
The Co-evolution of Institutional Environments and Organizational Strategies: The Rise of Family Business Groups in the ASEAN Region*

Michael Carney, Eric Gedajlovic

Abstract

Michael Carney
Department of
Management,
Concordia
University,
Montreal, Quebec,
Canada

Eric Gedajlovic
Department of
Strategy and
Business
Environment,
Erasmus
University, and
The Rotterdam
School of
Management,
Rotterdam, The
Netherlands

In this paper we consider Southeast Asian Family Business Groups (FBGs) as a form of business enterprise as well as existing theoretical accounts of their behaviour. To do so, we develop and describe a co-evolutionary framework that incorporates notions of interdependence, path dependence, and 'system openness.' This co-evolutionary framework is used to anchor a case study describing the developmental paths of FBGs and their institutional environments. Because such neo-evolutionary perspectives bring back into account adaptive behavior motivated by human agency and interests, they offer a promising means of capturing the dynamics (Fligstein and Freeland 1995) and complexity (Baum and Singh 1994) of the interaction between institutions and organizations.

Descriptors: co-evolution, family business groups, ASEAN, path dependence, institutional environments

Introduction

The influence of institutional environments (Hamilton and Biggart 1988) culture (Redding 1990; Hall and Xu 1990), and business systems (Whitley 1992) on East and Southeast Asian corporate organization has attracted a lot of attention recently. Such attention is due in part to the performance attributes of organizing principles that differ significantly from orthodox Western practice (Biggart and Hamilton 1992). Despite problems of definition, a number of popular and academic accounts of Southeast Asian industrialization have identified Chinese FBGs as the engine behind the region's rapid economic growth in the post WWII period (World Bank 1993; Seagrave 1995; Hodder 1996; Lim 1996; Weidenbaum and Hughes 1996). While other types of corporation such as multinational enterprises (MNEs) (Hobday 2000) and state-owned enterprises (Lall 1990) have contributed to the region's growth, FBGs controlled by ethnic Chinese entrepreneurs have undoubtedly played a key role in the economies of many East and Southeast Asian economies. The importance of FBGs in these economies indicates that their business models are an important subject for analysis.

In this paper, we consider the developmental path of FBGs as a form of business enterprise, and existing theoretical accounts of their behaviour. FBGs are prevalent in many emerging economies (Khanna and Palepu

1997) and have been analyzed from a variety of theoretical perspectives, yet they are not fully understood (Granovetter 1994). Institutional and cultural accounts of FBGs see causality running from external or institutional factors to internal organizational factors. In an earlier article in *Organization Studies*, Wilkinson (1996) argued that such deterministic accounts of Asian enterprise run the risk of legitimizing rather than critically evaluating non-Western forms of business enterprise. Wilkinson takes particular issue with institutional theories of East Asian enterprise that lack a plausible account of human agency. Our theoretical exposition addresses these concerns.

Concurrent with the debate regarding the origins of Asian corporate structures, there has been a series of studies reconsidering the accomplishments of institutional theory (e.g. Oliver 1991; Di Maggio and Powell 1991; Scott and Meyer 1994). A major concern in many of these reviews is that institutional theory focuses on the causes and consequences of organizational persistence and continuity. Organizations and institutional norms do change, sometimes quite radically, yet modern or neo-institutional theory has not put change at the centre of its agenda (Greenwood and Hinings 1996). Consequently, recent theorizing about institutions has focused on issues relating to change and the role of human agency (Kondra and Hinings 1998). In the light of these considerations, a number of theoretical perspectives such as structuration (Barley and Tolbert 1997), co-evolution (Keiser 1989; Baum and Singh 1994) and path-dependence (North 1990) have been advanced as either alternatives or complements to more deterministic accounts of the environment–organization interface. These alternative perspectives see human action as intendedly rational but constrained by circumstance, past action and existing norms. For example, North (1990) regards institutions as partially malleable entities that may be passively but critically influenced by sometimes small events that lock-in particular solutions to problems and subsequently limit the range of options available to later actors. Such a perspective highlights the fact that rational and reflective actors who are motivated by their values, economic incentives, or the need for collective action are often capable of significantly influencing institutional arrangements, but are nevertheless subject to constraints that limit their range of feasible and conceivable action.

In this paper, we develop the idea of mutual and reciprocal influence between institutional environments and organizational action. We outline a co-evolutionary framework that incorporates the notions of interdependence, path dependence, and ‘system openness’. Because such neo-evolutionary perspectives bring back into account adaptive behaviour motivated by human agency and interests, they offer promising ways to capture the dynamics (Fligstein and Freeland 1995) and complexity (Baum and Singh 1994) of the interaction between institutions and organizations. The co-evolutionary framework is illustrated with a historical analysis of FBGs in Southeast Asia’s ASEAN member states.¹ ASEAN members straddle a civilizational fault-line (Huntingdon 1997) consisting of predominantly Muslim (Malaysia, Indonesia), Buddhist (Thailand), Sinic (Singapore) and

Christian (The Philippines) societies. Sinic culture is prevalent throughout the region due to a broad and continuing Chinese Diaspora (Purcell 1965), but it is far from dominant. Notwithstanding cultural variation, over a thirty-year period a similar prominent organizational form emerged in each ASEAN country. This prominent form is the diversified FBG created and typically operated by migrants (or their descendants) from mainland China. A precise definition of who constitutes this Chinese merchant class in Southeast Asia has long challenged scholars of the region (e.g. Somers-Heidues 1974; Wu and Wu 1980; Suryadinata 1989; Hodder 1996). The Chinese in ASEAN are not a homogenous group (Suryadinata 1989). Ethnic Chinese are a linguistically diverse, relatively small and fragmented demographic minority within ASEAN as a whole. Except for Singapore, where ethnic Chinese are a demographic majority, they are a minority in most ASEAN states, yet they control a large proportion of each country's leading businesses (see Table 1).

The co-evolutionary framework outlined below indicates how the aggregate strategies of a prominent organizational form can produce collective outcomes such as successful system-wide economic performance. The framework also draws attention to self-reinforcing and self-limiting feedback effects of strategies that result in significant path-dependencies. Simply put, successful strategies run their course and what works in one set of conditions may not subsequently be functional, because strategies can change the very conditions that originally engendered them and allowed them to flourish. Consequently, strategies that at one point in time produce successful system-wide economic performance may later generate paradoxical or counter-intuitive outcomes. For instance, strategies that were once a source of system dynamism may later become a source of system rigidity (Oliver 1991).

Our analysis is focused on the institutionalization of the business models and investment practices of ASEAN FBGs. We adopt an historical perspective which tracks the emergence of FBGs from their roots in Southeast Asia's colonial past, and charts their ascendance through the Nationalist Era in the aftermath of WWII and into the Modern Era and the onset and aftermath of the 1997 Asian financial crisis. Our historical analysis is organized around a co-evolutionary framework that anchors a narrative illustrating the significance and consequences of their institutionalization.

Table 1
Chinese
Entrepreneurial
Performance in
Southeast Asia

Country	Population (millions)	% Ethnic Chinese Population	Ethnic Chinese % Ownership of Private Sector Assets	Number of Largest Firms Controlled by Ethnic Chinese (in%)
Indonesia	182	2.8	70	80
Malaysia	60	33	65	44
Philippines	66	1.5	40	33
Thailand	56	11	90	N.A.

Organizations and Their Environments: A Co-evolutionary Framework

Co-evolutionary perspectives have been primarily applied to the relationship between organizations and their technical environments (e.g. Levinthal and Myatt 1994; Rosenkopf and Tushman 1994). Baum and Singh (1994) expanded the focus to examine the co-evolution of an endogenous institutional environment and a population of social-service organizations. Following Meyer's (1994) suggestion that specific institutional environments are embedded in even wider world environments, we explore the co-evolution of national institutional settings in the context of broader global forces. This approach differs from many institutional accounts of Asian business enterprise, which focus exclusively on national factors. Moreover, in contrast to institutional accounts which restrict their analysis to the role of institutions in shaping organizational action, a co-evolutionary perspective provides a greater role for human agency by also focusing attention on how organizational action shapes institutions.

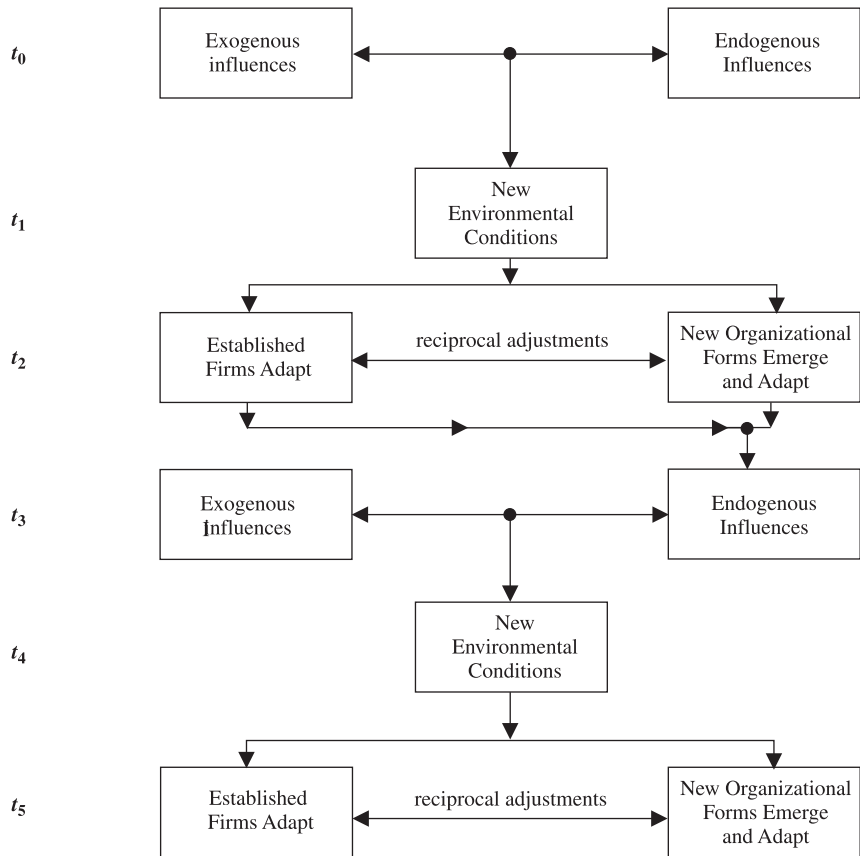
Figure 1 graphically portrays the elements of our co-evolutionary approach. The co-evolutionary framework indicates that organizational forms and practices have their genesis in a particular set of social and political circumstances (Keiser 1989). In turn, these environmental circumstances are forged from the interaction of both exogenous and endogenous influences (North 1990).

Endogenous influences are institutional and market forces that emanate locally from within societies and include the impact of both established and emergent firms and their adaptations to each other as well as to other elements in their endogenous environments. In contrast, exogenous influences are non-local social, economic, political or technological forces that emanate from outside a business system, but which nevertheless impact in important ways upon firms and their environments (Meyer 1994). For example, organizations commonly adopt business models from exogenous sources and institutional agents routinely mimic norms and practice drawn from world society (Meyer 1994). Similarly, once a nation enters the international trading system they become subject to global isomorphic forces that are both economic (North 1990) and bureaucratic in character (Meyer 1994), that emanate from beyond the local economy.

Below, we describe how the end of the Cold War, the emergence of Japan as an economic super-power and the rapid development and commercialization of new information and knowledge-intensive products and technologies (Shapiro and Varian 1998) are exogenous forces emanating from outside Southeast Asia, which have profoundly impacted upon firms based in that region. Such exogenous forces emanate from distant environments, but feedback effects from local environments on those distant forces are minimal. Thus a key distinction between endogenous and exogenous forces is the capacity of local agents to influence significantly endogenous, rather than exogenous forces.

As such, our co-evolutionary framework highlights the fact that business

Figure 1
The Co-Evolution
of Organizations
and their
Environments:
A Generic
Framework



systems are fundamentally open systems that evolve as a function of forces internal and external to the system. This is graphically portrayed in Figure 1, where both exogenous and endogenous influences and their interaction in t_0 shape environmental conditions in t_1 . As illustrated in Figure 1, changed environmental conditions in t_1 trigger organizational adaptations in t_2 .

The co-evolutionary framework predicts that organizational adaptations to environmental changes will take three broad forms in t_3 . First, established firms adapt and calibrate their business models and practices to fit better with their new environments. Importantly, these organizational adaptations constitute an endogenous influence on the environment to which they are adapting. In other words, as firms adapt to their environments, they can also shape those same environments (Baum and Singh 1994). A second organizational-level response to environmental change is the emergence of new organizational forms that match the altered environment more closely than that achieved by established firms (Hannan and Freeman 1989). The growth of particular organizational forms and business practices begin to feedback, and reshape environmental conditions (Levinthal and Myatt

1994). Such responses constitute another endogenous force for environmental change in subsequent periods. A third set of organizational-level responses are the reciprocal adjustments that are made by both established and emergent firms (Kondra and Hinings 1998). Since adjustments by established firms alter the competitive environment of emergent firms, the latter must adapt to the adaptations of established firms. Similarly, the emergence of new organizational forms with novel business practices, and variants of existing models, alters the competitive landscape of established firms and provides the impetus for further adaptive behaviour on their part.

This process is captured graphically in Figure 1, where the adjustments of established firms as well as the emergence of new organizational forms and their early adaptations in t_2 interact and create endogenous forces for environmental change in t_3 . In stage t_3 , these endogenous influences interact with new exogenous influences emanating from outside the system to shape the environmental conditions in t_4 . In turn, the environmental conditions in t_4 give rise to a new round of organizational-level adjustments in t_5 , which constitute new endogenous influences for environmental change in subsequent periods.

While Figure 1 suggests that both endogenous and exogenous forces and responses operate within clearly delineated and discrete time periods, the reality is not so neat. A particular force may emerge weakly, but grow in strength until it is recognized and acted upon in some way. A decision to act upon a particular force may appear as an event or as a point of evolutionary punctuation. Such shifts may also unleash pent-up forces, shift the direction of other forces, or otherwise bring about discontinuous changes that usher in categorically distinct institutional eras. For example, we argue below that the post-war growth of Japanese economic power has constituted an important exogenous force on Southeast Asia. However, the full effect of Japanese power was felt in Southeast Asia following a specific event, namely the 1985 Plaza Accord between the G5 countries that stimulated a sudden increase of Japanese investment into the region (OECD 1999).

The notion of interdependence is fundamental to a co-evolutionary perspective. Interdependence means that firms are influenced by, and use, the same environments to shape their own environments (Pfeffer and Salancik 1978; Oliver 1991; Baum and Singh 1994). Lindblom's (1968) '*muddling through*' thesis suggests that strategies of mutual adjustment, reciprocation, accommodation and co-optation among a '*policy community*' comprised of a diverse set of goal-directed actors can bring about significant institutional change. Similarly, Poroc (1994) proposes that co-evolutionary processes should be understood through the notion of an '*organizational community*' comprised of institutions, regulatory bodies and a population of firms. According to Poroc, the essence of such an organizational community is the web of transactions through which members actively and passively exchange ideas, resources and commitments. As such, the evolution of an organizational community can be conceptualized as the co-evolution of its constituent parts (Poroc 1994).

Importantly, the notion of interdependence reflects the fact that by employing purposive strategies in pursuit of their self-interested objectives, human agents can play a profound role in shaping their local environments. The influence of firms on their local environments may be a deliberate individual, or collective response to perceived threats and opportunities (Lieberman and Montgomery 1988; Nielson 1988). On the other hand, the influence of firms on their local environments may also be the product of unintended or emergent processes (Mintzberg and Waters 1985). Quinn (1980) has coined the term '*logical incrementalism*' to describe such intuitive and evolutionary processes through which decisions made by human actors and external events flow together to form the context for action. For example, Pascale (1994) describes how Honda revolutionized the U.S. motorcycle industry in the 1960s, largely because it lacked sufficient resources to compete with established firms in conventional ways.

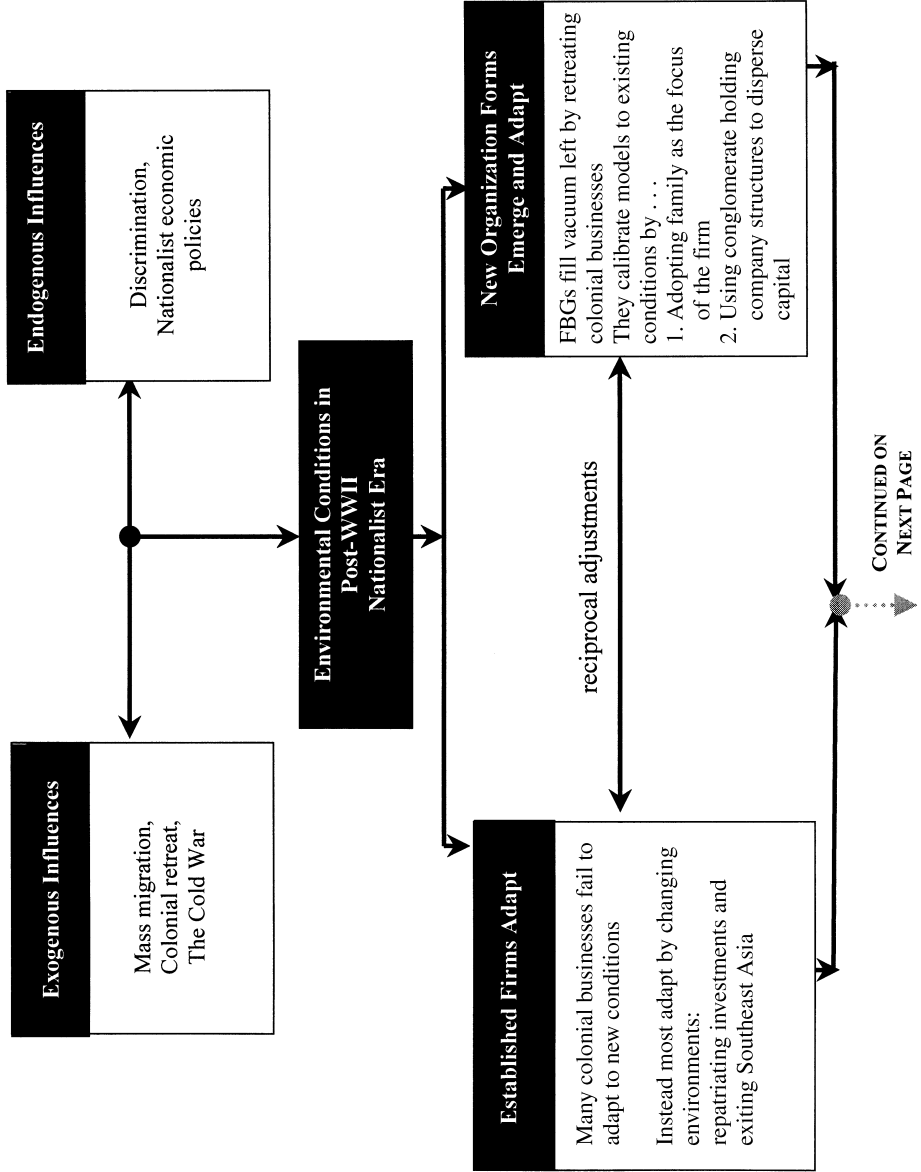
The notion of path dependence (North 1990) is also fundamental to our co-evolutionary approach, since it accounts for the fact that firms and environments are partly, but not exclusively, dependent upon historical patterns of firm–environment interdependence. The environmental conditions faced by a firm at the time of its founding casts a long shadow on its ability to adapt to subsequent environmental changes. Path dependence means organizations are permanently influenced by the circumstances prevailing at the time of their founding and early growth (Starbuck 1965; Prahalad and Bettis 1986; Hannan and Freeman 1989). Strategic practices that are developed in the first few years of a firm's operations become deeply rooted or imprinted in organizational memory and repertoires (Nelson and Winter 1987). In evolutionary terms, some strategies become '*locked in*' while others are simultaneously '*locked out*'. Importantly, locked-in practices condition subsequent rounds of organization adaptation as organizations respond to threats and opportunities in ways that, in the light of their origins, make sense. Thus, nascent conditions, and the adaptation of firms to them, exert an inertial force upon change and limit the range of options an organization may invoke in response to new environmental conditions (Tushman and Romanelli 1986).

In the sections below, we use our co-evolutionary framework to anchor an historical narrative describing the evolutionary path of Chinese FBGs operating in Southeast Asia.

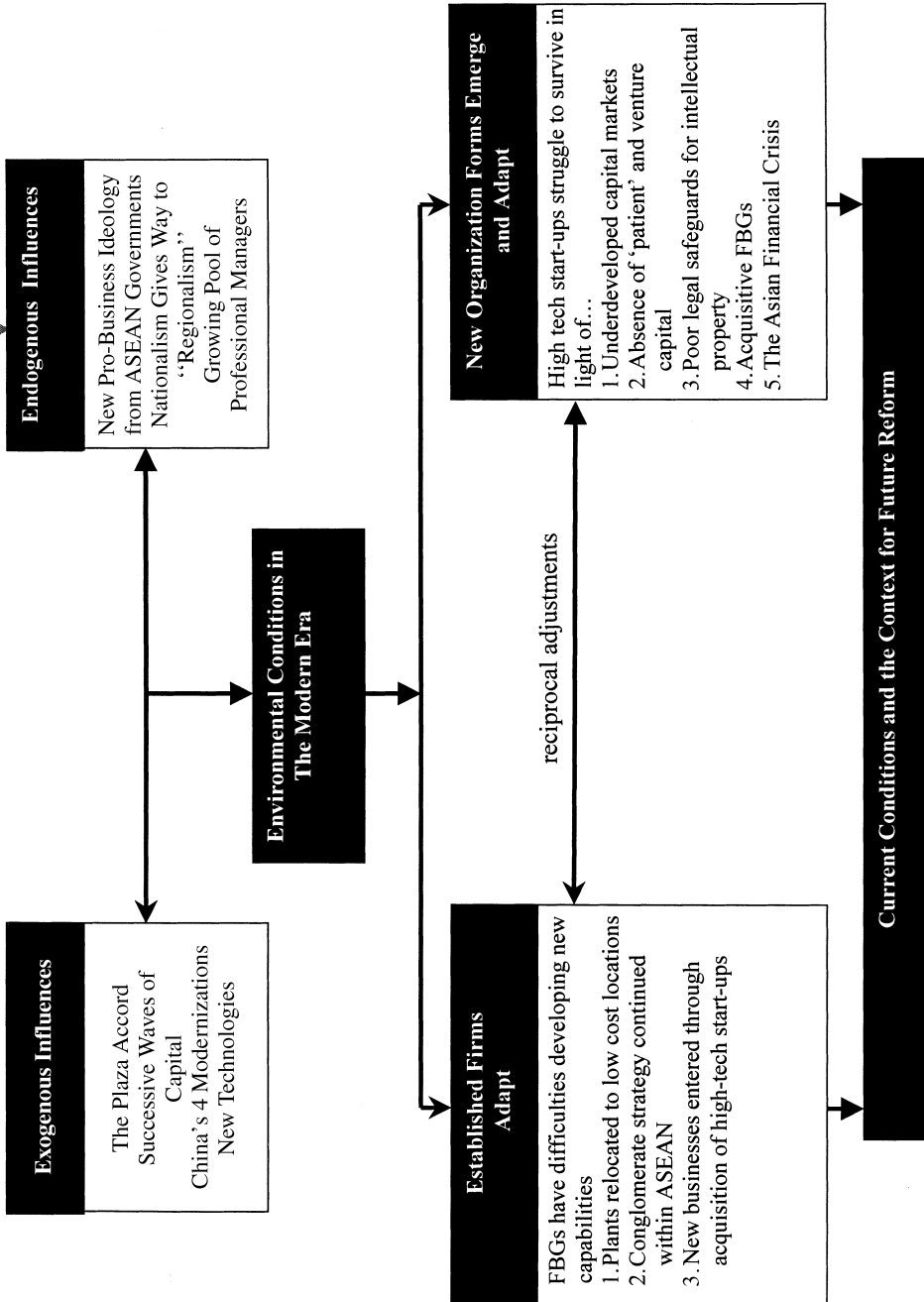
The Colonial Origins of Family Business Groups in ASEAN

Although long established as *petit* entrepreneurs in Southeast Asia (Somers-Heidhues 1974), Chinese entrepreneurship emerged as a significant economic force during and immediately following World War II (Wu and Wu 1980). From early colonial times until the beginning of WWII, ethnic Chinese entrepreneurs typically worked as middlemen, or *compradors* for the British, (Chapman 1985; Davenport-Hines and Jones 1989) Dutch (Allen and Donnithorne 1957) and Japanese-owned trading houses (Yoshihara 1988) which were then dominant in the region. These colonial-era relations were

Figure 2. The Co-Evolution of Southeast Asian Organizations and their Institutional Environments



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PREVIOUS PAGE



abruptly and permanently disrupted with the establishment of Japanese military administration (*Gunseikanbu*) over Southeast Asia's economy in 1941 (Purcell 1965). *Gunseikanbu* was draconian, but it propelled Chinese entrepreneurs into key trading and financial roles (Purcell 1965; Twang 1998).

The immediate aftermath of WWII was a period of intense economic, political and social upheaval in Asia. The major political forces at work included colonial retreat, communist insurgency and the rise of nationalist governments. It is in this environment that FBGs emerged as the region's major entrepreneurial force (McVey 1992). However, at the onset of WWII, the progenitors of now pre-eminent Chinese entrepreneurs occupied a precarious social status. At this time, Southeast Asia's ethnic Chinese were a fragmented and visible minority that was socially marginal, politically powerless and subject to legal discrimination, arbitrary state confiscation of their private property and sporadic popular violence (Purcell 1965; McVey 1992). While the specific threat faced by Chinese minorities differed from country to country across the region, ethnic Chinese faced a '*relentless restriction*' on their commercial activities (Wu and Wu 1980: 89).

The genesis of the Southeast Asian FBG in its modern form owes much to these unfavourable founding conditions. The emergence of FBGs as a major economic force in Southeast Asia can be traced to a number of environmental influences emanating both from within and from outside the region. In the following sections, we highlight the major exogenous and endogenous influences that provided the seedbed for the emergence of FBGs as a regional economic power. Figure 2 summarizes these important forces in terms of the co-evolutionary framework.

The Nationalist Era: Environmental Influences

Exogenous Influences

Three exogenous influences played important roles in providing the environmental conditions necessary for the emergence of the FBG in the post WWII Nationalistic Era of Southeast Asia: mass migration, colonial retreat and the Cold War.

Forces emanating from mainland China profoundly shaped social conditions in the region. Indeed, the mass migration or Diaspora of overseas Chinese in Southeast Asia was largely a product of turmoil in their native homes (Fairbank 1994). Recurrent civil wars produced a steady migration into countries bordering the South China Sea. Successive Imperial, Republican and Communist Chinese governments' disdain for commercial activity did little to advance the interests of entrepreneurs, so they emigrated to improve their lives (Redding 1990). The migrant Chinese who were later to become a dominant economic class in the region emanated from an unstable, warring society that placed little value on commercial activity and had a weak entrepreneurial tradition (Chan 1982).

In the late 19th and early 20th centuries, migrant Chinese workers settled in predominantly agricultural colonial societies where alien Westerners occupied elite economic and political positions. The main colonial industries of plantation agriculture, mining and oil extraction required new intermediary roles between colonists and indigenous groups (Allen and Donnithorne 1959; Davenport-Hines and Jones 1989), which recently landed Chinese immigrants were encouraged to take up (McVey 1992). New occupations such as tax collecting, retailing, money-lending and other ancillary roles related to resource-based industrialization were filled by migrant Chinese, who hitherto had had little entrepreneurial experience (McVey 1992). Within the colonial order, overseas Chinese entrepreneurs developed contacts with indigenous elites and developed commercial and manufacturing expertise that later filled a vacuum left by departing colonial businessmen (Yoshihara 1988).

Chinese migration was widespread in the region and entrepreneurs maintained personal contacts among entrepreneurs from the same family or language group in many Southeast Asian countries (Suryadinata 1989). Close-knit and regionally dispersed networks offered 'safe havens of capital' (Wu and Wu 1980: 94) and channels for mobilizing assets and for sharing information about business opportunities (Kao 1993). Mass migration produced an entrepreneurial class that was well placed to operate international networks and was attuned to the behaviour of a diverse group of key actors. On the other hand, the same expatriate entrepreneurs having left their ancestral homes, were forced to re-establish themselves in settings where they were a distinct minority and where they faced an uncertain future (Wu and Wu 1980; Hodder 1996).

Colonial retreat and the Cold War represented two other exogenous forces that profoundly influenced the post-WWII Asian environment. In the wake of WWII, colonialism began to wane around the world and independent and sovereign states in Southeast Asia became the rule, rather than the exception. As self-rule was achieved in successive countries, large British and Dutch colonial trading houses began their retreat and initiated the process of repatriating their assets (Davenport-Hines and Jones 1989). The retreat of Japanese trading houses occurred even more abruptly when their assets were confiscated at the end of WWII (Yoshihara 1988). One consequence of colonial retreat was the creation of a vacuum of entrepreneurial expertise that Chinese business people were willing and able to fill.

The Cold War and the rise of Asian communism represented an external threat to newly established independent countries and undoubtedly played an important role in setting up nationalistic economic agendas across the region (Stubbs 1999). The legacy of colonial rule left wariness of foreigners and along with the threat of ascendant communism added another reason for governments in the region to pursue nationalist agendas. As they were the largest indigenous group of experienced business people in Southeast Asia, these developments were highly propitious for migrant Chinese entrepreneurs.

Endogenous Influences

Interacting with forces emanating from outside the region were two important endogenous forces which shaped the nascent environments of FBGs: discrimination, and nationalist economic policies. In their traditional role as intermediaries for colonial trading houses, Chinese entrepreneurs were a highly visible ethnic minority that did not always enjoy the full protection of the state. In Thailand, (Laothamatas 1994), Indonesia (Twang 1998) and The Philippines (Hodder 1996; Hutchcroft 1994) official graft and bureaucratic rent seeking was common. In addition, Chinese entrepreneurs suffered official discrimination in Malaysia and Indonesia from nationalist policies intended to secure greater participation in the economy for ethnic nationals (Mackie 1992). Despite their economic success, and indeed possibly because of it, Chinese entrepreneurs faced an environment which they regarded as hostile (Brown 1995).

The top priority of post-WWII governments in the region was national security. In the context of a Western Cold War containment policy, many governmental policies of Southeast Asian nations were driven by the need to fight civil wars, restore internal order and to repel communist threats. Consequently, governments focused upon reinforcing coercive instruments of the state by channelling resources to the military, police, and intelligence services (Stubbs 1999). In Indonesia and in Thailand, senior government officials were predominantly drawn from the military. Where the bureaucracy was drawn from a more heterogeneous range of backgrounds, few knew much about business (McVey 1992). ASEAN economic agendas were limited to managing strategic industries and rebuilding basic infrastructure. Strategic industries were managed by establishing state-owned enterprises, and infrastructure was created with the assistance of US aid. Almost without exception, states in the region adopted highly nationalistic economic agendas featuring import substitution and export-oriented development policies (Stubbs 1999).

The Business Environment

As suggested by the co-evolutionary framework, the nascent environment of FBGs resulted from the confluence of influences emanating from within and from outside the Southeast Asian region. More specifically, mass migration, colonial retreat, the Cold War, discrimination and nationalistic economic policies created the opportunity for the ascendancy of ethnic Chinese entrepreneurs and profoundly shaped the business models and practices they adopted when they were given that opportunity. These forces interacted in a number of important ways.

For instance, mass migration from mainland China constituted an exogenous force that created an available pool of entrepreneurs and managers who were trained and functioned as intermediaries for the colonial trading houses. However, this migration was but one condition necessary for the emergence of the FBG as the economic engine in the region. Another

exogenous force, colonial retreat created the managerial and entrepreneurial vacuum that afforded an opportune environment for the emergence of the FBG. In addition, the influence of the Cold War and the legacy of colonialism drove nationalistic economic policies (an endogenous force) which favoured local entrepreneurs over foreign investors (Yoshihara 1988).

At the same time, as migrants from a turbulent Mainland China, many of the entrepreneurs who founded FBGs brought with them deeply held '*life-raft values*' (Kao 1993: 27) stemming from generations of economic and political uncertainty (Redding 1990). In their new homes, these entrepreneurs faced popular discrimination and bureaucratic harassment. The threat of discrimination in their new homes reinforced the belief that they faced a hostile environment and profoundly influenced both their world-view and their business practices (Brown 1995). Paradoxically, nationalistic economic policies that were discriminatory also created the opportunity for the ascendancy of ethnic Chinese entrepreneurs. Nationalization, import substitution and export-oriented policies put great discretionary power in the hands of state officials and politicians (McVey 1992). Such bureaucratic discretion offered the opportunity for Chinese entrepreneurs to cultivate personal connections, or '*guanxi*' in order to secure lucrative production franchises and other licenses (Mackie 1992).

Organizational Adaptations

As suggested by the co-evolutionary framework, three types of organizational adaptations took place in response to the altered post-WWII environment. First, established firms adapted to their altered environments. Second, new organizational types emerged which were calibrated with and better attuned to the Nationalist Era. Third, established and emergent firms engaged in reciprocal adjustments to each other's actions.

In the wake of WWII, the large expatriate colonial trading houses that had long been the dominant economic force in Southeast Asia were faced with some difficult choices. Long accustomed to being the compatriots of colonial administrators, the trading houses were now operating in hostile environments as newly constituted indigenous governments instituted far-reaching nationalist economic programmes (Falkus 1989; Van Helten and Jones 1989; Mackie 1992). As an obvious symbol of the region's colonial past, colonial businesses were especially vulnerable to anti-colonial sentiment. Thus, in a very short period of time, the benign operating environments enjoyed by colonial businesses for centuries were transformed into one that was fundamentally hostile to them (Drabble and Drake 1981).

Unaccustomed to operating in such environments, and with business practices rooted in the colonial order, colonial businesses were confronted with two fundamental options. They could either radically transform their business practices to the new nationalistic environment, or they could embark upon exit strategies designed to repatriate their investments in the region. Some colonial businesses chose the option of remaining and adapting, but

many more chose the latter option of repatriating their assets (Allen and Donnithorne 1957; Drabble and Drake 1981).

The fact that so many previously successful colonial businesses decided to adapt by changing environments, rather than adapting to their new environments, illustrates the profound importance of path dependencies on the ability of established firms to adapt. Locked into business models based upon assumptions and calculations that were no longer valid, the radically altered business environment they now faced made them a vestige of a by-gone era. The ascendancy of the FBG as the region's economic engine and the gradual and progressive marginalization of many colonial businesses in the years following WWII offers further evidence that a firm's nascent environment gives rise to powerful path dependencies.

Emergent Organizational Forms

Emergent FBGs faced their own path dependencies that facilitated, rather than hindered their ability to develop and calibrate their business practices and models to the new nationalist environment. The confluence of forces emanating from within and from outside the Southeast Asia region created an environment that was filled with both opportunity and hostility for the ethnic Chinese entrepreneurs who established FBGs. As such, the essential challenge faced by the emergent FBGs was twofold. First, they needed to develop business models which would allow them to take advantage of the tremendous opportunities afforded them by the retreat of colonial businesses and nationalistic economic policies designed to promote regional economic development from within (Mackie 1992). Second, the emergent FBGs needed to manage the discrimination and open hostility they faced as an ethnic minority but a growing economic power in their adopted homes (Hodder 1996).

The business models and practices developed by ethnic Chinese entrepreneurs were well-attuned to the post WWII environment in the Southeast Asia region and have become hallmarks of FBG business practices ever since. Perhaps, the most essential characteristic of FBGs is the fact that they are family-owned and managed operations, with family wealth creation and preservation as their overriding strategic goal (Wong 1985). Clearly, this form of business enterprise reflected both life-raft values and the grounded belief of ethnic Chinese entrepreneurs that they were confronted with a fundamentally hostile environment, where they could only trust close family members (Redding 1990; Kao 1993). In this regard, Fukuyama (1995) notes that, in the absence of institutional trust or faith in government, family firms and kin-based networks, such as the FBGs, arise as a basic defense mechanism against a potentially predatory state. As such, migrant Chinese brought suspicion of the state with them to their new homes, and their host societies did little to assuage such pre-dispositions. Together, their legacy as migrants and refugees from a feuding and war-like China and the discrimination they faced in their adopted homes played pivotal roles in driving the decision by Chinese entrepreneurs to utilize

tightly controlled family-owned and managed operating structures as the basis for their business activities.²

The adoption of tightly controlled and family-centric operating structures as the building block of their business models has driven both FBG strategic goals and business practices ever since. Since, the focus of the FBG enterprise is the family unit, it is not surprising to observe that these firms have strategic goals related to creating and preserving familial wealth as opposed to the organization-building goals of professionally managed firms (Redding 1990). To the Chinese families who control FBGs, their business units are essentially goal-attainment devices (Selznick 1957), and are disposable once they no longer advance familial interests. Such an attitude towards the firms they own and manage explains in large part the FBG propensity for rapid asset turnover and wide, unrelated diversification.

The operating structures of FBGs typically consist of multiple small-scale operating units tied together in a web of cross-holdings circuitously, but ultimately controlled by the family (Redding 1990). The subordination of FBG businesses to the interests of the family and the influence of the post WWII nascent environments of the FBG offer several interrelated explanations of why these firms adopted conglomerate structures.

First, the adoption of such conglomerate structures provides a means for the family to protect and diversify its wealth (Fukuyama 1995). Since the FBG is largely based upon both the primacy of family interests and the distrust of outsiders, product-market diversification provides a means of wealth diversification without the need to relinquish control to outside investors. As such, given the context faced by FBGs in the aftermath of WWII, the conglomerate holding structures represented a rational response to an uncoded institutional context characterized by undefined property rights, cronyism, underdeveloped capital markets, weak or non-existent product liability laws and a shortage of managerial expertise (Ghemawat and Khanna 1998). These structures allowed the FBGs to exploit new business opportunities and to cope with their hostile environments, while limiting their family's exposure to risk.

Second, another benefit of the conglomerate holding company structures of FBGs relates directly to the discrimination and open hostility they faced in their adopted homes. Specifically, dispersing family assets across multiple small-scale enterprises limited their visibility and was a rational means of managing the risk of discrimination and asset expropriation they faced in countries such as Indonesia, Malaysia and Thailand (McVey 1992; Mackie 1992).

Third, fear and mistrust of outsiders resulted in a managerial capacity constraint (Carney 1998). As FBGs grew into large-scale economic enterprises, they faced the problem of how to manage and control their empires as the need for outside managers grew. The operating structures adopted by the FBGs addressed this problem in the following manner. Structuring the family business in terms of discrete small-scale business units meant that the outside managers who were required could be evaluated and monitored through the financial results of their business units. In such a structure,

strategically placed family members could exercise effective control over their far-reaching portfolio of diverse operating units. An added advantage of these operating structures was that the impact of hired managers on familial wealth could be minimized. Relatedly, the adoption of these structures meant that no outsider could become indispensable to the FBG and in a position to challenge the interests of the family (Wong 1985; Redding 1990). As such, the use of conglomerate holding company structures consisting of multiple small business units allowed these firms to diversify away many potential managerial agency problems.

At the time of their emergence, FBGs were clearly a product of both their operating environments and their path dependencies. In contrast to the retreating colonial businesses, the path dependencies of FBGs made them especially well positioned to take advantage of opportunities available in the Southeast Asian region following WWII. Owing to their different path dependencies, FBGs could adapt to the new environmental realities, while the majority of colonial businesses could not. Moreover, the hand of human agency is clearly evident in the adaptations described above. FBGs did not passively accept the constraints imposed by their environments. Indeed, it is apparent that the structures and practices of FBGs represented rational, goal-seeking behaviour by agents who were aware of their interests and were capable of organizing to achieve them.

Reciprocal Adjustments

In the post-WWII period, the adjustments of colonial businesses facilitated rather than hindered the emergence of FBGs. At the same time, the adaptive behaviour of retreating colonial businesses was facilitated by the emergence of FBGs. Colonial businesses were faced with the problem of how to repatriate their investments. In this context, colonial businesses who were motivated sellers of assets found, in emerging FBGs, equally motivated buyers of those assets.

One obvious conclusion which can be drawn from our analysis of the respective adaptive abilities of colonial businesses and FBGs in the aftermath of WWII is that a firm's nascent environment and its path dependencies profoundly affect its ability to adapt to environmental changes later on in life. Colonial businesses were very much a product of the colonial order. Once, the colonial order was replaced by the nationalist order, after WWII, the colonial businesses became relics of the past that they had played an important role in creating. Their path dependencies made it difficult or impossible for most colonial businesses to co-evolve with their environments. Their environments changed, but most colonial businesses could not effectively change along with it, and responded by leaving Southeast Asia.

In contrast, in the aftermath of WWII, FBGs were a product of their times, and they developed and later calibrated their business practices to the environmental realities they faced. But what of subsequent changes to the business environment of Southeast Asia? If the lesson to be learned from the history of colonial business enterprises in Southeast Asia is that firms are

largely a product of their nascent environments and path dependencies, how would FBGs adapt to environmental changes later in life, as mature businesses? More specifically, how well would FBGs be able to adapt to epochal events in the 1970s, 1980s and 1990s, such as the emergence of Japan as an economic super-power, the opening up of China to foreign investment, the end of the Cold War and the emergence of new information and knowledge-intensive products and processes? These issues are addressed in the remainder of this article.

The Modern Era: Environmental Influences

Exogenous Influences

What can be referred to as the modern era in Southeast Asia began in the early 1980s and is defined by two geo-strategic events that profoundly changed the region's political and economic environment. Both events are exogenous influences in terms of the co-evolutionary framework (Figure 2).

The first major external event that marked the beginning of the modern era was the adoption by China in 1978 of Deng Xiao Ping's four modernizations. China's new open-door policy resulted in a gradual increase of foreign investment in China. China later became a major rival to ASEAN for foreign direct investment. More importantly, China's open door signalled a reduction in Cold War tensions.

A second major exogenous development was the 1985 Plaza Accord signed by the G5 countries in 1985 that led to the rapid appreciation of the Yen against the U.S. Dollar. While China's open-door policy ushered in a new post Cold War era in ASEAN (Anatolik 1990; Frost 1990), the Plaza Accord stimulated the movement of capital into and within the region. After the Plaza Accord, a wave of Japanese foreign direct investment flooded into the Southeast Asia region and was followed in the early 1990s by an even larger in-flow of Western and Japanese portfolio investments and bank lending (OECD 1999). FBGs benefited from these capital flows by increasing their subcontracting business and partnerships, first with Japanese companies, and later with Western multinational enterprises. FBGs were also leading recipients of foreign bank debt and minority equity investments (Henderson 1998; OECD 1999).

Endogenous Influences

As the economic power and influence of FBGs improved, so did relations between ethnic Chinese entrepreneurs and the state. In the early post-WWII environment, relations between the founders of FBGs and their host governments was one of mutual wariness and mistrust. Nationalist state bureaucracies of this era knew little of business and did little to promote business interests — except when it concerned the national interest. With the close of the Cold War, Southeast Asian bureaucrats began to realize the increased

importance of sustained economic development to political legitimacy (Bergsten 1992; Stubbs 1999). While the details differ in each ASEAN member country, the relationship between government officials and local business people became more mutually accommodating (Bowie 1994; Laothamatas 1989; Hutchcroft 1989; MacIntyre 1989). In this regard, Haggard (1994: 282) concludes that conflict between Chinese FBGs and the state was 'mitigated by the development of personalistic relationships between top political elites, bureaucrats and the larger Chinese enterprises'. By many accounts, alliances between Chinese entrepreneurs and state officials in the modern era have produced a corporatist environment where pro-business values are flourishing (e.g. McVey 1992; McIntyre 1994). These developments have transformed many ethnic Chinese entrepreneurs from socially marginal *petit* entrepreneurs into Southeast Asia's economic and social elites. More importantly, their political connections and their new social standing have afforded them access to senior officials and state-mediated resources such as franchises, licences and contracts (McVey 1992). With the end of the Cold War, threats to national security receded, permitting ASEAN member states to focus upon economic and trade concerns (Anatolik 1990; Frost 1990). States have recognized the benefits of trade and have taken some halting steps towards regional economic integration (Wu 1991). These endogenous developments have afforded well-connected firms like the FBGs with new opportunities for regional expansion and additional growth opportunities in emerging markets such as Vietnam and Cambodia.

At the same time, new migratory patterns in the modern era have eased the region's scarcity of trained professional managers with native sons and daughters returning home from the West with professional qualifications (Vogel 1991). Moreover, additional skilled managers were made available from the region's established business and engineering schools and the subsidiaries of multinational enterprises.

In summary, in marked contrast to the hostile business environment of the Nationalist Era, the Southeast Asian business environment from the mid-1980s up until the Asian financial crisis was quite accommodating and munificent in a number of important ways. Threats to national security had receded, FBG-government relations were improving, moving from conflict to cooperation, and human and financial capital was more abundant than ever.

Organizational Adaptation

As described above, FBGs developed their basic business models during the tumultuous aftermath of WWII. Consequently, their business practices reflected the need to exploit the diverse business opportunities created by departing colonial businesses, while coping with their social marginalization and the absence of many elements of a basic business infrastructure in their adopted societies. One might expect that, since the business models developed by FBGs dealt so effectively with an environment of scarcity

and hostility, these same models would serve them at least equally well during periods of relative munificence. On the other hand, a co-evolutionary perspective suggests that the practices developed during the early stages of a firm's founding cast a long shadow on its subsequent adaptive abilities. In this regard, firm capabilities developed in an era of scarcity may become locked-in, while other types of capability are locked-out or imperfectly developed.

In general, the ownership structure of a firm plays a key role in shaping the incentives of various organizational stakeholders, and consequently influences their willingness to make the contributions necessary for the development of many firm-specific capabilities (Barnard 1938; Cyert and March 1963; Pfeffer and Salancik 1978; Williamson 1999). In this regard, the family-centric ownership structures characteristic of FBGs engenders distinct inclinations and dis-inclinations towards the development of particular capabilities. More specifically, the coupling of ownership and control in FBGs creates strong incentives to manage businesses efficiently and profitably (Alchian and Demsetz 1972; Whitley 1992), but these same incentives make FBGs ill-equipped to operate in many capital-intensive and high-technology industries which require sustained investments in specialized human and physical assets (Redding 1990; Williamson 1991; Carney 1998). For example, the tendency of the entrepreneurs controlling FBGs to disperse their investments across multiple operating units is a potentially effective means of diversifying risk to the family's wealth while maintaining undiluted control over business operations (Kao 1993), but such a tendency deprives firms of the patient capital needed to develop more specialized assets (Redding 1990).

Similarly, while success in many technologically complex markets requires the hiring and retention of competent and specialized senior managerial, the insular and family-centric nature of the FBGs may deprive them of needed human resources (McVey 1992; Kao 1993). While the use of stock options as a means of attracting and motivating top management and technical personnel is standard practice in many high technology industries, FBGs rarely use such compensation strategies as it implies dilution of ownership and loss of familial control. Redding (1988) notes that even when FBGs hire skilled outsiders, they are often excluded from strategic decisions. Kao (1993) bluntly suggests that among such firms, an incompetent relative will be preferred to a competent outsider. Perhaps reflecting a consensus in the literature regarding FBGs, Redding concludes that they are governed by 'values which facilitate the initiating phase of entrepreneurship but which place barriers to the higher levels of co-ordination necessary for growth of the individual firm to large scale' (Redding 1988: 109). Like the business practices of colonial businesses in the wake of WWII, many FBG business practices have run their course, but remain in place due to powerful path dependencies. These path dependencies represent formidable barriers to organizational adaptation. Their business model did not require FBGs to develop the capabilities and resources necessary to institutionalize new product development, (Phongpaichit 1991) establish

brand-name equity, or build global distribution networks (Pananond and Zeithaml 1998). As a consequence, FBGs rarely developed these capabilities and instead focused on reproducing, or marginally improving, existing products at low cost and high quality (Hobday 1994).

In the early stages of ASEAN industrialization, the cost advantages of FBGs propelled an export-oriented system of industrial development in labour-intensive and technologically mature industries (World Bank 1993). In the modern era, such cost advantages have declined in importance, partly due to lower cost competition from mainland China and other emerging economies, but also because of the increasingly global scale of product, capital and factor markets and because of the growing importance of new high technology industries (Shapiro and Varian 1998). Unfortunately, despite considerable governmental attention and effort (Robison 1992; Schein 1996), FBGs have not generally been successful in overcoming their path dependencies and developing the capabilities needed to compete as innovators in high-technology industries. Instead, FBGs have generally remained importers, rather than originators of new technology and techniques (Lall 1990; Yamashita 1991). Additionally, few FBGs have developed the marketing capabilities necessary to compete in global product markets (Lecraw 1993; Pananond and Zeithaml 1998).

Rather than develop their competitive capabilities, FBGs in the modern era have continued to focus upon low-cost and high-quality manufacturing. When challenged by rising labour costs, FBGs have adapted by re-locating plants in lower-cost locations within ASEAN (Hobday 1994). Facing maturity in their traditional markets, FBGs have used their financial resources to acquire new businesses within the ASEAN region (Henderson 1998). Insofar as many FBGs have chosen to adapt by changing environments rather than developing new capabilities, such a response parallels that of the majority of colonial businesses at the beginning of the Nationalist Era.

Emergent Organizational Forms and Reciprocal Adjustments

In the Nationalist Era, the emergence of FBGs was facilitated by colonial retreat. FBGs, on the other hand, are unlikely to be the promoters of institutional reforms for which they are maladapted (Khanna and Palepu 1997). Both the path dependencies and ongoing business behaviour of FBGs may now have negative implications for the emergence of a new generation of firms in Southeast Asia.

For example, while a diverse range of specialized financial institutions is necessary to support the financing needs of firms with differing risk–return profiles, those operating in different industries and those at different life-cycle stages (Porter 1990; Prowse 1996), long-term debt and equity markets are under-developed in ASEAN economies. Such institutional voids reflect prior environmental conditions and firm adaptations. FBGs originally concentrated on non-capital-intensive industries, where expansion could be funded from internal sources. The availability of low-cost labour and the relative scarcity of capital in the Nationalist Era made the empha-

sis upon labour, rather than capital-intensive sectors an economically rational choice under the circumstances. Similarly, since equity markets were undeveloped or even non-existent in the wake of WWII, FBGs devised private financial networks as an alternative source of capital (Limligan 1986; Kao 1993). When industrial growth accelerated in Southeast Asia, equity markets did not develop rapidly, because FBGs already had private financial networks in place and did not need public markets as a principal source of capital. While insular FBGs do not especially need or want to rely heavily on public capital markets (Redding 1990; Kao 1993), it is now widely recognized that the underdevelopment of these financial institutions constitutes a serious impediment to the emergence of new high-technology firms in Southeast Asia (e.g. World Bank 1998; Henderson 1998; Prowse 1998).

The acquisitive propensities of FBGs represent another obstacle hindering the emergence of high technology start-up firms in ASEAN. Due to weaknesses in public capital markets, FBGs have become the principle source of financing for new high technology start-ups (Carney and Gedajlovic 2000). Consequently, many new firms are established under the umbrella of FBGs. Such FBGs may furnish high technology start-ups with financing, but having failed to develop the necessary organizational capabilities themselves, are unlikely to be able to provide these firms with the patient capital, managerial assistance and other resources needed for long-term growth and survival in businesses specializing in high-technology lines (Prowse 1996; *Business Week* 1999).

Conclusion: The Co-evolution of Firms and their Environments

Organizational strategies and institutional environments co-evolve along path-dependent trajectories. As such, firms reflect the institutional conditions in which they emerged. However, firms and their human actors also shape the environment both directly (through their strategies and resource allocation patterns) and indirectly with the passive development of infrastructure and other institutional structures to support their needs. Our examination of the ascendance of FBGs in ASEAN suggests that dominant organizational forms respond to their institutional environments as they find them. In doing so, they influence and re-create their institutional context in a path-dependent manner.

ASEAN's diversified family business groups are both a product and a source of their institutional environments. Indeed, at the beginning of the Nationalist Era, emergent FBGs filled many institutional voids that would otherwise have arrested their development. For example, systems of relational contracting (Rajan and Zingales 1998) and internal capital markets (Williamson 1991) were developed by FBGs to cope with the scarcity of external sources of financing. Similarly, as a means of coping with environments that did not provide adequate mechanisms to protect their property rights or equitably enforce contracts, FBGs developed closed and

tight business networks that ‘provided havens where property rights are respected’ (Khanna and Palepu 1999: 47).

Such adaptive responses allowed FBGs to flourish, but also influenced the developmental path of important institutions in Southeast Asia. Hitherto, the aggregate behaviour of dominant corporate forms in Asia has not been seen as a source of institutional path dependence, but more as the product of institutional patterns derived from (national) history (e.g. Hamilton and Biggart 1988; Whitley 1992). The co-evolutionary perspective adopted here highlights the reciprocal effects that firms and environments have on each other.

As McVey (1992) puts it, since the end of WWII, FBGs have graduated from being ‘pariahs to the paragons’ of the Southeast Asia business class. Lacking political and economic power at the outset of Southeast Asia’s industrialization, FBGs proactively negotiated a hazardous environment to achieve their private interests. The history of Southeast Asia’s FBGs also indicates that dominant organizational forms can influence their institutional environments in an emergent fashion (Mintzberg and Waters 1985). For instance, as we describe above, the response of FBGs to the weak business infrastructure they faced in the Nationalist Era was to develop relational forms of contracting. In doing so, FBGs effected the subsequent development of institutions in the region. In this regard, contemporary efforts by the region’s policy makers to replace the institutions of relational contracting with rules based on norms of ‘arms-length’ contracting have been frustrated, not by active resistance, but by the presence of deeply embedded institutional practice. Such a perspective on the influence of human actors on their environments differs markedly from views that emphasize unreflective behaviour (Di Maggio and Powell 1991). On the contrary, it suggests that locally rational responses of human actors to the stimulus of challenges that are specific to a particular time and place can fundamentally influence their institutional environment. This ‘muddling through with purpose’ as Lindblom (1968) puts it, is the essence of rational human agency from the perspective of the actors in their context.

Viewed in this light, the contemporary prevalence of relational contracting and weak capital markets in Southeast Asia can be seen to be outcomes of economic actors seeking self-interest objectives in an environmental context which they inherited, but fundamentally changed. Responding to post WWII forces, FBGs developed robustly competitive business routines and a structural form to safeguard their assets. The conglomerate organizations that emerged as the dominant business form across the wide range of national cultures found in ASEAN may be properly viewed as a superbly adaptive response by human agents to the region’s uncoded legal and regulatory environments. The package of organizational capabilities that co-developed was also well adapted to the prevailing conditions. However, the institutionalization of forms of business enterprise that require little legal or regulatory infrastructure may have profoundly negative implications regarding the ability of modern-day ASEAN economies to carry out needed infrastructural reforms.

In other words, a co-evolutionary perspective implies that changes initiated in the institutional environment, even changes widely perceived as legitimate, will not necessarily bring about organizational compliance. Instead, agents in dominant organizational forms may accurately perceive both their interests as well as the means to achieve them (Kondra and Hinings 1998) and act to offset any institutional processes that threaten them (Oliver 1991). As such, our co-evolutionary framework predicts a slow cycle of co-evolution between firms and their environments, rather than rapid and radical re-alignments.

In this respect, the within-species evolution of a particular form in relation to its institutional environment may be less vital to the development of an enterprise system, than the inter-species competition between fundamentally different organizational forms. Stinchcombe (1997) observes that institutions promoting organizational persistence (the protection of existing assets, jobs, and organizational competencies) generally enjoy greater legitimacy than those that promote the destruction of those valued assets. Consequently institutions that promote the destruction of old organizational populations or practices enjoy only a precarious legitimacy. Indeed, many economies never develop such institutions and evolve rigid and ossified economic structures that deliver persistently poor economic performance (North 1990).

Unfortunately, while critical to policy makers and managers around the world, outside North American and Western European contexts, we know very little of the processes through which new corporate forms come to be legitimized and institutionalized. As such, further research is needed on the processes by which organizational forms emerge, become institutionalized and ultimately become de-institutionalized in the context of emerging, developing and transformational economies. The co-evolutionary framework developed and described here may provide a useful basis for such research.

Notes

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1. ASEAN is an international organization established to promote economic, technical, scientific, and political cooperation between its members. Formerly created by the Bangkok Declaration in 1967, the original ASEAN founders were Indonesia, Malaysia, Singapore, The Philippines, and Thailand. Our analysis focuses upon FBGs in these five countries. Sufficient commonality of interest was perceived that The ASEAN Concord of 1976 called for greater industrial, trade and economic cooperation between these nations (Antolik 1990). Brunei, Laos, Vietnam and Myanmar subsequently joined ASEAN.

2. There is some evidence that earlier generations of Chinese migrants who faced less hostile environments developed enterprises along very different lines than those characteristic of FBGs. For example, the long established elite Chinese business class in the Dutch East Indies, (the *Peranakan*) were largely assimilated into Dutch colonial society. The *Peranakan* were educated in Dutch schools and were afforded legal rights similar to Europeans. Under these conditions, the *Peranakan* developed Dutch business habits and techniques. During the Japanese occupation and thereafter, the *Peranakan* declined in importance. Interestingly, Twang (1998) suggests that their approach to business was disrupted by new political conditions and became out of tune with the new times. In contrast, Indonesia's current Chinese business elite (the *Totok*), faced a distinctly more hostile environment in their adopted homes. The *Totok* were Chinese-born and migrated to Southeast Asia during the first three decades

of the 20th century. Most *Totok* established their initial businesses between 1940–1950 during the Japanese occupation and the subsequent communist–republican Civil war. In contrast to the earlier arriving *Peranakan*, the *Totok* were not generally assimilated into Indonesian society and were confined to the margins of Indonesia's social and economic life. According to Twang (1998), it was under these conditions that the *Totok* acquired many of their characteristic business practices.

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