection between psychological ownership and innovation, illuminating both the essence and its subsequent impacts, and thereby enriching the understanding about organizational innovation. This research uniquely identifies the aspects of psychological ownership that shape organizational innovation and contribute valuable insights not found in existing literature. This study addresses the crucial need to understand the contextual influences on the psychological ownership-innovation relationship by employing a comprehensive model that investigates mediating and moderating mechanisms. It reveals how these factors can amplify or diminish the connection between the stated relationship. This research, which is based in India, enriches the family businesses literature, which has traditionally been about developed countries. This expands the understanding of family businesses beyond that context and illuminates their diverse dynamics in developing economies.

Organizations that foster psychological ownership and knowledge transfer enhance their attractiveness to potential employees that increase their likelihood of being perceived as an employer of choice. Also, organizations turn into fertile ground for innovative ideas to flourish, making them magnets for creative talent. These findings pave the way for organizations to design and implement initiatives that effectively combine psychological ownership with knowledge transfer that can lead to higher rates of innovation. This research underscores the need for effective corporate communication in the organization that highlights its dedication to strong governance and leadership. The study found that there are significant advantages of transparent communication regarding the organization's innovation goals associated with small and medium-sized family businesses. The presence of sound governance practices gives organizations a competitive edge in terms of innovation. The organizations promoting innovation are likely to have efficient mechanisms for knowledge transfer for better results (Gedajlovic *et al.*, 2012; Hernández-Perlines *et al.*, 2019). The study has implications for even those organizations that put more stress on its governance practices. The knowledge transfer process in those organizations often gets hampered. This study's investigation of the interplay between psychological ownership and innovation pinpoints crucial factors that influence their connection. These insights highlight the importance of cultivating psychological ownership to effectively foster knowledge transfer and drive innovation within organizations.

Limitations and future research

The research encompasses certain limitations that offer valuable insights for prospective investigations. The findings cannot achieve causality due to the use of cross-sectional nature of the data that focuses primarily on small to medium-sized family businesses in India, organizations are advised to use these findings with discretion. Subsequent investigations could enhance the current study by employing a larger sample size in diverse settings, thereby providing more comprehensive results. The generalizability of the study's conclusions is impacted by the relatively small sample size. Future research could address this by employing more statistically robust samples, incorporating a broader spectrum of family-owned business sizes and industries. The author employed an experimental design to increase confidence in the causal relationships between the variables used in the study. However, it relied on a self-report survey that has concerns about common method bias due to the single data source (Podsakoff *et al.*, 2003). The survey used in the study was designed to minimize the risk of method bias by intermingling the questions related to different measures. Furthermore, ensuring anonymity in the survey was aimed at minimizing the potential for social desirability bias (Kreuter *et al.*, 2008). Also, beyond organizational innovation, it is crucial to explore alternative psychological processes that may mediate the impact of knowledge transfer within family businesses like organizational support, creativity, family involvement among others. Therefore, investigating moderators beyond formal governance mechanisms, such as individual personality traits or team dynamics, could shed further light on the contingent nature of the psychological ownership-innovation relationship in the context of family businesses.

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