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Cultural Origins in Corporate Business Management: Merchant Guild Culture and Corporate Strategic Choices

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Abstract: Previous research primarily focuses on the financial outcomes of corporate strategic choices, but rarely discusses why they differ in strategic choices. Informal institutions, such as culture, may explain corporate strategic decisions. Based on data from Chinese listed firms from 2007 to 2022, this paper finds that corporates more influenced by merchant guild culture are more likely to implement the defenders-type strategies, which aligns with the origin logic of risk aversion in historical merchant guilds, suggesting contemporary corporate strategic choices have cultural origins. In further analysis, we examined the mechanisms of risk avoidance. Overall, this study contributes to the literature about social norm and corporate behaviors, providing new evidence for the understanding of how informal institutional affect corporate behaviors.

1. Introduction

Strategic choices are crucial for corporates, with different orientations leading to significant differences in risk-taking and resource allocation, resulting in distinct corporate behaviors. Consequently, literature on strategic choices focuses on firm-level financial outcomes, such as cash holdings [1], financial asset allocation [2], commercial credit financing [3], debt maturity structure and defaults [4], cost stickiness [5], financial reporting misconduct and auditor judgments [6], and tax aggressiveness [7]. However, Zhong et al. (2022) highlight that existing research, especially Chinese firm-level studies, overlooks a fundamental question: Why corporations implement different types of strategies (e.g. prospectors- or defenders-type)? [8]

Recent research has gradually begun to address this question, mainly focusing on formal institutions in two areas: government-led macro-market policies [9][10] and corporate governance [8][11][12]. In general, evidence from informal institutions remains limited.

We constructed a sample of 32,940 annual observations of firms listed on the Chinese stock market from 2007 to 2022 to test the influence of historical merchant guild culture (MGC) on strategic choices of modern Chinese corporates. We found that corporates more influenced by MGC tend to choose stable defenders-type strategies rather aggressive prospectors-type strategies.

This study makes several contributions. First, it enhances the framework on how social culture and norms influence corporate behaviors. Previous research indicates that local cultures and norms shape individual beliefs, significantly impacting corporate decision-making in accounting, finance,

and corporate governance. Second, this study expands on the influence of historical MGC on contemporary corporates and their managers. Third, this study enhances research on macro institutional factors affecting corporate strategic choices.

2. Institutional background and hypotheses development

2.1. Merchant guilds in Chinese history

Merchant guilds, based on geographical and kinship identities, with affection and hometown bonds as emotional ties and "mutual assistance" as their purpose, are a type of business organization with guild halls, public offices, guilds, and temples as their activity venues. As commercial activities matured, concepts of market competition and operational risk control emerged, prompting merchants to unite spontaneously to establish organizations to resist cross-regional operational risks and provide mutual assistance.

From the perspective of informal institutions, Ming and Qing merchant guilds developed rigorous organizational forms and operation norms with unique regional characteristics during long-term commercial practices. These norms safeguarded the commercial interests of business organizations within specific regions and helped reconcile the interests of merchants and social conflicts [15]. Culture rooted in specific institutional environments significantly impacts modern corporate management, often through managers. They must adhere to social norms in social interactions, as deviating from acceptable behaviours incurs high costs [16]. Culture sets guidelines for managerial behaviour, influencing management models.

Some studies record the impact of MGC on corporate and managerial behaviors. For instance, the emphasis on diligence alleviates agency conflicts [14] and shapes virtue of benevolence, leading to active social responsibility [17][18][19]. Further research shows that MGC's corporate governance function aids firms in securing financing [20][21][22], thus reducing the need for high-level cash-holdings [23].

2.2. MGC and corporate strategy choice

As shown in Figure 1, theoretically, MGC may have two diametrically opposed effects on corporate strategic choices.

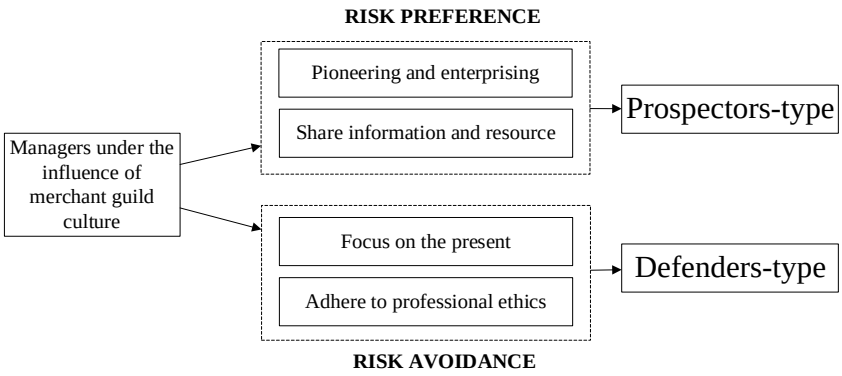

Figure 1: Theoretical framework

2.2.1. Risk preference

Commerce was inherently adventurous. First, MGC adheres to the philosophy of exploration and innovation. This cultural gene encourages firms and their managers to take risks, actively seeking

new business opportunities, whether in new regional markets or new products. In long-term business practices, firms face complex, changing markets, forming a spirit of flexibility and experimentation. This makes firms influenced by MGC more likely to adopt aggressive or unique strategies in response to market changes or technological innovations, aiming to seize new opportunities or address potential risks.

Second, merchant guilds served as platforms for sharing information and resources. Guild culture has physical carriers, such as guild halls, public offices, benevolent societies, and temples. Merchants gathered in these places during the agricultural era to share market information, development trends, and current events. This was crucial for understanding the operating environment and adjusting business strategies promptly. This environment fostered close cooperative relationships among merchants through mutual support. This legacy allows firms and managers to maintain flexibility and adaptability, leading to more dynamic and aggressive strategies.

Therefore, we formulated Hypothesis 1:

Hypothesis 1. Corporates with a strong influence of MGC prefer prospectors-type strategies

2.2.2. Risk avoidance

As mentioned previously, the formation of guilds originated from resistance to risks and uncertainties, which implies that guild culture carries genes of risk avoidance.

On the one hand, managers may focus more on the current operational environment. In a competitive environment, the market is flooded with redundant, complex, and even false information. As humans, managers evidently lack the perfect ability to handle vast amounts of information. Researchers have found that in a competitive environment, managers need to maintain a certain degree of myopia, especially regarding time cost. Such managers often focus on current strategies and maintain strategic stability over a period [24]. Therefore, managers influenced by MGC are expected to maintain a certain degree of myopia, thus preserving strategic stability.

On the other hand, managers may adhere more to professional ethics. Du et al. (2017) argued that MGC, emphasizing norms of integrity and mutual benefit, regulates unethical behaviors [14]. Managers in ancient Chinese guilds had to adhere to Confucian ethics as moral guidelines, or they would not be welcomed in society [14]. Therefore, it can be expected that managers influenced by MGC adhere more to professional ethics, have weaker motivations to capture private benefits through prospectors-type strategies, and are more inclined to receive incentives based on reputation, attempting to convey to shareholders and other stakeholders that they are excellent managers through stable defenders-type strategies.

Therefore, we formulated Hypothesis 2:

Hypothesis 2. Corporates with a strong influence of MGC prefer defenders-type strategies.

3. Research design

3.1. Sample Selection and data source

This study examines Chinese A-share listed firms from 2007-2022. After regular date-selection, we obtain 32,940 firm-level data points, covering 4,006 firms. All continuous variables are Winsorized at the top and bottom 1%. The data used in this study mainly from China Stock Market and Accounting Research Database (CSMAR).

3.2. Empirical model

To examine the influence of MGC on corporate strategic choice, we employed a regression

model that takes several control variables and fixed effect into account:

$$Strategy=\alpha_0+\alpha_1 MGC+Controls+FE+\varepsilon \quad (1)$$

In Eq. (1), the dependent variable, Strategy, is measured using the business strategy index developed by Bentley et al. (2013) [6]. The independent variable, MGC, is a distance variable based on geographic proximity that measures corporates' exposure to MGC. Controls include various factors affecting strategic choices, such as firm characteristics, corporate governance, and the macroeconomic environment. FE represents a set of fixed effects constructed with dummy variables to control for differences among industries, provinces, and years.

A significantly positive (negative) MGC coefficient suggests that corporates exhibit risk-preference (risk-avoidance) and prospector-type (defenders-type) strategies under strong MGC influence, supporting Hypothesis 1 (2).

3.3. Variable measurement

3.3.1. MGC

We first gathered latitude and longitude data for the top 10 guild origins and the office locations of listed firms. Using the spherical distance formula from Du et al. (2017), we calculated the distances between listed firms and each guild [14]. The shortest distance to a guild served as a proxy for MGC influence on listed firms. A smaller distance suggests greater MGC influence on corporates. To simplify empirical result interpretation, we multiplied the value by -1.

3.3.2. Strategic Choice

Bentley et al. (2013) constructed the business strategy index by six variables. Each of those variables are measured per firm-year based on the rolling prior five-year average and then ranked into quintiles per industry and year. The first five measures are assigned 5-1 from high to low and the last is assigned from low to high, and then sum up. As a result, we obtained Strategy score ranges along a continuum in value from 6 to 30 with defenders- and prospectors-type companies closer to the endpoints.

4. Empirical result

4.1. Baseline regressions

Table 1: Baseline regressions.

	Strategy				
	(1)	(2)	(3)	(4)	(5)
MGC	-0.610***	-0.642***	-0.787***	-1.066***	-0.984***
	(-3.083)	(-3.373)	(-4.025)	(-5.524)	(-5.110)
Firm characteristics	NO	YES	NO	NO	YES
Corporate governance	NO	NO	YES	NO	YES
Macroeconomic	NO	NO	NO	YES	YES
Observations	32,940	32,940	32,940	32,940	32,940
Year & Ind	YES	YES	YES	YES	YES
Adj-R^2	0.060	0.100	0.085	0.105	0.133
F	9.502	257.726	147.372	441.255	207.308

Robust t-statistics in parentheses, *** p<0.01, ** p<0.05, * p<0.1

Table 1 presents the baseline regression results. Since control variables are categorized into three dimensions, we used a stepwise control approach to test the competitive hypothesis. As shown in

Table 1, the coefficients of MGC are significantly negative, which strongly supporting Hypothesis 2.

4.2. Endogeneity concerns

4.2.1. The impact from competitive strategy

In the empirical examination of the relationship between MGC and corporates strategic choices, one of potential endogeneity issues may arise from competitive strategies. Corporates influenced by strong MGC may adopt various competitive strategies, such as differentiation or cost leadership, which can obscure the influence of cultural factors on strategic choices.

We obtained corporate competitive strategy basic data from Wingo Data. Following Hu et al. (2020), we first calculated the ratio of the differentiation strategy index to the cost leadership strategy index[25]. Competitive strategies (CS) with a ratio larger than the annual median were assigned a value of 1; otherwise, they were assigned 0. A value of 1 indicates a preference for differentiation strategy, while 0 indicates a preference for cost leadership strategy.

As shown in columns (1) to (2) of Table 2, the coefficients of MGC are all significantly negative, consistent with the baseline regression. The results in column (3) show that the coefficient of MGC remain significantly negative, while the coefficient on MGC*CS is negative but not significant.

4.2.2. The impact of clannish culture

We introduced the population share of the top three surnames in prefecture-level cities as a proxy for clan culture as a special control variable in Eq. (1). The results, as shown in column (5) of Table 2, show that after controlling for local clannish culture (CC), the coefficient of MGC is still significantly negative, consistent with the baseline regression.

Table 2: The impact of competitive strategy, clannish culture and IV-2SLS.

	Strategy				MGC	Strategy
	CS=1	CS=0	Interactive Effect	Clannish Culture	IV: First	IV: Second
	(1)	(2)	(3)	(4)	(5)	(6)
MGC	-0.742***	-0.830***	-0.754***	-0.942***		-1.965***
	(-2.694)	(-3.309)	(-3.897)	(-4.909)		(-3.317)
CS			-1.854***			
			(-34.920)			
MGC*CS			-0.157			
			(-1.382)			
CC				1.766***		
				(4.835)		
Geo					-0.170***	
					(-13.424)	
Controls & FE	YES	YES	YES	YES	YES	YES
Observations	16,195	16,745	32,940	32,940	32,940	32,940
Adj-R^2	0.093	0.191	0.175	0.133	0.928	0.132
F(Wald Chi ^{2})	63.520	126.158	304.233	195.636	41.139	5490.220

Robust t-statistics in parentheses, *** p<0.01, ** p<0.05, * p<0.1

4.2.3. Instrumental variable

We employed the IV-2SLS method to address causal endogeneity issues. The chosen instrumental variable is the terrain ruggedness at the provincial level (Geo). Nunn and Puga (2012) documented how rugged terrain obstructs trade and production activities globally [26]. Rugged

terrain likely led to professions specialized in trade and commodity circulation, such as merchants. Thus, terrain ruggedness satisfies the relevance condition for instrumental variables.

The results are listed in Table 2. In the first stage, Column (5) shows that the coefficient of Geo is significantly negative. After considering Geo, Column (6) shows that the coefficient of MGC remains significantly negative. This supports the baseline regression.

4.2.4. Alternative measurement of MGC

Referring to Du et al. (2017) and Kanagaretnam et al. (2019), we calculated the number of merchant guild origins within a specific radius around each corporate as a proxy variable for MGC [14][18]. The index positively measures the corporates' exposure to MGC.

We set radius scales of 50, 100, 150 and 200 kilometres. The regression results are listed in Table 3. The coefficients of MGC_R are all significantly negative, consistent with the baseline regression.

Table 3: Alternative measurement of MGC

	Strategy			
	R=50	R=100	R=150	R=200
	(1)	(2)	(3)	(4)
MGC_R	-0.182***	-0.199***	-0.045***	-0.069***
	(-5.601)	(-9.068)	(-3.680)	(-7.819)
Controls & FE	YES	YES	YES	YES
Observations	32,940	32,940	32,940	32,940
Adj-R^2	0.133	0.134	0.132	0.133
F	208.203	212.529	206.454	209.810

Robust t-statistics in parentheses, *** p<0.01, ** p<0.05, * p<0.1

4.3. Mechanism analysis: Risk Avoidance

We constructed Eq. (2) and Eq. (3) based on Eq. (1) for mechanism analysis. The results are presented in Table 4, with column (1) listing the baseline regression for Eq. (1).

$$Myopia(AETC)=\alpha_0+\alpha_1 MGC+Controls+FE+\varepsilon \quad (2)$$

$$Strategy=\alpha_0+\alpha_1 MGC+\alpha_2 Myopia(AETC)+Controls+FE+\varepsilon \quad (3)$$

The mechanism variables include Myopia and AETC. Myopia is based on the managerial myopia index constructed by Hu et al. (2021) using text analysis and machine learning [27]. Higher Myopia values indicate that managers are more focused on the current competitive environment. AETC stands for AETC, measured according to Kim et al. (2023) [28]. These costs indicate agency conflict, where managers misuse public resources for personal benefit. Therefore, lower AETC values suggest higher managerial ethics.

4.3.1. Focus on the present

The tests with Myopia as the mechanism variable are shown in columns (1) to (3) of Table 4. Based on the baseline regression, the coefficient of MGC in Eq. (2) is significantly positive, suggesting that in corporates more influenced by MGC, managers are more short-sighted and focused on the current competitive environment or competitors. The coefficient of Myopia in Eq. (3) is significantly negative, implying that managers with higher level of myopia usually prefer the defenders-type strategies.

4.3.2. Professional Ethics

The tests with AETC as the mechanism variable are shown in columns (1), (4), and (5) of Table 4. Based on the baseline regression, the coefficient of MGC in Eq. (2) is significantly negative, suggesting that AETC are lower in corporates that are subjected to greater MGC. The coefficient of AETC in Eq. (3) is significantly positive and AETC are positively related to prospectors-type strategy. The results in Table 4 support the expectation that MGC leads to defender-type strategies by inducing managers to avoid risks. These risks include competitive failure due to a lack of attention to the current competitive environment and competitors, and moral hazard arising from self-interested motives and agency problems.

Table 4: Mechanism analysis.

	Strategy	Myopia	Strategy	AETC	Strategy
	(1)	(2)	(3)	(4)	(5)
MGC	-0.984***	0.010**	-0.939***	-0.005***	-0.712***
	(-5.110)	(2.182)	(-4.912)	(-5.429)	(-3.809)
Myopia			-4.385***		
			(-15.362)		
AETC					50.786***
					(39.037)
Controls & FE	YES	YES	YES	YES	YES
Observations	32,940	32,940	32,940	32,940	32,940
Adj-R ²	0.133	0.144	0.138	0.026	0.177
F	207.308	49.308	211.575	25.630	298.643

Robust t-statistics in parentheses, *** p<0.01, ** p<0.05, * p<0.1

5. Conclusions

This study examines how macro-level MGC influences micro-level strategic decision-making within the unique research context of China. Our empirical findings confirm a negative relationship between the degree of MGC influence and the strategic business index, indicating that companies more heavily influenced by MGC tend to adopt defenders-type strategies. This relationship remains robust after rigorous endogeneity tests. Furthermore, we validated the risk avoidance mechanism, showing that the inclination towards defenders-type strategies is driven by managers' heightened awareness of the competitive environment and their commitment to professional ethics. Overall, these findings enhance our understanding of how cultural factors shape strategic decision-making.

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