

Cultural Origins of Business Formation

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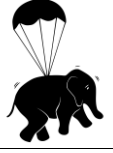
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Abstract

This paper presents a conceptual framework connecting historical kinship structures and generalized trust into modern business formation. Kinship intensity, defined as the degree of strength in family ties, is shaping the social and economic outlook of societies. Building upon the existing literature, I argue that societies with strong kinship ties often exhibit collectivist characteristics, leading to less trust towards outsiders. This hinders market efficiency and collaborative partnerships, resulting in business formation being largely confined to family-owned enterprises. Conversely, societies with loose kinship structures exhibits higher level of generalized trust that enable to promote engagements beyond family networks. This promotes establishing larger firms with strangers, more efficient markets, and greater cooperation with foreign firms. The paper suggests that kinship and trust behavior are deeply rooted in culture and influence social and economic development. It is important for policy-makers to support initiatives that foster trust beyond family ties to promote collaboration among diverse market participants.

Keywords: kinship, generalized trust, family business, market efficiency

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Firma Oluşumunun Kültürel Kökenleri

Öz

Bu makale, tarihsel akrabalık yapılarını ve toplumsal güveni modern iş organizasyonu ile ilişkilendiren kavramsal bir çerçeve sunmaktadır. Aile bağlarındaki güçlülük derecesi olarak tanımlanan kan bağları yoğunluğu, toplumların sosyal ve ekonomik görünümünü önemli ölçüde şekillendirmektedir. Mevcut literatüre dayanarak, güçlü akrabalık bağları olan toplumların genellikle kolektivist özellikler sergilediği ve bunun da aile dışı bireylere karşı duyulan güveni azalttığı düşünülebilir. Bu, piyasa verimliliğini ve işbirliğini engelleyerek firma oluşumunu büyük ölçüde aile işletmeleriyle sınırlı kalmasına neden olur. Tersine, zayıf akrabalık yapılarına sahip toplumlar, aile ağlarının ötesinde etkileşimleri teşvik ederek daha yüksek düzeyde toplumsal güven ortamının sağlanmasına imkan verir. Bu durum aile dışı bireylerle firmalar kurmayı, piyasaları daha verimli hale getirmeyi ve yabancı firmalarla daha fazla işbirliği kurulmasını teşvik eder. Bu makale, akrabalık ve güven davranışının toplum hafızasında derin köklere sahip olduğunu ve sosyal ve ekonomik gelişmeyi etkilediğini öne sürmektedir. Politika yapıcıların, çeşitli piyasa katılımcıları arasında işbirliğini teşvik etmek için aile bağlarının ötesinde güveni teşvik eden girişimleri desteklemesi önerilir.

Anahtar Kelimeler: aile bağları, toplumsal güven, aile şirketi, piyasa verimliliği



1. INTRODUCTION

Why do people tend to cooperate? This question receives an enormous attention across various social sciences because the ability to work together around a purpose create social structures that provide benefits for all members. Individuals unite to achieve common benefits such as collective advantages, autonomous states or large profitable companies. In this paper, I conceptualize a framework to explain the origin of cooperative behavior based on the recent literature in cultural anthropology, psychology and economics.

One way to understand how people cooperate around a common purpose is to observe differences across societies. Social psychology and anthropology theories claim that people have evolved moral systems such as religion that favors cooperation (Norenzayan, 2013), societal emotions of loyalty, fairness that promotes to build a group (Haidt, 2012), or even exploit guilt and shame to form cooperation (Boyd et al., 2003). However, these theories do not sufficiently explain the heterogeneity of cooperative behavior in a society that shares the same religious practices along with similar moral codes. Indeed, one could find a few societies from the same geography could share a similar cultural-religious traits and yet reveal different cooperative behavior. Furthermore, it is important to understand the way that societies construct cooperative behavior as it creates valuable economic and social outcomes. For instance, Putnam et al. (1994) argue that there is a social and economic divide between northern and southern Italy due to its historical roots of cooperative institutions. Northern territories were more able to establish civic associations in the Middle Ages, therefore, social capital accumulated in the region is higher than southern Italy. As a result, social capital accumulation reveals different economic institutions in Italy. Historical institutions can help to explain why some societies are more developed than the others (Acemoglu et al., 2001). While there is extensive literature on the economic and social implications of kinship characteristics, the evidence on how kinship indirectly influence the organizational behavior of companies and their ability to engage business activities is limited.

In this article, I attempt to develop a conceptual framework that links historical kinship ties with the modern business formation dynamics. Adopting a holistic approach, the degree of closeness of family ties (kinship) shapes the cooperative structures within a society. Societies with strong kinship enable cooperation within the family circle, whereas loose kinship promotes individuals to cooperate with strangers. As a result, a society's cooperative behavior depends on historical kinship and the trust level of trust towards others in the society. I conjecture that these cultural traits are transmitted to younger generations and influence our institutional and behavioral settings today.

The paper builds a conceptual framework between kinship, trust toward strangers and business dynamics. Societies with strong kinship ties are more likely to establish family businesses due to their low level of trust towards other members of the society. This can be seen as a cultural preference inherited from ancestors that leads to inefficient markets. Lack of trust against other



market players would restrict the availability of information and lead to information asymmetry in the markets. Hence, individuals with a strong kinship background will be reluctant to form a company and/or share market information with strangers. In addition, the outcome of these cultural traits could be larger when firms cooperate with international markets. Strong kinship would restrict the level of trust outside the culture group (outside home country), causing limited cooperation between incumbent firms and foreign firms. Consequently, joint projects and trade relations could be limited over time.

This paper contributes to the relevant literature by providing a novel framework that explores the cultural foundations of organizational behavior. Recent literature examines the role of the institutional environment in entrepreneurial behavior (Dickson and Weaver, 2008; Welter and Smallbone, 2011), firms' performance and size decisions (Kafouros and Aliyev, 2016; Hermelo and Vassolo, 2010; Cordes et al., 2011). However, previous studies have not adequately investigated the origins of institutional development embedded in culture. This paper aims to fill the gap by proposing that kinship is the key foundation of business formation and organizational behavior in firms. This channel can be understood through the mechanism of information asymmetry and generalized distrust against strangers in the market.

2. BACKGROUND

In this section, I provide a review of literature that provide a context to establish three main aspects of the paper's conceptual model.

2.1. Kinship Structure

In this paper, family formations play a central role in the conceptual framework. I define kinship intensity as the strength and depth of family ties and its level of obligations within a society. Recent literature highlights that kinship plays a central role in social and economic life. Henrich (2020) uses kinship to explain why the Western European countries favor individualism, trust in strangers, democracy and consequently achieve economic prosperity. In contrast, societies with strong kinship ties are often associated with collectivist characteristics, lower trust in strangers and authoritarian states.

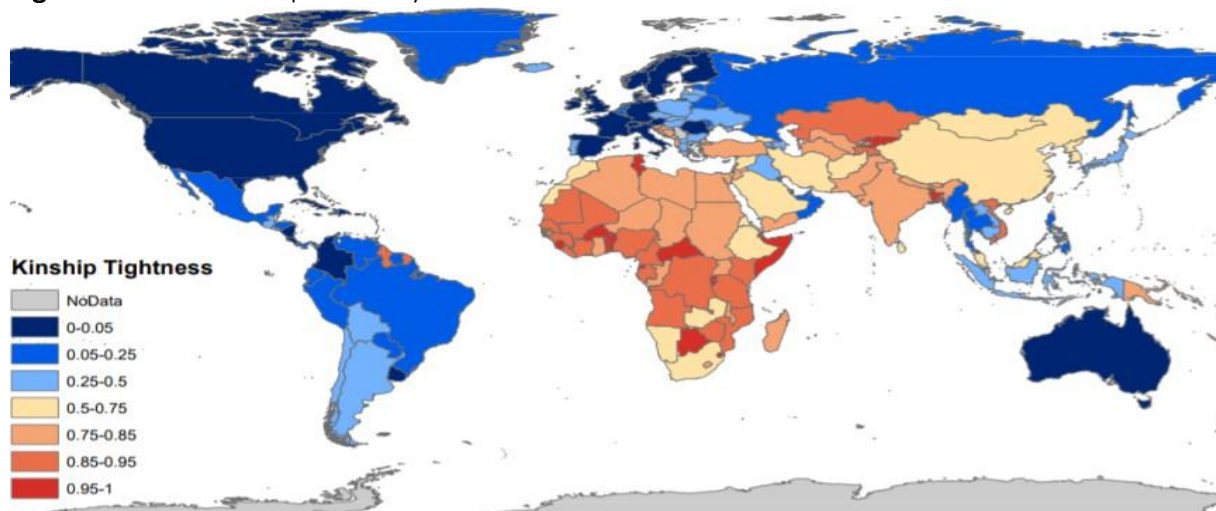
According to the recent body of literature in anthropology, the degree of kinship tightness can be determined by the presence of following indicators: cousin marriage, family size, post-wedding residence, inheritance rules. Firstly, marrying with a cousin can be seen as an incest, and rarely seen in Western societies, while it is a common practice in Middle Eastern countries with around 20% of all marriages (Bittles, 2012). Henrich (2020) suggests that discouraging cousin marriage in the society forces individuals to marry non-relatives, which weakens kinship ties. Secondly, whether having a nuclear family or an extended family influence the kinship tightness. For instance, nuclear family types are predominant in Western Europe causing extended kinship relation dissolves and foster individualism (Enke, 2019). Third, kin-based societies consider that newly wedded couples should live with husband's (sometimes of wife's)



family. This tradition triggers a structural change across societies such as family size, inheritance rules and even political environment (Todd, 1985). Lastly, inheritance rules may be unequal to different genders, which can influence the family structure. Equal inheritance increases extended family ties and discourage children to stay with parents after marriage. After combining these factors, Enke (2019) calculates a kinship score ranging from 0 (low kinship intensity) to 1 (high kinship intensity). It is important to note that these kinship intensity measures are commonly accepted by the existing literature with minor changes due to geographical differences that requires additional measures. Further discussion could be found at Enke (2019) and Henrich (2020).

Figure 1 represents the country-level kinship scores. Countries which exhibit very weak kinship scores are mostly in the Western Europe and in the North America and Australia, representing the developed nations. On the other hand, strong kinship can often be seen in Africa, Central-Southern Asia and the Middle East.

Figure 1. World kinship intensity index



Source: Enke (2019)'s calculations based on the Ethnographic Atlas in Murdock (1967).

Many studies often link kinship scores with various economic and development factors across in cross-country analyses. To provide a brief perspective, I present a visual comparison of kinship and human development, as shown in Figure 1 and 2. Figure 2 exhibits the Human Development Index (HDI) that measures overall achievements of countries in health services, gross education, and GDP per capita. It is widely accepted that HDI is a suitable measure of development because it does not only take into account economic performance but also the overall quality of life.

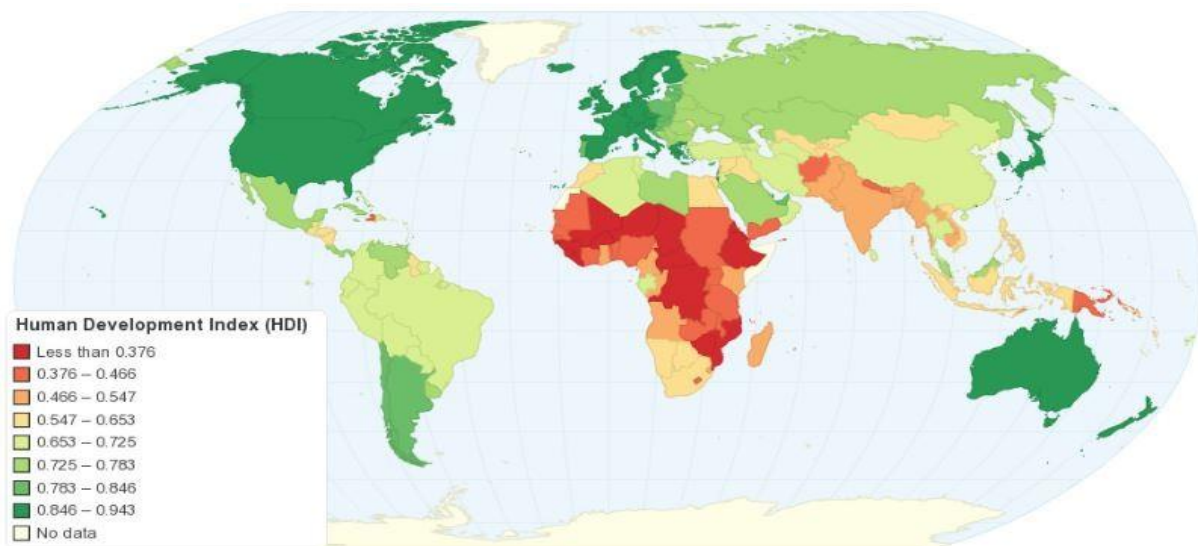
As it can be seen in Figure 1, Henrich (2020)'s argument holds with a few exceptions. Although the pattern is not flawless, countries with weak kinship ties are associated with higher HDI. It is certain that counties with the weakest kinship ties are correlated with highest HDI (vice versa).



2.2. Trust

Trust is one of the mechanisms that determine the connections among individuals. In a social context, generalized trust can be defined as “the expectation that arises within a community of regular, honest and cooperative behavior, based on commonly shared norms, on the part of other members of that community” (Fukuyama, 1995, p.26). Generalized trust differs from individual trust, as it refers to the trust against people outside the social group or family². This behavior helps to create various institutions depending on the level of trust against outsiders. When individuals trust strangers, it is easy to produce public goods and establish more democratic political institutions (Putnam et al., 1994; Banfield, 1958).

Figure 2. Kinship intensity index across the world



Source: United Nations human development reports by (UN, 2012).

A higher level of trust encourages participation in community activities such as political engagement, and reduces cheating patterns (e.g. free-riding, tax evasion, avoiding communal responsibilities). In addition, trust is strongly associated with better socio-economic indicators. Societies with high generalized trust often have better economic performance (Knack and Keefer, 1997; Whiteley, 2000), better political institutions (La Porta et al., 1997; Tabellini, 2010). Greif and Tabellini (2017) explains how different type of generalized trust forms political institutions by comparing Europe and China. In pre-modern period, China has formed a kin-based political organization because of the lack of trust outside family members (low generalized trust). On the other hand, in pre-modern Europe, there are local political institutions that are formed by individuals with no family ties, resulting in open communities promoting cooperation with members outside of family circle. This dynamic evolution causes a great impact on today’s social and political structure. While China follows more authoritarian and collectivist social structure, Europe adopts individual and trusting society.

² Hereafter, I use the terms of trust and generalized trust interchangeably.



2.3. Cultural Persistence

Many studies indicate that cultural traits evolve over time by a transmission from earlier generations to their descendants. Tabellini (2008) highlights that social norms are transmitted across generations, with parents filter out which values to impart to their children. Therefore, cultural norms often have deep roots in history and continue to influence behavior of individuals today. For example, Todd (1985) finds that various family forms in Europe during the Middle Ages determine the key ideological differences. Individuals raised in regions where extended family types are common tend to lean towards communal economical ideologies. Conversely, in regions with nuclear family settings, individualistic behaviors are prevalent because the children leave parental home at a younger age, and they can resist existing cultural norms more easily. According to Todd (1985)'s classification of families, Duranton et al. (2009) find that areas characterized by predominantly nuclear families in the Middle Ages tend to have smaller household size and higher social capital. In contrast, regions that historically dominated by extended family structures have larger household size lower social capital but better in income equality. The cultural persistence is not driven by the geography where people reside. Fischer (1989) shows how British migrants continue to sustain their cultural norms in the USA. For instance, English Protestants who value common order and universal education have established local institutions that promote effective government and education in the Northwestern US states. Similarly, Quakers have emphasized personal freedom, limited government and low taxes in the 17th century in the UK. Indeed, regions with Quaker ancestry continue to reflect these values in the Southern USA today.

Cultural persistence is not limited to kinship intensity or family structures. Deep historical and cultural factors such as institutional characteristics and distance to historical technological innovations play a crucial role on societies' economic development today (Spolaore and Wacziarg, 2013). Even the role of women in a society today has a longstanding correlation with the traditional position of women. Alesina et al. (2013) find that descendants of societies that require greater physical strength led to less female labor participation in the work force today. Gender norms remain persistent over time, even the descendants of those different societies born and raised in the same country.

3. RESEARCH PROPOSITIONS

This research conceptualizes a few propositions to extend the kinship framework into modern innovative applications. In this section, I begin with the framework using Enke's (2019) overlapping generations model. In pre-industrial (pre-modern) period, kinship intensity of societies is not determined by economic development and efficiency. At some point, some societies begin to cooperate outside close-kin because of external factors. For instance, marriage criteria have changed around 400 AD in the Western Europe by the Catholic Church, causing individuals to marry with someone outside kin-group. Such events lead these societies to loosen



the kinship structure over generations. In other societies which do not experience this kind of effect continue to follow traditional marriage practices and cooperate inside the kin-group.

Cooperation with strangers (society members outside the kin-group) requires trust. As explained in Section 2.2, tight kinship societies do not invest trusting behavior against strangers as cooperation already exist within the kin-group. In loose kinship societies, trusting strangers is a necessity because of the need for social interaction due to the limited size of the nuclear family (Moscona et al., 2017). Families with strong family ties have a causal association with lower level of trust (Ermiş and Gambetta, 2010). Therefore, continuous interactions among kinship structure and trust behavior have determined heterogeneous social norms across societies. Co-evolution of kinship and trust relation is embedded in societies, resulting in various economic and social outcomes.

Forming a company requires a lot of effort to build a team of co-founders which gather around the same purpose. It can be challenging, especially during the early stage, due to high uncertainty along with financial risk. Kinship framework can explain the prevalence of family-owned businesses. Some studies evaluate the cultural foundations of family business from a broad perspective (Gupta and Levenburg, 2012; Sabah et al., 2014). However, I conjecture that the essential source of variation in the share of family-formed business formations could be explained by historical kinship patterns.

Proposition 1: Countries with strong kinship ties are more likely to initiate family-run business.

The nature of business formation requires a certain level of trust among co-founders. In strong kinship societies, it is often more suitable to form a company with in-group members rather than with total strangers. This dynamic can shape the entrepreneurial culture by establishing norms that favor family-formed businesses. In fact, a potential mechanism behind this preference may stem from individuals' reluctance to trust strangers. As Moscona et al. (2017) emphasizes, the key difference between trust toward strangers and trust within the family arises from the generally low level of trust toward outsiders. In other words, all communities tend to have high trust in family members, even for strong or loose kinship structures, but the low level of trust in strangers is the main driving force of non-cooperation. Gambetta and Hamill (2005) show that individuals in high kinship societies prefer to cooperate among family members, this affect is also transmitted through generations (Enke, 2019). Thus, members of a strong kinship society are less likely to cooperate or form a business with strangers, suggesting that the organizational structure will be dominated by family-run businesses.

Proposition 2: Loose kinship structure helps to establish more efficient markets.

Akerlof (1970) demonstrates that information asymmetry between buyers and sellers can trigger a reduction in market efficiency, leading to adverse selection where buyers end up with low-quality products. In our context, markets where strong kinship is the norm, restrict market participants from sharing information and interacting with others outside their group. As a



result, the availability of information is limited to certain groups, causing severe information asymmetry. When individuals do not trust one another, trade and collaboration in the market weaken. Other studies find that studies with greater social capital accumulation leads to greater economic development (Knack and Keefer, 1997). This occurs because generalized trust promotes cooperation and economic growth (Whiteley, 2000). The interplay among social capital, trust, and kinship reveals institutional quality. Acemoglu et al. (2001) and Acemoglu and Robinson (2013) suggest that countries with high quality institutions contribute to better economic growth.

The type of information shared among people also differs between family members and strangers. A body of literature on relationship lending in banking indicates that soft information (i.e. subjective, qualitative data often based on relationship) is difficult to categorize and not available for all members in the market (Elyasiani and Goldberg, 2004; Uchida et al., 2012). The abundance of soft information that is available only to certain businesses may cause the market to shrink or even collapse of the market. Hence, weak kinship networks can boost trust among individuals so that cooperation among strangers will be easier. This leads to greater economic development associated with efficient markets.

Proposition 3: Strong kinship emasculates economic development through discouraging greater cooperation between incumbent firms and foreign firms.

Modern corporations were born in Europe. Greif (2006) defines them as corporations that are intentionally created, voluntary, interest-based and self-governed associations. This is no coincidence, especially when loose kinship societies flourish in Europe in the Medieval Ages. As described in Greif and Tabellini (2017), the evolution of family structure contributed to establish corporations to solve problems of conflict and cooperation. These historical institutions have long-lasting effects on the economic development of the counties. Hence, quality of institutions is deeply rooted in kinship structure.

Organizational structure heavily depends on the interrelation of different groups gathering around a common business purpose. Hofstede provide a framework to understand the differences between cultures using power distance, degree of individualism, masculinity, and uncertainty avoidance (Hofstede, 1984; Hofstede et. al., 2010). These behavioral packages shape the way businesses interact and cooperate with each other. In this paper, however, I propose a novel potential channel why kinship could alternatively influence economic development through organizational behavior of firms. Strong kinship ties would prioritize business networks within the family, or a limited geographic area. In this context, businesses may hesitate to engage international firms, which can deter investments in large projects that require collaborative partnerships.



4. CONCLUSION

In this paper, I present a conceptual framework suggesting that the co-evolution of historical kinship tightness and generalized trust determines modern business formation. Previous literature suggests that kinship shapes cooperative behavior within a society, affecting institutional capacity. I propose that kinship relations have broader economic outcomes, such as business formation and market efficiency. In strong kinship societies, businesses may prioritize forming enterprises with family members due to a reluctance to engage with outsiders. This behavior could restrict market efficiency due to limited cooperation with other firms. Conversely, societies characterized by loose kinship structures foster higher levels of generalized trust, encouraging interactions and partnerships with non-family members. This trust extends to strangers, thereby enhancing market efficiency and facilitating cooperation across various sectors. The result is a more dynamic and adaptable market environment that supports larger, more collaborative organizations, including multinational partnerships. This paper suggests that historical kinship structures influence the quality of economic institutions, particularly in the areas of information sharing, trust, and cooperation, all of which are foundational to market growth and resilience.

The exploration of kinship in the context of organizational behavior provides insights into how deeply rooted cultural norms can affect businesses. Understanding these connections allows us to evaluate family-run businesses and their struggles with market conditions within their cultural frameworks. Therefore, policymakers and international institutions can promote additional initiatives to foster trust beyond family ties to enhance cooperation. Furthermore, the potential effect of kinship structures on business formation may affect entrepreneurial behavior. The first phase of business formations often beset by cooperative behavior shaped by kinship. I conjecture that individuals with strong kinship background would have difficulties on establishing new businesses due to lower level of trust.

Future research can deepen our understanding of the role of kinship in business dynamics. One avenue could involve empirically testing this framework through quantitative analysis to assess the impact of kinship on business formation, market efficiency, and firm performance. In terms of market efficiency, empirical models could explore potential differences across industries and types of firms, such as startups, SMEs, and large corporations.

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