

MINORITY BUSINESS NETWORKS AS SOURCES OF SOCIAL CAPITAL FOR MINORITY FIRMS

IAN Y. BLOUNT

*The Ohio State University
The John Glenn School of Public Affairs
1810 College Road, Columbus, Ohio 43210
Blount.4@osu.edu*

DELMONIZE A. SMITH

*Rochester Institute of Technology
Saunders College of Business, 105 Lomb Memorial Drive
Rochester, New York 14623*

JAMES A. HILL

*The Ohio State University
The Max Fisher School of Business
2100 Neil Avenue, Columbus, Ohio 43210*

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Much of our understanding concerning minority-owned firms is based on nascent entrepreneurial businesses. Therefore, it is difficult to answer the question of how a minority-owned firm's age and size may influence the social capital derived from a minority business network. We utilize a resource-dependence perspective to hypothesize that the social capital derived from participation in a minority business network will be negatively related to the minority-owned firm's age and size. We find that firm size (as measured by revenue and number of employees) is negatively related with social capital derived from the minority business network. Our findings may help minority business owners understand the relative value of membership in minority business networks before committing limited resources.

Keywords: Social capital; networks; resource dependence; minority business.

1. Introduction

The Small Business Administration (SBA) defines a minority business as one owned by individuals who have been subjected to racial or ethnic prejudice or cultural bias because of their identity as members of a group. Included in these criteria are businesses owned by African Americans, Hispanics, Native Americans and Asians. According to the most

recent data from the [U.S. Census Bureau \(2010\)](#), the number of minority-owned businesses grew 45.6 percent between 2002 and 2007, compared to a growth rate of 13.6 percent by White-owned businesses. Demographic projections for the United States imply similar increases in minority-owned firms are likely to continue as the overall percentage of minorities increases.

Along with the substantial increase in minority-owned firms comes a corresponding increase in the number and prominence of minority business networks purporting to be a source of social capital for their members. Minority business networks claim to afford their minority business members the opportunity to expand their social and business networks by interacting with other minority firms as well as key decision makers from various corporations that may use their product and/or service. Research associated with social capital development suggests minority business owners may be more likely to draw upon these social and professional-oriented networks because they have the opportunity to interact with other minorities ([Mehra et al., 1998](#)). Social capital developed through networks based on minority and ethnic subgroup linkages often act as sources of trust and support ([Putnam, 2000](#)). In addition, minority business owners, on average, have been found to possess lower levels of education, less prior experience in business and lower levels of startup capital ([Fairlie and Robb, 2008](#)). In light of these findings, minority business networks may be of particular value by offsetting the effects of less education, experience and financial capital ([Coleman, 1988](#); [Loury, 1987](#)).

However, much of our understanding of minority firms is based on young, entrepreneurial firms. Therefore, it is difficult to answer the question of how a minority firm's age and size may influence the potential social capital derived from a minority business network. Specifically, we utilize a resource-dependence perspective to hypothesize that the social capital derived from participation in a minority business network will be negatively related to the minority firm's age and size. Our findings may help minority business owners understand the relative value of membership in minority business networks before committing limited resources. Our associated implications offer guidance to minority business networks who often employ a "one-size-fits all" value proposition to their minority business members.

We organize the paper as follows. First, we discuss the prevalence of minority business networks and their purported value. We then leverage existing research on social capital and resource dependence to develop our hypotheses. Next, we present our sample, methodology and analysis. Finally, we conclude with our findings, practical implications and potential limitations of our study.

2. Literature Review and Research Hypotheses

2.1. Social capital from minority business networks

Hundreds of minority business networks exist in the United States. Some operate as national networks, others are organized by state, and still others operate on a local or regional level. The largest minority business networks often have a national headquarters and reach minority businesses across the country through an extensive network of regional

affiliate offices. Some minority business networks are inclusive of all minority members (e.g., *National Minority Supplier Development Council*), while others focus on a particular minority group (e.g., *Native American Chamber of Commerce*). Most of these networks operate as nonprofit organizations and accept membership from minority-owned businesses after they pay a membership fee. But why would a minority-owned business decide to be a member of a minority business network?

Networks that exist in many ethnic minority communities are often considered vital to the start-up of ethnic enterprises (Ward and Randall, 1988) and inter-firm relations (Werbner, 1984), and are seen as the basis of such firms' competitive advantage (Ward, 1991). More specifically, minority business networks are a potential source of social capital for minority-owned businesses. Social capital refers to the ability of actors to extract benefits from social structures, networks and memberships (Portes, 1998). The social capital derived from minority business networks can provide the minority firm with access to useful, reliable and exclusive information, which, in turn, improves a firm's likelihood of success (Brüderl and Preisendörfer, 1998). Establishing meaningful relationships through such networks has also been found to improve firm performance by increasing social capital that can result in securing adequate financing, access to potential customers and specialized education (Aldrich and Zimmer, 1986; Shane and Cable, 2002). Such networks help form trust quickly in the beginning of a relationship, particularly when direct experience with the other party is limited. Reputation is an important strategic resource and helps distinguish minority firms from competitors (Flanagan and O'Shaughnessy, 2005). Lewicki and Brinsfield (2009) explain how organizations accumulate reputation through social capital-rich networks:

Networks contribute to social capital by offering access to other individuals who control valued resources and with whom one can exchange resources or contributions. Such networks help form trust quickly in the beginning of a relationship, particularly when direct experience with the other party is limited. Network members are often able to form perceptions of other members despite incomplete information based on reputation and other network information.

In an effort to confirm "social capital" as a value proposition minority business networks convey to their members, we reviewed websites of well-known minority business networks. For example, *MBEConnect* (2012) describes itself as "a business social network designed to generate meaningful connections between M/WBEs [minority/women business enterprises] and potential business partners, including other M/WBEs, corporations, organizations and government agencies." The *Minority Business Network* (2012) refers to itself as "a non-profit organization created to empower small-to-medium sized minority businesses through sharing knowledge, positive reinforcement, training and exposure." The *National Black Chamber of Commerce* (2012) purports "to economically empower and sustain African American communities through entrepreneurship and capitalistic activity within the United States and via interaction with the Black Diaspora." A primary goal of the *United States Hispanic Chamber of Commerce* (2012) is "increasing

business relationships and partnerships between the corporate sector and Hispanic-owned businesses.” One of the largest minority business networks in existence today, the *National Minority Supplier Development Council (NMSDC)* (2012), “affords its minority business members the opportunity to expand their social and business networks by interacting with other minority firms as well as purchasing managers from various corporations.” NMSDC accomplishes this by organizing formal and informal events that allow minority business members to meet corporate purchasing managers and financing agencies. A distinction of NMSDC is that their rigorous certification process is considered the gold standard for certifying minority-owned businesses and as such, is used by virtually all corporations to verify firms’ minority-owned status.

2.2. Evolving resource dependence

Minority-owned business success may be predicated, in part, on the owner’s or president’s ability to accumulate social capital, and in turn, assemble critical resources through the minority business network (Starr and MacMillan, 1990). However, a resource-dependence perspective would suggest the social capital derived from the minority business network may be a factor of the minority firm’s stage of growth. A resource-dependence perspective contends that most organizations do not control all the resources necessary for survival and depend on other organizations or stakeholders to provide them (Pfeffer and Salancik, 1978). The extent to which a firm is dependent upon external organizations and stakeholders hinges on the importance of a particular resource to the firm, the degree to which those who control the resource have monopoly over the resource and the discretion they have over its allocation. However, at any given organizational stage, certain external stakeholder groups, because of their potential to satisfy critical organizational needs, will be more important than others (Jawahar and McLaughlin, 2001). In some stages, certain needs are likely to be so critical that if they are not fulfilled, the firm is unlikely to survive. As a result, priorities of top management will vary with a firm’s stage (Smith *et al.*, 1985). For example, gaining customer acceptance and establishing customer contact may be among the most critical needs at the startup stage (Dodge and Robbins, 1992).

Less-established ventures require myriad resources, from information and capital to symbolic support such as endorsement, approval and legitimacy (Singh *et al.*, 1986). Many researchers have addressed the difficult task young firms face when attempting to garner new business and attribute this partially to a lack of legitimacy with potential customers (Cason *et al.*, 2008; Greve, 1995). Young minority firms lacking important relationships may face high mortality risks, a condition entrepreneurship research has long referred to as the “liability of newness” (Stinchcombe, 1965). This liability arises, in part, from the difficulty in gaining the trust and support of resource providers who perceive a risk stemming from the limited track record and lack of legitimacy of the young venture (Akerlof, 1970; Singh *et al.*, 1986). As Aldrich and Fiol (1994) noted, “Trust is a critical first-level determinant of the success of entrepreneurs because, by definition, there is an absence of information and evidence regarding their new activity.” Consequently, success in both overcoming this liability and obtaining necessary resources may depend heavily on

the minority business owner's ability to create sustained exchange relationships with resource providers (Katz and Gartner, 1988). Therefore, minority business networks may become a legitimizing agent, particularly for early stage minority firms that are small and not well established (Stuart *et al.*, 1999).

As entrepreneurs grow their ventures over time, they should rely less on trust rooted in social-relations and begin relying more on institutional trust based on a history of competent interactions (Smith and Lohrke, 2008). The focus on larger and more established minority businesses will likely shift from overcoming liability of newness and survivability to such challenges as market segmentation, product differentiation and competition (Hofer, 1975). As the minority firm grows, the linkages between the owner and the set of essential firm relationships are less likely to be solely interpersonal commitments, and the exchange processes are no longer necessarily attached to particular individuals, but rather based on repeated exchange cycles between organizations (Katz and Gartner, 1988). Thus, at this stage, the minority business owner or president may reallocate time from external activities such as networking, to more internal activities such as supply chain optimization, total quality management and operations (McCarthy *et al.*, 1990). Empirical support for this transition is provided by research examining the evolution of young firm networks, research that found supplier contacts shifted from a social to business basis over time (Schutjens and Stam, 2003). Additional support is provided by research positing that the proportion of socially based ties within the firm's network will decrease as the firm moves from emergence to early growth (Hite and Hesterly, 2001). This evolution occurs because of the increased number of weak ties that are more market-like or arms-length than socially embedded (Granovetter, 1973).

2.3. Hypotheses

Therefore, we hypothesize that larger, more established minority firms will derive less social capital from minority business networks.

Hypothesis 1: Age of the minority-owned firm will be negatively related to the social capital derived from the minority business network.

Hypothesis 2A: Size of the minority-owned firm, as measured by revenue level, will be negatively related to the social capital derived from the minority business network.

Hypothesis 2B: Size of the minority-owned firm, as measured by number of employees, will be negatively related to the social capital derived from the minority business network.

3. Methods

3.1. Sample and data collection

Our sample consists of minority business owners and/or presidents who belong to a well-established minority business network. The minority business network, headquartered in New York City, is an organization comprised of 38 affiliate regional councils across the

country. Nationally, the network has over 3,500 corporate members and more than 15,000 certified minority business enterprises. The goal of the network is to provide a direct link between its corporate members and minority-owned businesses. Specifically, our data come from minority businesses that belong to their affiliate regional council servicing Central and Southern Ohio. The regional council has offices in Cincinnati, Columbus and Dayton, with approximately 433 certified minority-owned businesses. The following statements were provided on the minority business network's website describing the organization's purpose:

“We grow and foster relationships between minority business enterprises, corporations, and government entities. We grow value-driven partnerships between our certified MBEs and Corporate Members. Our most important function is to connect corporate purchasing and procurement departments with minority business enterprises. Results driven and strategic in our efforts, we bring unparalleled value to our membership base.”

In coordination with the president of the minority business network, we drafted an introductory notification that went out to all members to notify them of the forthcoming survey. Three days later, the first email with the hyperlink to the survey was sent out with a message from the president of the minority business network encouraging its members to participate. Utilizing suggestions by Dillman (2000) to increase response rates, we also sent two subsequent email requests two weeks apart. We received 132 usable responses, resulting in a 30 percent response rate. We compared early respondents (respondents within the first two weeks) and late respondents (responses received within the fourth week or later) in terms of the mean responses on each variable using a *t*-test (Lambert and Harrington, 1990). The results revealed no significant differences between the early and late respondents.

The majority of the participants were male (70%). The largest ethnicity group was African American (65%), followed by Hispanic (14%), Asian (14%) and Native American (4%). More than half the companies (62%) had been in business more than seven years and approximately half of the companies had 1–10 employees (53%). The mean number of years as a member of the minority business network was 6.3 with a standard deviation of 5.4. The three largest represented industries were professional services (31%), manufacturing/wholesale trade (30%) and construction-related (16%).

3.2. Measures

3.2.1. Dependent variable

Social capital was a scale derived from the value often purported to come from social networks. The items were related to credibility (Stuart *et al.*, 1999), visibility (Rao, 1994), access (Brüderl and Preisendörfer, 1998) and information (Inkpen and Tsang, 2005).

- “There is a perceived endorsement of credibility by having [network] affiliation”
- “Certification through [network] has increased the visibility of my organization”

Table 1. Factor analysis of social capital construct.

	Factor Score (Maximum Likelihood Estimation)	Corrected Item-Total Correlations	Alpha if Item Deleted
There is a perceived endorsement of credibility by having [network] affiliation.	0.72	0.65	0.79
Certification through [network] has increased the visibility of my organization.	0.81	0.75	0.74
Participation in [network] provides access to purchasing or decision-making personnel.	0.87	0.54	0.84
Having information through networking activities provided by [network] has a high degree of influence on my business.	0.85	0.70	0.76

Reliability Construct Cronbach's Alpha = 0.83.

- “Participation in [network] provides access to purchasing or decision-making personnel”
- “Having information through networking activities provided by [network] has a high degree of influence on my business”

Social capital was measured using four questions; therefore, we created a single summated scale for this construct and conducted an empirical assessment of the adequacy of this scale by means of factor analysis. Results of this analysis, using maximum likelihood estimation, are provided in Table 1. Diagnostic tests reveal that factor analysis is appropriate for these data. Factor loadings for each item exceed the recommended value of 0.50 for practical significance. Corrected item-total correlations exceed 0.30 and Cronbach's alpha for the construct is 0.83, thus ensuring reliability of the scale. A Hotelling's T-square test of the null hypothesis that all items on the scale have the same mean was significant.

3.2.2. Independent variables

Three independent variables were introduced in the analysis. Years in business was measured as a self-reported scale (1 = 1–3 years; 2 = 3–7 years; 3 = 7+ years), revenue level for the previous year was a self-reported scale (1 = \$10K–\$100K; 2 = \$101K–\$250K; 3 = \$501K–\$1M; 4 = \$1M–\$2.5M; 5 = \$2.5M–\$5M; 6 = greater than \$5M), and number of employees was a self-reported scale (1 = 1–10 employees; 2 = 11–20 employees; 3 = 21–50 employees; 4 = 51–100 employees; 5 = greater than 100 employees).

3.2.3. Control variables

To provide more accurate estimates of our hypothesized variables, we controlled for length of membership in the minority business network, industry type and ethnicity. Length of membership was assessed in years as a self-reported scale. Industry was assessed by categorizing the self-reported industry classification (*Construction-Related; Manufacturing/Retail; Professional Services; Information Technology; Transportation; Administrative/Support; Accommodations/Food Services*). Ethnicity was a self-reported, categorical assessment (*African American; Hispanic; Native American; Asian; White*).

4. Results

Table 2 presents means, standard deviations, correlations, and coefficients for the control, independent, and dependent variables. We find that social capital is significant and negatively related to number of employees and revenue level.

To test our hypotheses, we used hierarchical regression analysis. Table 3 shows the regression results of the control variables entered in step 1, followed by the dependent variable in step 2.

Table 2. Descriptive statistics, correlations, and reliability coefficients.

Variables	Mean	s.d.	1	2	3	4	5	6	7
1. Membership	6.29	5.37							
2. Industry	2.64	1.31	-0.05						
3. Ethnicity	1.71	1.16	-0.09	0.12					
4. Years in business (H1)	2.51	0.70	0.49**	0.04	0.14				
5. Number of employees (H2A)	1.98	1.31	0.15	0.05	0.02	0.32**			
6. Revenue level (H2B)	4.27	2.12	0.25**	0.01	0.07	0.35**	0.66**		
7. Social capital	2.28	0.78	-0.03	0.18*	0.18*	-0.04	-0.20*	-0.20*	(0.83)

* $p < 0.05$. ** $p < 0.01$. two-tailed test.

Table 3. Results of regression analyses for social capital.

	β	$SE\beta$	R^2	ΔR^2
Step 1			0.04	
Membership	0.01	0.01		
Industry	0.10	0.06		
Ethnicity	0.13*	0.07		
Step 2			0.04	0.00
Membership	0.01	0.02		
Industry	0.10	0.06		
Ethnicity	0.14*	0.07		
Years in business (H1)	-0.10	0.12		
Step 1			0.05	
Membership	0.01	0.01		
Industry	0.11*	0.06		
Ethnicity	0.13*	0.07		
Step 2			0.09	0.04*
Membership	0.02	0.01		
Industry	0.12*	0.06		
Ethnicity	0.13*	0.07		
Revenue level (H2A)	-0.08*	0.03		
Step 1			0.06	
Membership	0.00	0.01		
Industry	0.11*	0.06		
Ethnicity	0.15*	0.07		
Step 2			0.09	0.04*
Membership	0.01	0.01		
Industry	0.12*	0.06		
Ethnicity	0.15*	0.06		
Number of employees (H2B)	-0.12*	0.06		

* $p < 0.05$. ** $p < 0.01$. two-tailed test.

Hypothesis 1 proposed that the age of the minority-owned firm will be negatively related to the social capital derived from the minority business network. The control variable of ethnicity is significant and positive ($\beta = 0.14, p < 0.05$). However, there is not a significant relationship between years in business and social capital. Therefore, hypothesis 1 is not supported.

Hypothesis 2A proposed that the size of the minority-owned firm, as measured by revenue level, will be negatively related to the social capital derived from the minority business network. The control variable of industry is significant and positive ($\beta = 0.11, p < 0.05$) as well as ethnicity ($\beta = 0.15, p < 0.05$). There is a significant and negative relationship between revenue level and social capital ($\beta = -0.08, p < 0.05$). Therefore, hypothesis 2A is supported.

Hypothesis 2B proposed that the size of the minority-owned firm, as measured by number of employees, will be negatively related to the social capital derived from the minority business network. The control variable of industry is significant and positive ($\beta = 0.12, p < 0.05$) as well as ethnicity ($\beta = 0.15, p < 0.05$). There is a significant and negative relationship between number of employees and social capital ($\beta = -0.12, p < 0.05$). Therefore, hypothesis 2B is supported.

5. Discussion and Conclusion

We utilized a resource-dependence perspective to hypothesize that the social capital provided to a minority firm by a minority business network will be negatively related to the minority firm's age and size. Support was found for the significance of minority firm size, using both revenue level and number of employees. Our findings clearly show that "size matters" when it comes to the value that minority firms perceive from being a member of a minority business network. As revenue and number of employees increase, minority firms derive less social capital from membership in minority business networks. We did not find support for the significance of age as a factor influencing social capital derived from the minority business network. One might conclude that the number of years in business is not significantly related to accumulation of, or access to, resources. For example, the owner of a minority firm may have been in business for several years but still operate as a "life-style business" with few to no employees. Support for this explanation is found in the fact that the mean number of paid employees for African American and Latino-owned firms is one (U.S. Department of Commerce, 2011). In such a case, the social capital derived from membership in a minority business network may not change because the resource requirements of the minority business will likely stay constant.

Our findings have potential implications for both minority business owners as well as minority business networks. Industry type was found to play a significant role in the amount of value derived from minority business networks. Specifically, administrative and service-based businesses derived the greatest social capital from their minority business networks, while other sectors such as construction and information technology reported significantly lower values. Our findings are in line with Davidsson and Honig (2003) who posited that business networks that focus on general concepts such as "business education"

and “financial analysis” become less valuable to firms over time. Moreover, they argued that as businesses mature, they derive more value and better performance when interacting with networks that provide very specific industry knowledge, as opposed to primarily focusing on the development of social capital. Based on these findings, it could be promulgated that minority-owned businesses operating in administrative and service-based industries may require less technical/area specific knowledge; therefore, they would continue to derive value from minority business networks. Alternatively, minority-owned businesses operating in certain industries, such as construction and technology, may be better served joining knowledge-specific networks.

Results from our research may be effective as a prognostic tool to help minority-owned businesses understand the relative return on committing their limited resources to networking activities. Minority business owners of larger firms may want to limit the time and monetary investments required for membership in the current set of minority business networks. At the very least, larger minority-owned businesses will want to ensure the investment and opportunity costs associated with minority business networks are commensurate with the value received from membership. The difficulty for many minority-owned entrepreneurial firms is discerning if allocating limited time and resources to membership in minority business networks provides value. [Wollebaek and Selle \(2003\)](#) found higher levels of participation in social networks by firms in nascent stages. Other research by [Kuntaric et al. \(2012\)](#) found that nascent firms will stretch themselves and in some cases sacrifice other managerial responsibilities to participate in social networking activities if they feel it will lead to long term results for their organization. Our findings suggest that minority-owned entrepreneurial firms, primarily characterized as having fewer employees and lower revenue, will derive social capital from membership in minority business networks. This value for minority-owned entrepreneurial businesses should persist until the firm grows in employees and revenue.

Significant practical implications for minority business networks are revealed from our findings. Minority business networks employing a “one size fits all” approach to their minority business members may want to consider the implementation of segmented programming. For example, such networks may begin with the “fundamentals of business” for minority-owned entrepreneurial members, but then tailor their programs and services to specific industry knowledge sessions to meet the needs of larger, minority-owned businesses in certain industry sectors. Having segmented programs related to industry type and minority business size would better enable minority business networks to offer their members value throughout the business maturation process. Acknowledgement of this potential size effect can be seen by recent actions of the National Minority Supplier Development Council to recognize a “Supplier of the Year” in four revenue classes, ranging from under \$1 million dollars to over \$50 million.

As with any study, there are potential limitations to our research. Information for our research was derived from cross-sectional data that lacked spatial, dynamic and temporal richness. As a result, we were unable to analyze how perceived social capital varied over the length of membership in the minority business network. This limitation also precluded us from evaluating the marginal or incremental perceived social capital value.

Future longitudinal research would offer greater insight as to how social capital, particularly as it relates to the opportunity cost of building such capital, changes over time. An additional limitation is that the majority of our participants were African American-owned firms. This is not surprising considering the minority business network where we obtained our sample has a greater proportion of African American-owned businesses, as is the case for most minority business networks not targeted toward a specific minority group (e.g., U.S. Hispanic Business Association). However, existing research suggests ethnic differences exist when examining minority-owned businesses (Fairlie and Robb, 2008). Our findings support this line of research. Specifically, African American businesses reported significantly lower levels of social capital from the minority business network as compared to other ethnic groups. Future research designed to capture a larger percentage of diverse ethnic groups across a multitude of minority business networks may help explain such differences in perceptions of social capital. Despite these limitations, we believe our research adds to our limited knowledge base of the resource dependencies, orientations and strategic choices of larger and more established minority-owned businesses. We encourage greater research in this area, particularly as the number of minority-owned firms continues to outpace the number of White-owned businesses in the United States.

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