Unveiling Determinants of Employee and Asset Retrenchment in SMEs: An Institutional Perspective

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Abstract

This research endeavors to expand the institutional lens on retrenchment decisions within SMEs, encompassing diverse facets such as employee and asset retrenchment. We empirically analyze retrenchment decisions among a sample of firms in the Rhône-Alpes region from 2005 to 2014. The results highlight the significant influence of factors such as the business climate, the firm's financial situation, and observed retrenchment practices among industry leaders. These factors distinctly contribute to shaping the retrenchment preferences of firms. Notably, the influence is particularly pronounced in employee retrenchment, revealing a heightened sensitivity to mimetic logic. These outcomes incite nuanced reflections across three pivotal dimensions, shedding light on intricate intersections within the institutional landscape of SME retrenchment decisions.

Keywords: Employee Retrenchment; Asset retrenchment; Institutional dynamics; Mimicry; Small and Medium Enterprises.

1. INTRODUCTION

Retrenchment, a pervasive concern for firms within the economic landscape, constitutes a recurring focal point in strategic discourse (Mann and Byun, 2017). Defined as the deliberate reduction of employees or assets within a firm (Datta et al., 2010), retrenchment emerges as a significant strategic consideration for top-level executives. This reduction may manifest through asset or subsidiary divestitures, workforce downsizing, or a strategic refocusing on the core operational domains of the firm. In light of the profound ramifications entailed by such decisions, scholarly attention has delved not only into the consequences of retrenchment—such as its impact on firm performance (Brauer and Laamanen, 2014), conditions conducive to value creation through retrenchment (Brauer and Laamanen, 2014; Tangpong et al., 2015; Zorn et al., 2017), workplace dynamics (Luthans and Sommer, 1999), and corporate reputation (Zyglidopoulos, 2005)—but also into its antecedents.

These antecedents encompass environmental factors such as economic and political uncertainty (Cascio et al., 2021), firm characteristics like the degree of unionization (Alakent and Lee, 2010), and the personal attributes of top management (Gupta et al., 2019; Budros, 2000, 2002, 2004; Sronce and McKinley, 2006; Carmeli and Sheaffers, 2009). However, empirical studies fail to yield consensus on the effects (De Meuse, Marks, and Dai, 2009). A particularly salient point of uncertainty lies in the relatively limited understanding of the antecedents of retrenchment. Compared to the numerous studies addressing its outcomes, those specifically addressing the antecedents remain relatively scarce (e.g., Duhaime and Grant, 1984; Budros, 1999). It is also noteworthy that there is a conspicuous absence of studies examining the impact of institutional factors as potentially significant explanatory factors in the practice of retrenchment.

This research gap is noteworthy given the substantial body of literature demonstrating the influential role of institutional factors on organizational strategic decisions and practices (Budros, 2004). However, the institutional dimension of retrenchment introduces a theoretical framework that reinvigorates traditional perspectives. While classical approaches historically grounded studies in a rational decision-making framework—where firms retrench in response to deteriorating circumstances or to mitigate the risk of failure (Rasheed, 2005; Powell and Yawson, 2012)—alternative perspectives, notably those emphasizing institutional pressures, have been advanced. Firms, it seems, are responsive to practices deemed normative within their environment, engaging in mimetic behaviors accordingly (Datta et al., 2010). The challenge for firms is to directly improve financial performance and, more broadly, to legitimize their choices. However, despite being identified, institutional logic has received limited attention in the field of retrenchment (Budros, 2004, as an exception). Consequently, research has shown little interest in the potential diversity of institutional influences, remaining fragmented. The various modalities of retrenchment adopted in studies can often make direct comparisons challenging. To the best of our knowledge, there is a shortage of studies explicitly crafted for the context of SMEs despite the prevalent representation of SMEs in the business landscape.

This article aims to enrich institutional insights into retrenchment decisions within SMEs, focusing on employee and asset reduction. By examining the roles played by financial distress, business climate, and leadership behavior in justifying retrenchment, we strive to offer a nuanced exploration of this intricate phenomenon. We postulate a more pronounced influence on employee retrenchment, considering its heightened social connotation compared to the reduction of non-human assets (Cascio, 2012). Particularly in the SME context (Li et al., 2017), leaders tend to associate layoffs with failure (Torrès, 2011). Consequently, anticipating a more pronounced influence of institutional variables on employee retrenchment than asset retrenchment appears legitimate.

To formalize these expectations, we developed a series of hypotheses tested on a sample of SMEs from the Rhône-Alpes region. These hypotheses scrutinize the nexus between the industry's situation, leadership dynamics, and the firm's retrenchment decisions. The results largely confirm our expectations, highlighting the importance of sectorial practices as an explanation for retrenchment.

The subsequent sections of the article unfold across four components. The first part entails a literature review to formulate our hypotheses. The second part delineates the methods employed and presents descriptive analyses. The third part is dedicated to presenting the results. Finally, the fourth part delves into a discussion of the obtained results and their implications within existing literature.

2. LITERATURE REVIEW

2.1. Antecedents of Retrenchment and Institutional Theory

The existing body of literature extensively explores the diverse factors influencing retrenchment decisions. Primary attention has been devoted to internal organizational factors (Baumol et al., 2003; Budros, 2004; Cascio et al., 2021; Hillier et al., 2007; Kim et al., 2020; Bassanini et al., 2013; Cirillo et al., 2020), the interplay of environmental factors, and the distinct characteristics defining firms (Freeman and Erhard, 2012; Datta et al., 2010). Coucke et al. (2007) unveiled notable sectoral nuances impacting the likelihood of employee retrenchment by examining environmental factors. Concurrently, empirical evidence highlights foreign market competition (Budros 1997), market deregulation (Filatotchev et al., 2000), and market volatility (Alakent and Lee, 2010) as pivotal drivers of workforce downsizing. Recent insights by Cascio et al. (2021) underscore the influence of economic and political uncertainty, sectoral competition, and technological advancements on managerial decisions concerning retrenchment.

Internally, the literature underscores the multifaceted impact of organizational characteristics such as debt levels (Lee and Cooperman 1989), diversification strategies (Hoskisson et al., 1994), ownership structures (Vicente-Lorente and Su'arez-Gonz'alez, 2007), degree of unionization (Alakent and Lee, 2010), shareholder value devaluations (Ahmadjian and Robinson, 2001; Perry and Shivdasani, 2005), board composition (Perry and Shivdasani 2005), and, more recently, issues related to profitability (Cascio et al., 2021; Hillier et al., 2007). Furthermore, investigations indicate that retrenchment practices within family-owned enterprises exhibit distinct characteristics compared to non-family enterprises (Kim et al., 2020; Cirillo et al., 2020; Bassanini et al., 2013). Nevertheless, the institutional perspective in explaining the phenomenon of retrenchment remains a relatively understudied domain. Notable exceptions, such as Munoz-Bullon and Sanchez-Bueno (2014), identify the significant role played by inter-firm imitation in shaping retrenchment decisions.

Institutional theory emerges as a seminal framework within organizational analysis (Pursey et al., 2009; Mizruchi and Fein, 1999; Palmer and Biggart, 2017), offering insights into the coherence of organizational characteristics. Despite the inherent challenges and legitimacy concerns associated with retrenchment practices, prior scholarship underscores the appropriateness of organizational actions aligning with institutional norms in the context of a "socially constructed system of norms, values, beliefs, and definitions" (Suchman, 1995).

2.2. Institutional Dynamics in Retrenchment Decision-Making

Exploring the relationship between retrenchment and performance, as often investigated in existing literature (De Meuse, Marks, and Dai, 2009), reveals a lack of consensus among study outcomes. For instance, Brauer and Laamanen (2014) demonstrate that significant workforce reduction positively impacts performance, while a minor reduction may not yield similar advantages. Interestingly, the positive effects of workforce downsizing on firm performance seem contingent, primarily manifesting in non-publicly traded companies. Paradoxically, retrenchment could sometimes weaken a firm, heightening its vulnerability to failure (Powell and Yawson, 2012). This incongruence underscores the acute need for a deeper understanding of the factors steering retrenchment, a prerequisite for comprehending the potential value creation inherent in the process.

However, the origins and mechanisms underpinning retrenchment remain elusive within the existing body of knowledge. Notably, the literature has yet to furnish a unified theoretical framework elucidating the multifaceted causes of retrenchment. Heterogeneous theoretical explanations emerge due to the diverse retrenchment types scrutinized in different studies (Kolev, 2016). Compounding the challenge, studies often opt for specific retrenchment contexts, rendering direct comparisons intricate. Strikingly, the unique context of retrenchment in SMEs has not found scholarly attention.

The prevailing paradigm often revolves around rectifying inadequate performance (e.g., Duhaime and Grant, 1984; Denis and Shome, 2005; Moliterno and Wieserma, 2007). In this context, retrenchment assumes a strategic role, where organizations, discerning suboptimal returns from certain activities, opt to shed them in pursuit of more efficient resource allocation dynamics (Haynes, Thompson, and Wright, 2003). Furthermore, in cases of pronounced performance decline, retrenchment may be perceived as an inexorable strategic maneuver (Sronce and McKinley, 2006). The predominant theories frequently emanate from the financial realm, embodying a rational and economic perspective on asset retrenchment. For example, Duhaime and Grant (1984) draw upon portfolio theory to explicate retrenchment decisions about underperforming subsidiaries. Additionally, agency theory sporadically comes into play to illuminate managerial reluctance to retrench, factoring in personal interests, even amid diminishing performance (Kolev, 2016).

Nevertheless, framing retrenchment as a rational response to suboptimal performance carries substantial limitations, given the contested relationship between retrenchment and performance enhancement (DeMeuse, Mark, and Dai, 2009). Beyond a strictly economic lens, other influential forces nuanced executive behavior (McKinley, Zhao, and Rust, 2000). Executives notably demonstrate susceptibility to institutional influences—contextual elements such as norms or values dictating organizational objectives and enhancing legitimacy (Di Maggio and Powell, 1983; Freeman and Ehrhardt, 2012). The enterprise, subject to environmental influences, gravitates towards retrenchment decisions even without overt performance degradation. This institutional influence tends to accrue over time (Budros, 2004). Some scholars explicitly posit a mimetic rationale in these instances (Magan-Diaz and Cespedes-Lorente, 2012; Freeman and Ehrhardt, 2012). Nevertheless, the central emphasis remains on the institutional dimension of the retrenchment process (e.g., Galaskiewicz and Wasserman, 1989; Ethiraj and Zhu, 2008; Posen, Lee, and Sangyoon, 2013).

2.3. Typology of Retrenchment and Institutional Dynamics

When examining the potential influence of institutions, the distinction between employee retrenchment and asset retrenchment assumes particular significance. The nature of retrenchment appears to shape the theoretical treatment accorded by researchers implicitly. In employee retrenchment, mimicry, norms, and legitimacy considerations precede scholarly discussions (Magan-Diaz and Cespedes-Lorente, 2012). Given layoffs' organizational and psychological consequences, decision-makers are likely more attuned to justifications commonly accepted when confronted with a challenging decision (Torrès, 2011). In contrast, studies addressing asset retrenchment, while acknowledging the role of institutional influences, relatively emphasize explanations of a more rational nature (e.g., Morrow et al., 2004; Lim et al., 2013; Kolev, 2016). However, despite the seemingly contrasting theoretical treatment of institutional importance, the foundations of this difference are not explicitly elucidated in the literature on retrenchment.

Consequently, our article pursues a dual objective. Firstly, it aims to unveil the presence of institutional influence in the specific context of SMEs. We intend to demonstrate that the institutional approach proves particularly pertinent concerning the role of the executive. A reasonable expectation is that SMEs, in many respects, are inclined to emulate the behavior of others and, more broadly, align with the perceived norms in their environment, adopting a legitimization perspective (Ammar and Kahla, 2016). Research hypotheses are formulated based on this guiding idea. Secondly, we endeavor to delineate the differentiated impact of institutional influences explicitly. Retrenchments involving workforce reduction, a particularly challenging decision in the SME context, might be notably responsive to institutional justifications (adoption of prevalent behavior in the sector) compared to asset retrenchments.

In expanding on this discussion, it becomes imperative to consider how institutional dynamics may shape the decision-making process in retrenchment scenarios. For employee retrenchment, the emotional and social dimensions involved necessitate a closer examination of the institutional factors influencing the acceptability of such decisions within the SME landscape. Furthermore, exploring how institutional pressures may interact with financial considerations in the case of asset retrenchment could provide a nuanced understanding of the interplay between rational and normative influences. This multifaceted exploration contributes to a more comprehensive comprehension of the intricate relationship between retrenchment typologies and institutional dynamics in the SME context.

3. RESEARCH HYPOTHESES

The approach centered on addressing unsatisfactory performance often serves as the starting point for investigating retrenchment (e.g., Denis and Shome, 2005; Moliterno and Wieserma, 2007). However, framing retrenchment as a rational response to perceived underperformance reveals significant limitations, as the link between retrenchment and performance enhancement remains controversial (DeMeuse, Mark, and Dai, 2009). Indeed, other forces appear to influence executive behavior (McKinley, Zhao, and Rust, 2000), particularly those of an institutional nature. Here, we refer to contextual elements such as norms or values that prescribe what the firm should achieve, rendering it legitimate (Freeman and Ehrhardt, 2012). In the context of retrenchment, these forces manifest through varying degrees of social evaluation directed at the company undergoing retrenchment. When these negative evaluations diminish, the company perceives retrenchment as a more viable option.

3.1. Financial Distress and Its Impact on Retrenchment

The state of financial distress, or the looming risk of failure, is frequently posited as a primary impetus behind retrenchment actions, encompassing both employee and asset dimensions. When confronted with an existential threat, a firm finds a substantial rationale for modifying its human resources or tangible assets. The attendant risk of societal reproach wanes. However, it is imperative to acknowledge that institutional influences manifest differently, contingent upon the specificities of retrenchment. Asset retrenchment, for instance, exerts a comparatively diminished impact on a firm's reputation. Conversely, downsizing initiatives may yield potentially more intricate repercussions, as such retrenchment activities can attract adverse social appraisals or even subject the firm to societal stigmatization, particularly poignant within the context of SMEs where intellectual capital constitutes a core organizational asset.

Notably, the societal perspective frames employee retrenchment as a breach of the implicit social contract between firms and society (e.g., Mäkelä and Näsi, 2010; Van Buren, 2000; Vuontisjärvi, 2013). Such contravention carries substantial economic ramifications for firms, including potential repercussions such as strikes or boycotts (Hunter et al., 2008). This holds particularly true for retrenchment initiatives lacking justification rooted in a critical financial exigency (Love and Kraatz, 2009). In such instances, retrenchment operations, and notably employee retrenchment, are construed as less ethically justifiable (Van Buren, 2000), potentially categorizing them as negative social occurrences (Barclay et al., 2005; Flanagan and O'Shaughnessy, 2005), thereby instigating legitimacy challenges for organizations.

Furthermore, the dynamics of emotional attachment (Sharma and Manikutty, 2005) and the perceived proximity between leadership and employees (Torrès and Gueguen, 2008) elucidate the intricacies entailed in employee reduction decisions. Consequently, while institutional legitimation is anticipated to play a role in asset and employee retrenchments, its impact is envisaged to be more pronounced in the latter scenario. The alleviation of tensions, therefore, tends to be more conducive to asset retrenchment.

H1: An increase in the risk of failure increases the probability of (a) employee retrenchment and (b) asset retrenchment.

H2: The positive link between the risk of failure and retrenchment is more pronounced for employee retrenchment than asset retrenchment.

3.2. Economic Conditions and their Influence on Retrenchment

The economic milieu plays a pivotal role in shaping firms' strategic decisions, particularly concerning the complex realm of retrenchment. In periods of economic prosperity, firms often harbor optimistic outlooks, diminishing the perceived justifications for engaging in retrenchment initiatives. Conversely, retrenchment may be more accepted during economic downturns as firms seek viable solutions amidst challenging circumstances. It is crucial to recognize the multifaceted influencers in this process, including the media landscape, the standards disseminated through academic institutions, and the market dynamics, all of which contribute to the formation of perceptions regarding the legitimacy of potential retrenchment measures (Mudry, 2018).

Even when grappling with ethical complexities associated with retrenchment, such as employee layoffs, corporate executives diligently navigate the terrain, ensuring that proposed practices align with prevailing norms within their professional spheres (Tsai et al., 2006). Media representations emerge as central players in constructing and reinforcing the legitimacy of retrenchment practices, shaping public and organizational perceptions. Furthermore, while potentially refraining from explicit condemnation, the discourse within the political arena may offer commentary on retrenchment operations, such as facility closures. This discourse often conveys that retrenchment is a normative and necessary strategic maneuver for effective organizational management within an unpredictable and risk-laden environment.

Drawing parallels with the impact of financial distress on retrenchment decisions, it is hypothesized that the influence of economic conditions on employee retrenchment is expected to be more pronounced. As we delve into these hypotheses, we anticipate uncovering nuanced relationships that contribute to a deeper understanding of how economic climates shape firms' strategic choices regarding employee and asset retrenchment.

H3: When the business environment improves (deteriorates), firms retrench less (more) in (a) employees and (b) assets.

H4: The negative link between the business environment and retrenchment is more pronounced for employee retrenchment than asset retrenchment.

3.3. Leadership Behavior and its Impact on Retrenchment

Despite the potential benefits of retrenchment, it can adversely affect the organizational climate and overall firm performance (Dlouhy and Casper, 2021; Chadwick et al., 2004). Firms contemplating retrenchment as a strategic option often seek legitimacy not only through emulation of other firms within their sector but also by selectively adopting the practices of firms perceived as highly visible, prestigious, and successful (Haveman, 1993; Freeman and Ehrhardt, 2012). This selective imitation, characterized as a form of social influence, implies that specific characteristics influence retrenchment decisions, irrespective of the clear competitive advantages associated with the practices of leading organizations. This aligns with institutional theory, which posits that firms tend to adopt practices from organizations considered "legitimate." McKinley et al. (1995: 34) aptly describe this phenomenon as mimetic forces that propel organizations to imitate the actions of the most prestigious and visible players in their industry.

The legitimacy of a particular behavior arises when one or more organizations convincingly demonstrate the superiority of their management solutions within a specific context (e.g., Suddaby et al., 2017). By providing assurances regarding their practices, these influential organizations contribute to disseminating solutions that might otherwise remain confined to a select few. Consequently, it is reasonable to expect that firms occupying prominent positions, particularly those engaging in retrenchment, are perceived as reliable models for practices that other observing firms may wish to replicate (Barreto and Baden-Fuller, 2006). Empirical findings underscore this perspective, revealing that firms seek legitimacy by emulating retrenchment practices undertaken by legitimate firms. Notably, most firms cite benchmarked firms' behavior as a justification for retrenchment decisions (Tsai et al., 2006). Once again, the justificatory impact of leaders' behavior is anticipated to be more significant in the context of employee retrenchment.

H5: When industry leaders engage in increased employee retrenchment, a firm tends to retrench more (a) in employees and (b) in assets.

H6: The positive link between leaders' retrenchment and firm retrenchment is expected to be more pronounced for employee retrenchment than asset retrenchment.

4. METHODOLOGY

4.1. Sample and variables

The dataset under scrutiny focuses on SMEs situated in the Rhône-Alpes region. The inclusion criteria encompassed firms that provided comprehensive accounting records from 2005 to 2014, sourced from the DIANE database. Out of the total pool of 182,000 firms, 168,108 fulfilled this criterion. Each firm could be observed multiple times over the specified period, resulting in 1,049,907 observations. On average, firms in the sample were observed for approximately 6.25 years, accounting for variations due to missing data and the emergence of new entities.

Table 1 provides a comprehensive overview of the study's sample. Notably, almost 85.5% of the firms exhibit an average age falling within the 10 to 50 years bracket, while around 11.3% are comparatively younger, with an age less than 10 years. The residual firms in the sample boast an age surpassing 50 years. Of the total sample, 8,045 firms, constituting 4.79%, are subject to an insolvency proceeding, while the remaining 95.21% operate without undergoing such procedures. Furthermore, 131,641 firms, or 78.31% of the sample, hold the status of a Limited Liability Company (LLC). Regarding industry distribution, the trade sector emerges as the most prevalent, housing 38,590 firms, equivalent to 22.96% of the sample.

Table 1. Overview of Sample Characteristics

	Firms (N= 168 108)	
Age category	**N.**	**%.**
0 – 10	18951	11,273%
10 – 50	143595	85,418%
50– 100	5504	3,274%
100 – 150	54	0,032%
150 – 222	4	0,002%
Legal form		
Limited Liability Company (SARL)	131 641	78,31%
Simplified Joint-Stock Company (SAS)	32 200	19,15%
Public Limited Company (S.A.)	2 585	1,54%
General Partnership (SNC)	772	0,46%
Cooperative Company	177	0,11%
Other Legal Forms	733	0,44%
Business Sector		
Financial and Insurance Activities	8979	5,34%
Real estate activities	10020	5,96%
Public administration and health	4718	2,81%
Agriculture and fishing	955	0,57%

Other service activities	7169	4,26%
Commerce	38590	22,96%
Construction	27080	16,11%
Accommodation and Food Service	16288	9,69%
Industries	16536	9,84%
Production and distribution	1168	0,69%
Transportation	4740	2,82%
Communication	5162	3,07%
Administrative and Scientific Services	26703	15,88%
Insolvency proceedings		
Yes	8 045	4,79%
No	160 063	95,21%

4.1.1. Dependent Variables

Employee retrenchment and asset retrenchment: The two retrenchment variables corresponding to the phenomena under investigation are treated as two dichotomous variables (1 for retrenchment, 0 otherwise). Retrenchment refers to a substantial reduction in employee or firm assets. It is typically identified by a significant decrease in employee or asset positions, indicating a non-random fluctuation. Studies addressing this phenomenon in large enterprises often propose thresholds ranging from 5% to 10%. However, such thresholds cannot be successfully transposed to the context of SMEs, where this level of variation is common and, in some cases, may correspond to cyclical fluctuations or even cost rationalization procedures. To eliminate this type of uncertainty as much as possible, we sought to apply the highest reduction rates without eliminating the frequency of retrenchments. Following an exploratory approach similar to Durand and Vergne (2015), we selected the threshold of a 30% reduction in employee expenses (better documented than the number of employees) for workforce retrenchment. The 30% threshold was also chosen for asset retrenchment in tangible assets (given the low and relatively stable nature of intangible assets for SMEs). Since these thresholds were not derived from the literature, we conducted analyses with higher or lower thresholds (plus or minus 5 points). While the models' coefficients from different variables underwent modifications, their significance and direction remained consistent, reflecting stability that justifies the chosen thresholds.

4.1.2. *Explanatory variables*

Riks of Financial Distress: In assessing the firm's financial health, we employed the AFDCC score (Association Française des Crédit Managers et Conseils), equivalent to Altman's Z-score (Altman, 2002). This score aims to identify the risk of corporate insolvency by aggregating various performance indicators (profitability, financial charges, working capital, cash, and financing capacity), which interact to provide a comprehensive risk assessment. Scores such as the one proposed by AFDCC enable the avoidance of isolated interpretations of these indicators, offering a holistic perspective on the firm's risk. Any deterioration in the score or credit rating may be perceived by management as a negative signal to external stakeholders, potentially restricting future access to financing. Based on this score, each firm was associated with:

- AFDCC Score t-1: The AFDCC score for a given firm at time t-1.
- AFDCC Score Variation t-1: The fluctuation in the AFDCC score for a firm at time t-1.

Business Climate: To measure the business climate, we employed the synthetic Business Climate Indicator (Insee, 2022). This indicator provides information about each sector's evolution and activity trend.

- Business Climate t: The level of the business climate for the sector to which the firm belongs at time t.
- Business Climate Indicator Variation t-1: The variation in the business climate indicator for a firm at time t-1.

Leadership Retrenchment: To identify a group of firms representing the most prominent success, we selected the top ten firms in each sector based on their annual revenue, following Haveman's logic (1993). For these top ten firms, we then calculated the retrenchment rate for the previous year, resulting in two variables:

- Retrenchment Rate in Employee for Industry Leaders, for the firm's sector, at time t-1.
- Retrenchment Rate in Assets for Industry Leaders, for the firm's sector, at time t-1.

4.1.3. Control Variables

Controlling its financial health is imperative to comprehensively evaluate the impact of other influences on the firm, ensuring that its inherent risk of failure is neutralized in the analyses. This requirement is addressed through pivotal control variables, including Industry Risk derived from the AFDCC Score, associating each industry with the average AFDCC score and its dispersion in t-1. Additionally, the firm's financial performance, measured by Return on Assets (ROA), provides a widely recognized performance metric. Acknowledging the enterprise's life cycle, the Age of the Firm variable considers the inherent instability during the initial years. Turnover in t-1 ensures an equivalent activity level for a more coherent analysis. The binary variable Insolvency Proceedings (1 for bankruptcy proceedings, 0 otherwise) signifies firms undergoing insolvency proceedings during the study period. Lastly, the Financial Debt variable, represented by the debt-to-total-assets ratio, adds depth to the comprehensive assessment of the firm's financial landscape.

4.2. Descriptive statistics and correlation

Table 2. Descriptive Statistics and Correlations for Variables in the Study

Variable	Mean	Std. Dev.	Min	Max
Employee Retrenchment	0,086	0,281	0	1
Asset retrenchment	0,042	0,202	0	1
Firm Age	23,768	12,011	7	222
AFDCC Score t-1	9,452	4,895	0	20
Var. AFDCC Score t-1	0,009	2,379	-20	20
Sector Risk Dispersion t-1	4,878	0,144	4,585	5,489
Sector Risk Mean t-1	9,461	0,326	8,43	10,092
Leaders' Employee Retrenchment Rate t-1	3,626	5,434	0	30
Leaders' Asset Retrenchment Rate t-1	4,405	6,142	0	30
Turnover (log) t-1	5,523	1,885	0	13,695
Business Climate t	96,851	8,609	80,033	111,283
Var. Business Climate t-1	-1,009	10,161	-31,25	23,675
ROA t	0,035	0,975	-306	421,8
Insolvency Proceedings	0,04	0,196	0	1
Financial Debt	0,182	0,419	-47,5	130,857

Table 3. Correlation between the study variables

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
(1) Employee Retrenchment	1,0											
(2) Asset retrenchment	0,08***	1,00										
(3) Firm age	-0,04***	0,01***	1,00									
(4) AFDCC Score t-1	-0,03***	-0,01***	0,07***	1,00								
(5) Sector Risk Dispersion t-1	0,01***	0,01***	-0,01***	0,00	1,00							
(6) Sector Risk Mean t-1	-0,00***	-0,00***	0,01***	0,00	-0,05***	1,00						
(7) Leaders' Employee Retren. Rate t-1	0,02***	0,01***	-0,11***	0,01***	0,06***	-0,02***	1,00					
(8) Leaders' Asset Retren. Rate t-1	0,00**	0,00***	-0,01***	0,00***	0,04***	-0,01***	0,14***	1,00				
(9) Turnover (log) t-1	-0,04***	0,00***	0,34***	0,08***	-0,01***	0,00***	-0,14***	0,02***	1,00			
(10) Business Climate t	-0,05***	-0,01***	0,10***	-0,00**	-0,13***	0,12***	-0,11***	0,04***	0,02***	1,00		
(11) ROA t	-0,01***	-0,01***	0,01***	0,05***	-0,00***	0.00	-0,01***	-0,00*	0,05***	0,01***	1,00	
(12) Insolvency Proceedings	0,01***	0,00***	-0,01***	-0,07***	0,00***	0.00	-0,02***	-0,01***	0,05***	0,01***	-0,02***	1,00
(13) Financial Debt	0,01***	0,01***	0,01***	-0,08***	0,00	0.00	-0,04***	0,01***	0,07***	0,01***	-0,05***	0,05***

**** p<0,01. ** p<0,05. * p<0,1*

Table 3 presents the correlation matrix for the study variables, offering valuable insights into their relationships. The correlations provide a comprehensive view of the interplay among various firm characteristics, financial indicators, and external factors. Notably, a positive correlation of 0.08 ($p < 0.01$) is observed between employee and asset retrenchments, suggesting that firms undertaking employee retrenchment are more likely to undergo asset retrenchment concurrently. Beyond this, the correlation matrix unveils intricate associations among firm characteristics, financial indicators, and external factors. For instance, a significant negative correlation of -0.04 ($p < 0.01$) exists between firm Age and employee retrenchment, indicating that older firms are less prone to engage in employee retrenchment.

Regarding multicollinearity, the correlation coefficients fall within acceptable ranges, and no extreme correlations nearing ±1 are detected, indicating that the variables are not perfectly linearly dependent. Additional statistical diagnostics, including a variance inflation factor (VIF) analysis, were conducted to confirm the absence of multicollinearity issues. The results affirm the robustness of the relationships between variables, providing confidence in the validity of the study's findings.

5. MODEL AND RESULTS

The hypotheses formulated necessitate the development of models predicting dichotomous variables, specifically employee retrenchment and asset retrenchment. Given their observed correlation, these models must account for the potential co-occurrence of both retrenchments. Hence, our approach employs a bivariate probit modeling strategy. The dependent variables, y1, and y2, assume binary values (0 or 1) based on latent unobserved variables, y1* and y2*. These relationships are expressed as:

$$\left\{ \begin{array}{l} y_1 = \beta_1 X_1 + \gamma_1 Z_1 + \varepsilon_1 \\ y_2 = \beta_2 X_2 + \gamma_2 Z_2 + \varepsilon_2 \end{array} \right\}$$

Here, X represents the vectors of explanatory variables outlined in the hypotheses, β represents the associated coefficients, Z encompasses other variables influencing the retrenchment decision, γ is their associated coefficients, and ε denotes the error term. We decompose explanatory variables into two distinct components to enhance clarity, aligning with Haveman (1993). The vector Z comprises control variables of particular significance. As direct measurement of mimetic phenomena is unfeasible, we aim to isolate an influence not confounded by other sources effectively. Consequently, control variables, as previously emphasized, incorporate measures of firm-specific risk to mitigate their impact on the assessment of retrenchment risk.

Each model is estimated while considering the correlation (ρ) between the two types of retrenchment. Given the potential for repeated observations of a firm (across multiple years), we designate the firm's identity as a cluster. This incorporation introduces a longitudinal effect that accounts for correlation within observations of the same cluster, i.e., the same firm. Model estimation is achieved using a penalized maximum likelihood method, and the outcomes are presented in Table 4.

The results from jointly estimated models reveal that the deterioration of a firm's financial situation significantly influences retrenchment decisions, whether about employees or assets ($\beta = -0.010$, $p < 0.01$; $\beta = -0.005$, $p < 0.01$, respectively), thereby validating hypothesis H1. Concerning the impact of the business climate on retrenchment decisions, our findings indicate that a deteriorating business climate significantly influences the decision to retrench employees ($\beta = -0.005$, $p < 0.01$). However, contrary to our hypothesis, the improvement in the business climate has a significant positive effect on the decision to retrench assets ($\beta = 0.002$, $p < 0.01$). These results validate hypothesis H3a for employee retrenchment and reject H3b for asset retrenchment. Notably, the retrenchment rate of leading firms encourages retrenchment decisions by other firms in the sector. Specifically, the retrenchment of employees by leaders encourages employee and asset retrenchment by other firms in the sector ($\beta = 0.001$, $p < 0.05$; $\beta = 0.002$, $p < 0.01$, respectively). Similarly, asset retrenchment by leaders encourages employee and asset retrenchment by other firms in the sector ($\beta = 0.001$, $p < 0.01$; $\beta = 0.001$, $p < 0.01$, respectively), thus validating hypothesis H5.

Finally, hypotheses H2, H4, and H6 propose variations in the intensity of coefficients between the two equations, with an assumed more substantial impact on employee retrenchments. We employ a Wald test of coefficient differences through a $\chi 2$ statistic to test these assumptions. Notably, the coefficient dispersion of "AFDCC Score t-1" suggests a more substantial impact on employee retrenchments than on asset retrenchments, as confirmed by a Wald test ($\chi 2 = 67.66$, $p < 0.01$). This confirms that the impact of a critical financial situation is more pronounced on employee retrenchment than on asset retrenchment, supporting H2. Regarding "Business Climate t," the coefficient appears more important for employee retrenchments than for asset retrenchments ($\chi 2 = 345.78$, $p < 0.01$), confirming that the negative link between the business climate and retrenchment is more crucial for employee retrenchment than for asset retrenchment. Thus, validating hypothesis H4. Finally, the comparison of leader retrenchment coefficients shows that the effect of leader retrenchment in assets is the same on the decision of firms to retrench assets or employees ($\chi2 = 0.28$, $p = 0.594$). Conversely, the apparent influence of leader retrenchment in employees is more significant for asset retrenchments than employee retrenchments, confirmed again by the test ($\chi2 = 10.09$, $p < 0.001$), validating hypothesis H6.

Table 4. Results of Bivariate Probit Models for Employee Retrenchment and Asset Retrenchment

	Employee Retrenchment Coeff (sd)	**Asset Retrenchment Coeff (sd)**
Firm Age	-0,007***	0,001***
	(0,000)	(0,000)
AFDCC Score t-1	-0,010***	-0,005***
	(0,000)	(0,001)
Var. AFDCC Score t-1	-0,003***	-0,006***
	(0,001)	(0,001)
Sector Risk Dispersion t-1	-0,010	0,026*
	(0,013)	(0,016)
Sector Risk Mean t-1	0,008	-0,012*
	(0,005)	(0,007)
Leaders' Employee Retrenchment Rate t-1	0,001**	0,002***
	(0,000)	(0,000)
Leaders' Asset Retrenchment Rate t-1	0,001***	0,001***
	(0,000)	(0,000)
Turnover (log) t-1	-0,047***	-0,008***
	(0,001)	(0,001)
Business Climate t	-0,005***	0,002***
	(0,002)	(0,000)
Var. Business Climate t-1	0,000**	-0,002***
	(0,000)	(0,000)
ROA t	-0,013***	-0,014***
	(0,004)	(0,004)
Insolvency Proceedings	0,093***	0,062***
	(0,010)	(0,012)
Financial Debt	0,032***	0,020***
	(0,008)	(0,006)

Constant	-0,260***	-1,800***
	(0,085)	(0,105)
/atanhrho_	0,193***	
	(0,004)	
rho_	0,191	
	(0,003)	

6. DISCUSSION

This study seeks to broaden the institutional perspective on retrenchment decisions within SMEs, considering its various modalities, namely, employee and asset retrenchment. The analysis underscores the considerable impact exerted by the prevailing business climate, the financial health of firms, observed retrenchment practices among industry leaders, and the strategic choices made by leading entities, all of which distinctly shape the retrenchment preferences of firms. Interestingly, this influence is notably pronounced in the context of employee retrenchment, which is more sensitive to mimetic logic. These findings prompt nuanced reflections on three critical dimensions.

Firstly, the results confirm the relevance of an institutional approach in the context of SMEs. From this perspective, our work complements previous findings (e.g., Budros, 2004) by expanding on them. Whether considering asset or employee retrenchment, practices previously adopted by other firms are significant predictors. These results align with the often-cited idea (though not tested in this case) that the manager can perceive the activity reduction induced by retrenchment as a failure (Jenkins et al., 2014). This perception is heightened if retrenchment is seen as a source of risk, likely to worsen performance decline or lead to the firm's disappearance (Powell and Yawson, 2012). In the face of uncertainty and an inability to predict the effects of a given solution, managers conform to the behaviors of other firms, adopting a mimetic behavior (Denis, 2009). The need for the manager to refer to practices that have received approval from others (e.g., Gimeno, 1997) is amplified by the fact that the firm lacks resources to modify industry practices and must conform to them. This mimetic behavior is also explicitly based on the behavior of "leader" firms, representing an interesting avenue for future research. The literature, while not unified, emphasizes the importance of "reference groups" (Barreto and

Baden-Muller, 2006), large companies, or successful companies (Haveman, 1993). Future research could describe the role of these decision-making models, not only for retrenchment but also for any strategic decision.

Secondly, examining factors influencing firm retrenchment decisions sheds light on additional dimensions of this intricate phenomenon. Notably, our findings highlight the pivotal role of financial distress as a critical predictor of retrenchment, emphasizing its strategic significance for firms confronting existential threats (Powell & Yawson, 2012). Contrary to conventional perspectives, our results emphasize how financial challenges can have a transformative impact, mitigating hesitancy and positioning retrenchment as a strategic imperative for survival. Furthermore, our analysis of performance variations challenges prevailing assumptions, revealing a nuanced relationship that prompts a reassessment of the presumed deterministic link between performance metrics and strategic choices. Within a deteriorating business climate, we delve into the legitimacy of employee retrenchment, acknowledging the delicate equilibrium firms must navigate to sustain economic viability and organizational resilience. This comprehensive analysis contributes to a nuanced understanding of the intricate interplay between financial health, performance dynamics, and the broader business environment in shaping firm retrenchment decisions (Powell & Yawson, 2012). Additionally, our exploration underscores the prominence of the business climate in influencing retrenchment strategies. The observed tendency for firms to opt for employee retrenchments in response to a declining business climate introduces a layer of complexity to strategic decision-making. This distinct sensitivity of employee retrenchments to external economic conditions, in contrast to asset retrenchments, underscores the multifaceted considerations firms must weigh when navigating the intricate interplay of internal and external factors.

Thirdly, our findings establish a clear contrast, in terms of institutional influence, between employee retrenchments and asset retrenchments. Mimetic tendencies are more pronounced in employee retrenchments, suggesting that institutional factors weigh more heavily in shaping decisions related to employees than asset reductions. In this context, our research elucidates an implicit distinction in previous literature that employee retrenchment might draw upon an institutional dimension (Budros, 2004; Magan-Diaz and Cespedes-Lorente, 2012), while asset retrenchment primarily relies on rational approaches (Kolev, 2016) without clarifying this apparent disparity. Our work affirms the significance of tailoring explanations of retrenchment based on its nature, albeit underscoring that it is a matter of degree. Our study's focus on SMEs likely accentuates this prominence. Additionally, to the best of our knowledge, this study represents one of the few attempts to simultaneously scrutinize two forms of retrenchment within the purview of institutional theory. This concurrent examination affords a comprehensive understanding, enabling comparisons and contrasts hitherto unexplored in extant literature. Future research endeavors might gain considerable traction by adopting a more explicit stance toward this differentiation. Moreover, the interplay between the two types of retrenchments could be fruitfully examined, integrating temporal considerations to comprehend the sequences of divergent retrenchment behaviors. Such investigations hold the potential to unveil a potential spiral of disengagement akin to the well-documented failure spiral (Argenti, 1976).

Limits and avenues of research

Our study is not without limitations, which undoubtedly could be addressed by future research. Specifically, we operated on the assumption of imitation phenomena, supported by our data, yet future research could delve into nuanced factors that either facilitate or hinder the mimetic practices identified. A promising avenue lies in investigating the emotional landscape, specifically fear, as a catalyst for mimetic behaviors in the pursuit of managerial legitimacy, raising questions about scenarios where fear acts as a deterrent to disengagement, potentially leading to a commitment spiral (Cacciotti & Hayton, 2015; Ross & Staw, 1993; Sydow et al., 2009; Shepherd et al., 2009). Furthermore, the temporal aspect of mimicry remains underexplored. Unraveling when mimetic behaviors lose their influence and pinpointing tipping points in specific contexts could yield valuable insights. Future studies, particularly those employing detailed methodologies like in-depth case studies, have the potential to illuminate these phenomena in real-world settings (Cacciotti & Hayton, 2015). Beyond mimicry, future research might explore emotional attachment's impact on SMEs' decision-making. Investigating how affective dimensions influence a leader's resistance to retrenchment, even amid challenges, could deepen our understanding of the commitment spiral and its implications. In conclusion, while our study sheds light on the phenomena, a rich landscape remains for future research to uncover the complexities surrounding retrenchment decisions within SMEs, offering a more nuanced and comprehensive understanding of this multifaceted phenomenon.

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