

Institutional Influence on “Love Money”:

Informal Investment to Family, Friends, and Strangers across Countries

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Entrepreneurs have to rely on informal investment rather than banks to grow their business in the early-stage. Investments which fund family and friends (versus strangers) are regarded as supplying “love money.” Love is universal, but “love money” varies across nations; informal investors in developed, individualistic nations, such as the US, invest more readily in ventures of family than friends, whereas the reverse is true in East Asian nations. A research framework based on institutional theories and structural-functional theories on family is proposed to account for informal investment across nations. A multi-level study across 38 countries shows that poor legality and venture capital environment, prevalent early-stage entrepreneurship, less innovation, and strong family may explain the supply of “love money.” Implications of the findings to research and practice are discussed.

Entrepreneurs usually do not have enough startup capital, and they need to solicit funding from outsiders. Securing sufficient funding is essential to survival and the development of new ventures (Shane, 2009). Many studies have shown that most founders cannot rely on traditional channels, such as banks, so they have to turn to informal investors (Mason, 2006). Informal investors, including family, friends and angel investors (Wetzel, 1983), supply the scarce funding to founders during their setting up of new firms. Some studies have investigated the prevalence of informal investment across nations (e.g., Burke, Chantal, Stelb, & Suddleb, 2010; Landström, 1993). Informal investment is particularly important to early-stage ventures whose smaller size and higher risk are not palatable to venture capital. Thus, without informal investment, many new ventures would wither before they are large enough to attract the attention of institutional investors.

Current research has distinguished informal investment as angel investing and informal investing. The former does not include investment in businesses run by family and friends, which “will be influenced by the social relationship between the investor and the entrepreneur” (Shane, 2009: 18). Indeed investments from family and friends has earned it the nicknames “amateur investors,” “believer capital,” or simply “love money.” In other studies, family investment is regarded as different from friends’ and other investors (e.g., Erikson, Sørheim, & Reitan, 2003). In any case, scholars are concerned with their benefits to the society when public money is used to encourage informal investment from family and friends. They argued that lacking expertise and blinded by love, family and friends may pick inferior ventures to invest. As a result, their investment has higher failure and lower performance compared to high-impact ventures invested by professionals, like venture capitalists (Short & Riding, 1989).

The stake of informal investment is large because of its sheer size and its function. Each investment is small in size. But in aggregate the total amount of informal investment is multiple times larger than venture capital around different nations (Shane, 2010). Also, since

new businesses can introduce advanced technology, new business models, and new jobs (Headd, 2010), informal investors play a key role to bring innovation to the economy. To many developing nations, informal investment may even be the only source for emerging firms to obtain capital for shaping a new market for themselves. China, as an example, had informal capital driven its high growth despite poor institutions (Allen, Qian, & Qian, 2005).

This paper aims to serve two purposes. First, it strives to consolidate present research regarding “smart money” in venture investment by angels and “love money” in venture investment by family and friends. The discussion would cover research on different types of informal investment and the motives underlying their happening. This shall set the stage for the second objective of the paper, that is, to investigate the so-called “love money” (Shane, 2009). Whilst present research distinguishes “smart money” from “love money,” it often treats family money and friend money as the same and assumes that the same factors can explain their usage and performance. However, friendship and family love is not the same. Marriage and blood ties are inborn or prescribed; they bring identity and relationship and serve functions differently from friendship ties. Indeed, as detailed below, informal investors in developed, individualistic nations tend to invest in family rather than friends. On the other hand, East Asian nations, in spite of Confucian influence (Fukuyama, 1995; Weidenbaum & Hughes, 1996), prefer investing in ventures of friends.

Our observations are that informal investment across nations defies a simple explanation and deserves a careful theoretical analysis. In addition, if informal investment is an important source of initial capital, it does matter whether the money goes to family, friends and angels. This is because the initial capital structure of new firms can exert a path-dependent influence on the growth potential of the venture (Cassar, 2004). Investing in family’s new ventures would support more family businesses which may invest less in R&D (Ahlstrom, Young, Chan, & Bruton, 2004) and more in the socio-emotional aspects of the family (Gomez-Mejia, Haynes, Nunez-Nickel, Jacobson, & Moyano-Fuentes, 2007).

However, they may not create as many innovations and new jobs as policy makers desire from new ventures (Headd, 2010; OECD, 2010). The following will advance an explanatory framework, guided by the institutional perspective (e.g., Baker, Gedajlovic, & Lubatkin, 2005), regarding whom informal investors invest their money. Results of empirical testing are also reported. Before introducing this framework, we first give more detail on informal investment across nations.

Informal Investment across Nations

In over 30 countries, capital from family members—parents, siblings, uncles, and the like—accounts for 42% of informal capital (Bygrave, 2005). Friends and neighbors make up the next biggest group, contributing 29% of informal investment. Angels or strangers represent a small portion. Thus, among informal investors, the dominant group providing financing is family followed by friends. Yet, this is not the same across all countries. For instance, Au and Kwan (2009) have pointed out that friends are preferred to family in Hong Kong, Shenzhen, Singapore and even other Chinese communities (Zimmer & Aldrich, 1987). They found it surprising that informal investment to friends is preferred to family because family is central in these Confucian societies, and business is conducted in family context (Ahlstrom et al., 2004; Fukuyama, 1995).

We extended the observation to include other countries based on the GEM 2007 data (enhanced through bootstrapping).¹ As shown in Figure 1, the findings do not show a simple picture. For example, India has more family investors than friend investors, while Switzerland shows the reverse pattern. Surprising also, friends are preferred in other East Asian nations, such as Japan and China, whereas family is preferred in European and South American nations. Noteworthy is the US. It shows a preference towards family instead of friends or angels. This is against the common belief of the US as a country with individualistic characters striving to go independent on themselves or with their peers rather than the parents or the family. By inspection, the differences

between family and friends vary across countries that do not go along clearly with economic development and human value. The observed patterns are beyond one or two factors may explain.

Informal Investment in Institutional Perspective

Informal investment is reminiscent of new venture enterprising. The difference is that entrepreneurs are from the sell-side or supply-side whereas investors are from the buy-side or demand-side (Shane, 2009). Like entrepreneurs, investors must make good use of business opportunity. We derived a discourse of explanations on informal investment across countries by extending the entrepreneurial process model revolved around new business opportunity (Shane & Venkataraman, 2000). As Baker, Gedajlovic, and Lubatkin (2005) puts it, “a nation’s social context (i.e., its institutional and cultural structures) strongly influences the character of opportunities and the individuals who discover, evaluate, and exploit them” (p. 493). That is, the social context or the institutional environment influences the three activities in the entrepreneurial process. Opportunity discovery refers to the matching of enterprising individuals with the stocks of information and knowledge through which they might discover opportunities. Opportunity evaluation may refer to how investors evaluate the benefits out of a discovered opportunity. Furthermore, opportunity exploitation refers to how and from where investors pursue favorably evaluated opportunities.

Since institutionally-dictated reference points affect the above three activities (Baker et al., 2005), we will discuss why different types of informal investment vary across nations based on the idea that institutional factors affect how investors discover, evaluate and exploit business opportunities. Busenitz, Gómez and Spencer (2000) have shown that there exist regulatory, cognitive, and normative dimensions in institutional systems related to entrepreneurship. These three “pillars” in institutional theory are commonly used to conceptualize national environment in international management (e.g., Kostova, 1999; Xu & Shenkar, 2002). We will discuss and propose hypotheses on how the three “pillars” affect informal investment. The discussion will start with

legality theory (e.g., La Porta et al., 1997) on which present studies have shown the benefits of good legal environment on venture investments and economic development. It gives a blanket explanation on why good institutions facilitate angel investment compared to investments from family and friends. The discussion on the cognitive and normative dimension will then follow. Last but not least, family as an essential institution is highlighted separately given the purpose of this paper is on love money (Aldrich & Cliff, 2003; Steier, 2009). We strive to explain how family differs from friends in their informal investment guided by a structural-functional view of the family. Table 1 summarizes the discussion in a grid.

Regulatory Dimension of Institutions on Informal Investment

Following the framework of Busenitz, Gómez, and Spencer (2000), the regulatory dimension may be regarded as laws, regulations, and government policies related to informal investment. Studies in law, finance, and entrepreneurship has suggested that good legal systems lower the monitoring costs of entrepreneurs, so that they could look beyond their personal scope for opportunities and maximize their benefits (La Porta et al., 1997; Pollak, 1985). In a recent study, Cumming, Schmidt, Walz (2010) studied venture capital in 39 countries. They found that better laws facilitate faster deal screening and better deal governance to reap higher benefits out of the investments. The reason is that good legal systems lower transaction costs, such that investors can find, evaluate, and exploit opportunities from any sources, usually looking for better deals. In contrast, inefficient legal systems hamper the rate of investment and ability of a fund to properly manage deal flow and the financing of meritorious entrepreneurial firms, as bad legal systems increase transaction costs to investors when they try to use legal instruments to monitor and enforce deals. Thus, investors may become wary of investing in people they do not know well. Thus, they would rely rather on personal relationships and means to monitor and control for business deals.

Like venture capitalists, informal investors can also benefit from good legal systems. They may also reap benefit when they look for opportunity beyond personal relationship, even though informal investments are less structured and legally intensive with more personal judgments involved (Mason, 2006), informal investors also need to monitor entrepreneurs just like venture capitalists. They also need to do due diligence, negotiate and formulate a deal with entrepreneurs through legal means (Shane, 2009). Thus, even though personal touch plays a more important part in informal investment, good legal systems would give informal investors an incentive to look beyond deals from people they do not know instead of just from friends and family.

People invest to get a good return. Benign legal and regulatory systems are important for ventures to grow, but eventually informal investors want to exit and benefit from appreciation of assets in the venture (Shane, 2009; Wetzel, 1983). However, informal investors on family ventures are less interested to exit, as they usually hold different investment objectives, such as maintaining long-term security of the family (Erikson, Sørheim, & Reitan, 2003; Redding, 1990). Thus, since informal investors can exit easier, a country with policies and regulations that facilitate financial exit, such as IPO and trade sale, would induce more people to invest in ventures not from family.

H1a: Better legal systems render informal investors to favor investments of strangers rather than that of family and friends.

H1b: Better exits for ventures render informal investors to favor investments of strangers rather than that of family and friends.

Cognitive Dimension of Institutions on Informal Investment

The cognitive dimension refers to the knowledge and skills related to informal investment (Busenitz, Gómez, & Spencer, 2000). Informal investors can find and discover more opportunities

if good knowledge on entrepreneurship and informal investment are commonly available. If entrepreneurial knowledge is common, founders of new ventures do not rely merely on their ingroups to get access to such knowledge. Other things being equal, founders can form new ventures with strangers and friends just as readily as with family, and they can find more and probably better opportunities (Brehm & Rahn, 1997). Informal investors are thus more likely to find good opportunities regardless the origin of the ventures (Shane, 2009). This agrees with the finding that active startup activities in a country can boost informal investment (Burke et al., 2010). By the same token, given common knowledge in society on new venture investing, informal investors can exploit and reap the benefits of ventures of strangers and friends more readily than merely from ventures of family. Therefore, the better the knowledge in entrepreneurship and informal investment, the more likely informal investors would favor ventures other than from family.

H2a: Better knowledge on entrepreneurship renders informal investors to favor investments of strangers rather than that of family and friends.

H2b: Better knowledge on venture investing renders informal investors to favor investments of strangers rather than that of family and friends.

Normative Dimension of Institutions on Informal Investment

Following the framework of Busenitz, Gómez, and Spencer (2000), the normative dimension may refer to support to informal investment and admiration on creativity and innovation. “Love” money is meant to support friends and family, and has less to do with making a lot of money and advancing new ideas (Erikson, Sørheim, & Reitan, 2003). That is why informal investors investing in friends and family are criticized as amateur investors, and researchers have shown that they are ineffective in their investment and waste public money (e.g., tax recession) not

be used to subsidize their investments (Scott, 2009; Short & Riding, 1989). Indeed, optimizing return by investing in the best creative ideas and innovative technology is not the primary objective of investors investing in family ventures (Erikson, Sørheim, & Reitan, 2003). Family businesses, though capable of innovation, are more often regarded as competing in relationship-based and relatively stable businesses (Craig & Moore, 2006; Steier, 2009). Thus, we would expect people in nations with an admiration of innovation and growth to favor investing in strangers' ventures rather than ventures of friends or family's. Since investing in companies of the latter group would promote conservative venture and would not serve the purposes of innovation and growth, we propose the following:

H3a: More innovation renders informal investors to favor investments of strangers rather than that of family and friends.

H3b: Strong expectation on growth renders informal investors to favor investments of strangers rather than that of family and friends.

Family as an Institution Affecting Informal Investment

Family may mean a nuclear two-generational group sharing the same household who fulfill familial functions together. This structural-functionalism view of the middle-class family, though limited in scope (Aldrich & Cliff, 2003; Ingoldsby & Smith, 1995), spells out the common understanding and the analytical elements of a family. Recent developments in society have led to family changes, but Aldrich and Cliff (2003) argues that family continues to play an indispensable role in new business venturing. Their family embeddedness perspective on new venture creation posits that three sets of family system characteristics affect venture creation processes and venture outcomes. These characteristics are related to the procreation, economic, and socialization functions that the family performs across nations (Georgas et al., 2006; Murdock, 1949). The first set of

family system characteristics includes structure, roles and relationships, such as size, divorce, and relationships in the family. The second set refers to monetary, personnel, and physical space as resources the family can offer in the startup process. The last set may refer to family values and norms regarding interaction between family members, security, and career.

Friends differ from family members as they do not share consanguineous ties, family identity, and growth experience in a family. Yet, friendship is by all means important to people. Other than procreation, humans spend precious time with friends and rely on them for satisfying expressive and instrumental needs. These needs would include funding support in the startup process (Hoang, & Antoncic, 2003; Zimmer & Aldrich, 1987). Family and friends, together with angels, play a complementary role in supplying initial capital to entrepreneurs. We suggest that as family varies across nations as an important institution (Georgas et al., 2006; Harrell, 1997), its participation and role would vary vis-à-vis that of friends in providing initial capital. Focused on the three characteristics of family system, we discuss how family compared to friends affects investors in opportunity discovery, evaluation, and exploitation and propose three research hypotheses for testing.

The structure of a family would affect opportunity discovery, that is, how investors match with information to discover possible opportunities. Integral families, compared to disgruntled families, would mean more meetings between family members. The interchange between members would also be more in-depth, interest-sharing, and risk sharing. As a case in point, Chinese families are reported to be active in providing funds to startups of family members (Redding, 1990; Whyte, 1996). In an indepth case in Canada, Steier and Greenwood (2000) documented how a family gathering can allow ideas exchange, opportunity discovery, and then family investment first, followed by that of friends and neighbors. Investors have limited funds to invest. Whilst friendship networks can provide the same function as family (Zimmer & Aldrich, 1987), strong family acts as a platform for opportunity discovery, if not as replacement, of friendship networks. We therefore propose that:

H4a: More family strength renders informal investment to favor family rather than friends.

After its discovery, opportunity is evaluated by investors to see if it can really bring benefit to them. Families develop different values and norms regarding the interaction, the career, and the security needs of members. Due to historical, cultural and social factors (Yang, 1998), families of different societies vary in its importance and closeness to family members. A family from society where family is central or close would mean that it tends to view the success of its members of higher significance in terms of, say, serving the security and career needs of its members. This also means that the family can share the benefits and success more readily (Yang, 1988). Investors from such kind of families would therefore evaluate investment to opportunity of family members' as bringing in more benefits comparing to that of friends. Thus, we propose that:

H4b: Higher family importance renders informal investment to favor family rather than friends.

Opportunity can be discovered for bringing in benefit, but the investor would need to exploit the opportunity which requires various resources. An important reason why entrepreneurs have to go to friends for resources is probably because their family has no resources and ability to invest or bear the risk. This is particularly true for countries whose household income and accumulated family wealth are low. Due to imperialism and wars, China and India, for example, do not have a real entrepreneurial-class or middle-class until rapid development occurs in the past two decades (Allen, Qian, & Qian, 2005). In comparison, in developed nations, such as Europe, many families, even if people are just working class, their families have stable income and could have accumulated some wealth through savings, bequest or long-term investment. These families may also have network and space resources that they can contribute for its family members for successfully

pursuing their business opportunity. These family resources are less likely to be made available to friends. Such resources are also difficult to come by in their developing nation counterparts. In short, families from more wealthy countries would have more resources to provide to their family members for exploiting opportunity. Thus, we propose that:

H4c: More wealth in family renders informal investment to favor family rather than friends.

Method

To test the institutional influence on informal investment direction across countries, we utilized data from several reliable sources. We used the individual data from the Adult Population Survey of the Global Entrepreneurship Monitor's (GEM 2007)². GEM carried out surveys around the world by multiple national teams since the late 1990s. The data from GEM has contributed to a growing number of papers (e.g., Bowen & De Clercq, 2008). The country-level data come from several credible sources, including the World Bank Governance report, World Bank country profile data, GEM expert survey, and World Value Survey.

Dependent Variable

The dependent variable is the relationship between informal investors and their investees. The GEM adult population survey asked the participants, "What was your relationship with the person that received your most recent personal investment?" Participants chose one among the categorical answers: 1= Close family member, such as a spouse, brother, child, parent, or grandchild; 2= Some other relative, kin, or blood relation; 3= A work colleague; 4= A friend or neighbor; 5= A stranger with a good business idea. For the research purpose of differentiating investing in strangers, friends and family, we recoded original data into three categories: family (the original "1" and "2"); friends (the original "3" and "4"); and strangers (the original "5"). In final

² The website for GEM project: <http://www.gemconsortium.org/>

sample, on average, 54.4% have invested in family, 38% have invested in friend, and 7.6% have invested in stranger. They were tested in multinomial distribution models (3 categories).

Independent Variables

Regulatory Institutions. For informal investment, we divide the regulatory institutions into legal system and investment exit. Legal system is indicated by the Governance index, from the World Bank's worldwide governance project. The project aggregated individual governance indicators for 213 economies over the period 1996–2009, for six dimensions of governance: Voice and Accountability, Political Stability and Absence of Violence, Government Effectiveness, Regulatory Quality, Rule of Law, Control of Corruption. We take the average of these six indexes as our legal system index in this study. The Cronbach alpha is 0.95.

Investment exit was indicated by total amount of venture capital committed in 2006 by each nation. To supplement the results, we add one more indicator for investment exit: Financial environment related with entrepreneurship, which is derived from the GEM expert 2007 (Bowen & De Clercq, 2008). Most of the informal investments will try to exit by trade sale, merged with other firms, and management buy-out, all of which aim to be listed in an IPO. Therefore, the financial environment for such exit is very important to informal investment.

Cognitive Institutions. Knowledge on entrepreneurship was proxied by the Total Entrepreneurship Activities (TEA) index from GEM report 2007. TEA measures the proportion of a nation's adult population engaging in entrepreneurial activities, including starting-up a business or running a newly formed business. TEA index has been used in several important papers (e.g., Bowen & De Clercq, 2008). Knowledge on venture investing was proxied by the informal investor prevalence ratio (INV), from GEM report 2007. INV measures the proportion of a nation's adult population having personally provided funds for a new business started by someone else, excluding any purchase of stocks or mutual funds.

Normative Institutions. For innovation, we used the Innovation subindex from Global competitiveness report 2006-2007. The Innovation subindex was calculated by combining the survey data, including technological readiness, firm-level technology absorption, company spending on research and development, and university/industry research collaboration, and hard data, including utility patents, and tertiary enrollment.

Expectation on growth was proxied by the High-Growth Expectation Early-Stage Entrepreneurship (HEA) index, which is the prevalence rate of new and nascent entrepreneurs who expect their business to employ at least 20 people in five years' time in the adult population. HEA is also derived from GEM report 2007. We also use the GDP growth to supplement the analysis, since GDP growth is also an indicator for expectation on growth. GDP growth 2007 was taken from the World Bank annual country data.

Family systems. This set of variables included family strength, family importance, and personal wealth. Family strength was proxied by the divorce to marriage ratio (e.g., Cullen et al., 2004), aggregated by the World Bank database (2005-2007). Family importance index comes from WVS 2005-2009 wave survey. The index is measured as the percentage of individual who answers "very important" to the question "do you think family is important to you" (1 = very important; 2 = rather important; 3 = not very important; 4 = not important at all). Family importance has been widely used in previous research (e.g., Bertrand & Schoar, 2006). Personal wealth was proxied by GDP per capita since there is no direct measure of personal wealth in these countries. The GDP per capita data comes from the World Bank database (2007). Household wealth would be a better proxy but we could not find data from enough countries.

Control variable

As to control variables, we control for individual differences in terms of gender, age, education, and income, Gender was measure by 0=male and 1=female. Age was measured by 7 categories. Education was measure by asking their education attainment in three categories: 1=

secondary and lower; 2= post secondary; 3=graduate and above. Income was measure by asking their household annual income and was grouped into 3 categories. For the country level variable, we control economic size (log GDP). GDP was derived from the World Bank database 2007.

Results

Table 2 shows the summary statistics and correlations. This study tested the multi-level effect of environmental factors on informal investment direction, and Hierarchy Linear Modeling (HLM) was used. Using the cross-level model, we captured the influence of the higher-level factors on individual behavior. A two-level model, in which level-1 was individual level and level-2 was country-level, was specified in this study. For all the models, at level-1, we included individual-level control variables and dependent variable; at level-2, we entered GDP (log) and the testing variables. For Hypotheses 1 to 3, “strangers” was the reference group to compare with family and friends.

Table 3-6 presents the results. For Model 0 in Table 3, we included the level-1 control variables and the results supported that there is significant between-country variance ($\gamma = 1.979, p < .001$; $\gamma = 1.614, p < .001$). In other words, there is significant between-country variance in the informal investment direction to be explained by country-level predictors.

Regulatory Institutions. In order to test whether good legal systems have an effect on the investment direction of stranger versus family and friend, we put the world bank governance indicator at level-2, with data of 38 countries. As shown in Table 3, in a country with better legality and governance systems, people tend more to invest in strangers, rather than to invest in family ($\gamma = -.421, p < .01$) or friends ($\gamma = -.298, p < .1$). Therefore, Hypothesis 1a receives support.

Hypothesis 1b states that better exits for ventures render informal investors to favor investments of strangers rather than that of family and friends. The results showed that when there are plenty investment of venture capital in the country, informal investors tend more to invest in strangers rather than invest in family member ($\gamma = -.002, p < .01$) or friends ($\gamma = -.002, p < .1$). Also,

in a country with better financial environment supporting entrepreneurship (judged by GEM experts), people tend more to invest in strangers rather than invest in family ($\gamma = -.561, p < .05$) or friends ($\gamma = -.599, p < .05$). Accordingly, hypothesis 1b also receives support.

Cognitive Institutions. Hypothesis 2a suggests that widespread of entrepreneurship knowledge promotes more investments to strangers. The results, presented in Table 4, show that TEA has a positive effect on both paired comparisons that in a high TEA country, people tend more to invest in family ($\gamma = .074, p < .001$) and friend ($\gamma = .083, p < .001$) rather than strangers. The results are opposite to Hypothesis 2a. Furthermore, for knowledge on venture investing, we found that investment prevalence rate does not exert a direct effect on informal investment direction. Hypothesis 2b is not supported.

Normative Institutions. We used innovation and expectation on growth to test the influence of cognitive institutions on informal investment direction (see Table 5). The results turn out that in a more innovative country, individuals tend more to invest in strangers rather than family ($\gamma = -.313, p < .001$). But there is no significant different between the propensity of investing in stranger and friend in countries with varied innovation level ($\gamma = -.151, p = .199$). Therefore, Hypothesis 3a is partially supported. For growth expectation, we found that High-Growth Expectation Early-Stage Entrepreneurship (HEA) does not influence the investment direction between family and stranger ($\gamma = .066, p = .439$). But in high HEA country, people tend more to invest in friends compared to strangers ($\gamma = .231, p < .05$). Lastly, for GDP growth, which indicates the general expectation to new venture and investment results related the general economic development, the results show no effect of GDP growth on investing in strangers and family ($\gamma = .042, p = .203$), and that in strangers and friends ($\gamma = .058, p = .137$). Hypothesis 3b is not supported.

Family systems. Different from the above analysis, “family” was the reference group to compare with strangers and friends for the sake of presentation. To test Hypothesis 4a, we entered the family strength index at level-2. The results show that family strength, indicated by the divorce/marriage ratio, does not exert an effect on the investment direction between friends and

family ($\gamma = .071, p = .763$), but have a positive effect between strangers and family ($\gamma = 1.693, p < .01$). That is to say, when the family strength is strong, people tend more to invest family compared to stranger, but show no significant tendency between friend and family. Hypothesis 4a is partially supported.

To test Hypothesis 4b, we used the same procedure to examine family importance. The results show that family importance has a negative effect between investing in friend and family ($\gamma = -.012, p < .01$). So, in a country with high family importance, people tend more to invest in family rather than friends. But people tend more to invest in stranger than family ($\gamma = .030, p < .10$), although it is only marginally significant. Thus, Hypothesis 4b is partially supported. Lastly, to test Hypothesis 4c, we entered personal wealth into our model. The results show that in the country with average high personal wealth, people tend more to invest in stranger ($\gamma = .001, p < .01$) and friend ($\gamma = .001, p < .05$) compared to investing in family. Hypothesis 4c is not supported.

Discussion

This study came out of the observation that informal investors across nations show different preferences in funding new business ventures of family, friends, and strangers. Such pattern of preferences is not simple and defies a straight-forward explanation. Previous studies investigated the prevalence of the informal investment in a simple theoretical framework (e.g., Burke et al., 2010), and do not distinguish the targets of the investment. Guided by institutional theories, this study explored several explanations and found some interesting results to shed light on this neglected area. It contributes theoretically and empirically on why nations channel so-called “love money” for new business ventures. It also gives hints on why “love money” invested in ventures of family and friends is not the same. Given that informal investment is large in total amount and initial capital structure exerts a path-dependent effect on the development of a new venture, the findings demonstrate some practical implications as well.

Based on the findings, we affirmed that good legal and financial environment promotes more informal investment to strangers (or angels) compared to investment to family and friends. Lower transaction costs to invest and exit renders informal investors to see less need and advantage in investment on friends and family (Cumming et al., 2010; Steier, 2003). In addition, more innovative nations tend to have more investment on strangers than on family and friends. This fits with the nature of “love money,” which is to provide support rather than profit-maximizing or advancing major impact to society. Different from what’s expected, more early entrepreneurial activities (TEA) are actually related to more investments to friends and family. We expected that more activities actually suggest that entrepreneurship is wide-spread and thus conducive to investing in ventures of strangers. This result requires further testing and examination with more confounding effects controlled. For one thing, TEA is related negatively to GDP per capita.

Turning to variables related to family systems, it is found that family strength (divorce/marriage) explains why investors in some nations prefer family ventures to strangers’. However, it does not explain that between family and friends. On the other hand, the importance of family in a nation does explain why informal investors tend to invest in family instead of friends. This finding is what’s expected. However, personal wealth (as a proxy to family wealth) shows an effect opposite to our expectations. Investors in more wealthy nations tend to put their money in strangers and friends rather than family. We thought that more wealth in family may mean that the family can afford to invest in members’ ventures. Perhaps, the finding suggests that investors in poorer nations need to support their members more, as other channels of funding is even less available as in wealthier nations.

Despite its possible contribution, this study is only a beginning for understanding institutional influences on informal investment across nations. There are many aspects of the family under the scrutiny of the structural-functional theories, but this study discussed and tested only a handful of them. Other aspects related to the structure, values and norms, and resources of the family (Aldrich & Cliff, 2003), for instance, size of household, financial role of parents, and family

networks, shall be investigated. Particularly, the socio-psychological aspects of family can be a fruitful area. The present analysis of family business and informal investment inclines towards transaction costs and agency theories (e.g., Pollak, 1985; Steier, 2003), and pays less attention to the social and emotional side (Mason, 2006), such as personal autonomy of family members (Au & Kwan, 2009). In a 30-nation study on families, Georgas et al. (2006) documented the emotional distance as well as financial roles of the parents and other members of the family. Their rich data can be used in future studies on informal investment to investigate family ventures and other aspects of family business. Obviously, structural-functionism is merely one genre of theories on family. Social exchange theory and family systems theory (Ingoldsby & Smith, 1995), for example, shall also be considered in future research on informal investment. Lastly, this study confirms that family as an institution can play a major role in influencing informal investment across nations. However, the findings also show that family is far from the only institution useful for understanding informal investment. Institutional profiles of entrepreneurship, i.e., regulatory, cognitive, and normative (Busenitz, Gomez, & Spencer, 2000; Bowen & De Clercq, 2008) vary across countries, and shall be studied in future studies.

An exploratory research like this study is inevitably limited in scope and generalizability due to its restricted choice of data and variables. Using data sets other than GEM and alternative compilation of variables, for example household wealth, may lead to more substantial and positive results. Besides, we must be cautious with the causal direction in interpreting the findings; for instance, whether more innovations lead to less investment on family ventures, or the other way around. Yet, keeping such weaknesses in mind, the findings point to two practical aspects of interest. First is that a regulated legal environment and governance is not just good for developing large corporations and venture capital industry. It facilitates investment to new ventures of strangers and thus benefits angel investment in the country. To the extent that angel investment brings more technology and innovative businesses instead of existing, stable businesses (Erickson et al., 2003; Short & Riding, 1989), many governments would desire more angel investment.

To business families, the perceived importance of family and family strength, or so-called familism value (Yang, 1998), turn out to be a driver behind why people invest in family's new ventures. Au and Kwan (2009) argues that if Chinese continue to invest in friends' business instead of family's, the dominant landscape of Chinese family businesses will change in the future. They may be right. But if love in family is what is important (Jaffe, 2000), there is every reason for families to invest in new business ventures of the family. The question is how love will remain or even blossom in light of the rapid change in institutions and the society (Georgas et al., 2006; Yang, 1988). The findings here come from societal level analysis, but they may have some implications for entrepreneurs who want to solicit funding from family members. Family is usually less interested in innovative products but more interested to support family members. The closer the family, the stronger is the support. Entrepreneurs should understand this nature and pledge their case with a reason to support. They may also have more success if they pitch mundane business ideas or try to wrap ideas on innovative products with a message appealing to ordinary products.

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Table 1: Informal Investment as a Function of Relationship with the Informal Investor

Country	Family (%)	Friends (%)	Stranger (%)	Other (%)
United States	45.0	27.4	7.2	2.9
Russia	49.6	49.7	0.0	5.2
Greece	40.6	57.3	0.0	0.0
Netherlands	36.5	37.4	12.6	3.5
Belgium	56.3	24.5	8.8	3.4
France	42.4	29.8	11.5	11.4
Spain	59.8	34.1	1.4	1.7
Hungary	26.3	84.7	5.2	0.0
Italy	64.5	37.2	2.8	8.9
Romania	34.2	20.6	0.7	11.6
Switzerland	39.9	45.4	9.8	5.6
Austria	36.8	24.3	7.6	7.8
United Kingdom	57.7	46.0	4.1	1.9
Denmark	36.3	27.4	17.1	8.7
Sweden	56.5	36.0	2.7	1.6
Norway	29.7	33.6	14.3	3.7
Peru	62.9	40.1	0.5	0.0
Argentina	38.4	32.3	5.5	1.1
Brazil	73.8	23.2	0.0	5.7
Chile	61.7	33.4	1.3	1.1
Colombia	55.9	41.9	0.0	5.7
Thailand	53.9	45.0	0.8	0.0
Japan	18.2	51.6	7.0	0.0
China	42.0	47.6	4.6	2.7
Turkey	65.2	38.1	1.2	0.0
India	50.0	14.9	2.6	9.3
Portugal	42.8	32.9	6.6	14.4
Ireland	77.1	46.4	10.7	0.0
Iceland	34.5	41.9	11.1	2.4
Finland	48.4	36.8	10.3	5.0
Latvia	18.5	35.2	13.6	0.0
Serbia	50.6	41.8	5.3	0.0
Croatia	44.7	14.3	15.7	0.0
Slovenia	44.5	47.6	4.2	0.0
Venezuela	73.4	21.3	0.0	0.0
Uruguay	60.8	49.2	4.2	1.7
Kazakhstan	57.9	34.2	6.3	0.0
Puerto Rico	87.4	31.1	4.6	0.0
Hong Kong	43.0	54.9	0.9	0.0
United Arab Emirates	37.4	32.9	7.6	0.5
Israel	43.8	29.6	15.0	0.0
Dominican Republic	54.8	49.6	1.7	2.0

Table 2: Descriptive Statistics of the Variables

Variable	Means	s.d.	No	1	2	3	4	5	6	7	8	9	10	11
<u>Level 2</u>														
1. H1a-Governance	0.70	0.84	38											
2. H1b-VC	186.29	271.85	20	0.216										
3. H1b-Financial Environment	2.90	0.47	27	0.300	-0.202									
4. H2a -TEA	9.02	6.26	38	-0.532 ***	-0.326	-0.001								
5. H2b-INV	4.54	4.61	38	-0.220	-0.304	0.146	0.279 +							
6. H2c-Opportunity	3.40	0.31	27	0.176	-0.089	0.478 **	0.470 *	0.460 *						
7. H3a-Innovation	3.58	1.13	37	0.711 ***	0.157	0.453*	-0.432 **	-0.347 *	0.264					
8. H3b-HEA	1.11	0.96	38	-0.257	-0.156	-0.304	0.452 **	0.211	0.192	-0.333 *				
9. H3b-GDP Growth	5.28	2.91	38	-0.651 ***	-0.094	-0.123	0.495 ***	0.437 **	0.132	-0.613 ***	0.434 **			
10. H4a-Family Strength	0.38	0.21	29	0.297	0.289	0.491 *	-0.367 *	-0.270	0.283	0.213	-0.260	-0.138		
11. H4b-Family Importance	87.78	8.19	23	-0.117	-0.027	-0.080	-0.254	-0.124	-0.251	0.184	-0.392 +	-0.303	-0.084	
12. H4c-Wealth	27802.79	21585.47	38	0.839 ***	0.046	0.356+	-0.444**	-0.269+	0.140	0.706** *	-0.211	-0.570 ***	0.192	0.019
<u>Level 1</u>														
Variable	Means	s.d.	No	13	14	15	16	17						
13. Gender	1.40	0.489												
14. Age	4.14	1.32		0.020										
15. Education	1.80	0.85		-0.016	-0.019									
16. Income	2.12	0.79		-0.070 ***	0.057 ***	0.254 ***								
17. Investment Direction	1.53	0.64		-0.168 ***	-0.061 ***	0.053 ***	0.045 **							

Table 3 Hierarchical Linear Modeling Results for Regulative institutions

	Model 0 ^a		Model 1 ^b		Model 2 ^c		Model 3 ^d	
	C1	C2	C1	C2	C1	C2	C1	C2
Intercept	1.979 (0.000) ***	1.614 (0.000) ***	1.993 (0.000) ***	4.629 (0.000) ***	1.773 (0.000) ***	1.230 (0.000) ***	2.168 (0.000) ***	1.752 (0.000) ***
Level-1 CV								
Gender	0.642 (0.001) ***	-0.247 (0.165)	0.654 (0.001) ***	-0.216 (0.206)	0.731 (0.012) *	-0.353 (0.285)	0.698 (0.004) **	-0.143 (0.536)
Age	0.032 (0.595)	-0.212 (0.006) **	0.046 (0.449)	-0.198 (0.009) **	-0.058 (0.504)	-0.386 (0.001) ***	-0.030 (0.592)	-0.306 (0.000) ***
Education	-0.138 (0.147)	0.0215 (0.838)	-0.135 (0.166)	0.024 (0.829)	-0.211 (0.146)	-0.006 (0.974)	-0.185 (0.156)	-0.040 (0.794)
Income	-0.090 (0.389)	-0.086 (0.425)	-0.069 (0.501)	-0.065 (0.545)	-0.111 (0.534)	-0.040 (0.803)	-0.158 (0.277)	-0.156 (0.330)
Level-2 CV								
Ln GDP			-0.101 (0.073) +	-0.086 (0.170)	-0.138 (0.327)	-0.018 (0.896)	-0.149 (0.042) *	-0.162 (0.0072) **
Level-2 IV								
1. H1a -Governance			-0.421 (0.006) **	-0.298 (0.057) +				
2. H1b -VC					-0.002 (0.010) **	-0.002 (0.008) **		
3. H1b -Financial Environment							-0.561 (0.029) *	-0.599 (0.031) *

a Model 0: 38 countries

b Model 1: 38 countries

c Model 2: 20 countries

d Model 3: 27 countries

+ p < .10

* p < .05

** p < .01

*** p < .001

Two-tailed tests.

Table 5 Hierarchical Linear Modeling Results for Cognitive institutions

	Model 0 ^a		Model 1 ^b	
	C1	C2	C1	C2
Intercept	1.967 (0.000) ***	1.598 (0.000) ***	1.994 (0.000) ***	1.643 (0.000) ***
Gender	0.650 (0.001) ***	-0.206 (0.232)	0.650 (0.001) ***	-0.256 (0.148)
Age	0.049 (0.42)	-0.195 (0.011) *	0.040 (0.506)	-0.214 (0.005) **
Edu	-0.133 (0.143)	0.036 (0.732)	-0.135 (0.163)	0.016 (0.886)
Income	-0.098 (0.324)	-0.094 (0.367)	-0.075 (0.470)	-0.073 (0.520)
Ln GDP	-0.064 (0.319)	-0.014 (0.884)	-0.134 (0.036)	-0.095 (0.128)
4. H2a -TEA	0.074 (0.001) ***	0.083 (0.000) ***		
5. H2b-INV			-0.008 (0.609)	-0.030 (0.116)
6. H2c -Opportunity				

a Model 0: 38 countries

b Model 1: 38 countries

+ p < .10

* p < .05

** p < .01

*** p < .001

Two-tailed tests.

Table 6 Hierarchical Linear Modeling Results for Normative institutions

	Model 0 ^a		Model 1 ^b		Model 2 ^c	
	C1	C2	C1	C2	C1	C2
Intercept	1.954 (0.000) ***	1.617 (0.000) ***	1.991 (0.000) ***	1.614 (0.000) ***	1.980 (0.000) ***	1.609 (0.000) ***
Level-1 CV						
Gender	0.666 (0.000) ***	-0.227 (0.188)	0.673 (0.001) ***	-0.206 (0.247)	0.655 (0.001) ***	-0.221 (0.206)
Age	0.046 (0.469)	-0.202 (0.008) **	0.041 (0.505)	-0.206 (0.008) **	0.042 (0.489)	-0.206 (0.007) **
Edu	-0.120 (0.208)	0.048 (0.648)	-0.151 (0.116)	0.002 (0.986)	-0.136 (0.152)	0.022 (0.838)
Income	-0.082 (0.432)	-0.094 (0.386)	-0.101 (0.321)	-0.923 (0.403)	-0.094 (0.356)	-0.087 (0.425)
Level-2 CV						
Ln GDP	-0.035 (0.581)	-0.086 (0.220)	-0.135 (0.023) *	-0.073 (0.162)	-0.124 (0.044) *	-0.083 (0.198)
Level-2 IV						
7. H3a -Innovation	-0.313 (0.008) **	-0.151 (0.199)				
8. H3b -HEA			0.066 (0.439)	0.231 (0.035) *		
9. H3b -GDP Growth					0.042 (0.203)	0.058 (0.137)

a Model 0: 37 countries

b Model 1: 38 countries

c Model 2: 38 countries

+ p < .10

* p < .05

** p < .01

*** p < .001

Two-tailed tests.

Table 7 Hierarchical Linear Modeling Results for Family system

			Model 0 ^a		Model 1 ^b		Model 2 ^c	
	C1	C2	C1	C2	C1	C2	C1	C2
Intercept	-1.978 (0.000) ***	-0.365 (0.000) ***	-2.031 (0.000) ***	-0.338 (0.000) ***	-2.140 (0.000) ***	-0.279 (0.002) **	-1.972 (0.000) ***	-0.355 (0.000) ***
Level-1 CV								
Gender	-0.643 (0.001) ***	-0.889 (0.000) ***	-0.524 (0.010) **	-0.756 (0.000) ***	-0.797 (0.001) ***	-0.881 (0.000) ***	-0.628 (0.001) ***	-0.866 (0.000) ***
Age	-0.032 (0.597)	-0.244 (0.000) ***	-0.016 (0.822)	-0.261 (0.000) ***	0.044 (0.427)	-0.234 (0.000) ***	-0.039 (0.515)	-0.241 (0.000) ***
Edu	0.137 (0.148)	0.159 (0.002) **	0.224 (0.108)	0.151 (0.022) *	0.193 (0.099) +	0.243 (0.000) ***	0.149 (0.139)	0.162 (0.004) **
Income	0.091 (0.387)	0.004 (0.930)	-0.007 (0.961)	0.033 (0.613)	0.191 (0.218)	-0.052 (0.448)	0.059 (0.563)	-0.002 (0.972)
Level-2 CV								
Ln GDP			0.212 (0.002) **	0.058 (0.237)	0.272 (0.002) **	-0.015 (0.717)	0.068 (0.231)	-0.021 (0.624)
Level-2 IV								
10. H4a -Family Strength			1.693 (0.010) **	0.071 (0.763)				
11. H4b -Family Importance					0.030 (0.097) +	-0.012 (0.006) **		
12. H4c - Personal Wealth							0.001 (0.002) **	0.001 (0.018) *

a Model 0: 29 countries

b Model 1: 23 countries

c Model 2: 38 countries

+ p < .10

* p < .05

** p < .01

*** p < .001

Two-tailed tests.

Figure 1: Informal Investment on Family and Friends across Countries

