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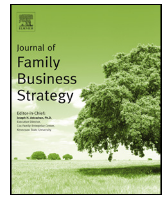

Family involvement and firm performance: Evidence from UK listed firms

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ABSTRACT

This study examines how family involvement affects the performance of UK companies listed on the London Stock Exchange (LSE). Using a panel dataset from 1998 to 2008, the econometric models evaluate the effect of family involvement in terms of ownership and management on firm performance (measured with accounting ratios and Tobin's *Q*) while controlling for a number of conditions external to the firm as well as business characteristics. Our findings illustrate a non-linear relationship between family ownership and firm performance, with performance increasing until family shareholding reaches thirty-one percent, at which point performance begins to decrease. Moreover, the findings illustrate that the higher the involvement of the family in terms of management (i.e., through a family CEO) and governance (board representation and/or CEO-Chairman dual role), the higher the performance the firm appears to sustain over the long run and across generations.

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Introduction

A plethora of studies have provided evidence that family ownership is a relatively common phenomenon in publicly listed firms across market economies worldwide (La Porta, Lopez-de-Silanes, & Shleifer, 1999). For instance, in the U.S., one-third of the 500 largest corporations have been classified as family-owned (Anderson & Reeb, 2003; Villalonga & Amit, 2006; among others), while in Western Europe, family firms represent approximately 44% of listed firms (Faccio & Lang, 2002). Given the dominance of the family firm model, research in the field of governance has increasingly embarked on exploring the influence of family on the performance of a listed firm (e.g., Anderson & Reeb, 2003; Andres, 2008; Barontini & Caprio, 2006; Block, Jaskiewicz, & Miller, 2011; Sraer & Thesmar, 2007; Villalonga & Amit, 2006).

Studies conducted to date reveal inconclusive evidence regarding the influence of family involvement on the performance of listed firms. Some studies show that family involvement in ownership creates value (Anderson & Reeb, 2003; Kowalewski, Talavera, & Stetsyuk, 2010; Maury, 2006; Pindado, Requejo, & Torre, 2008; San Martin-Reyna & Duran-Encalada, 2012), while others claim that listed family firms do not outperform their non-family counterparts (Filatotchev, Lien, & Piesse, 2005; McConaughy & Phillips, 1999; Miller, Le Breton-Miller, Lester, & Cannella, 2007). The same dichotomy is evident with regard to the relationship between family involvement in management and performance (Anderson & Reeb, 2003; Andres, 2008; Giovannini, 2010; Villalonga & Amit, 2006) and family involvement in governance (e.g., through board representation or a board chair role) and performance (Filatotchev et al., 2005; García-Ramos & García-Olalla, 2011; Giovannini, 2010; Villalonga & Amit, 2006), where both positive and negative relationships are established. These contradictory results are apparent due to a number of interplaying factors including the diverse definitions of a "family firm," sampling techniques, variables, methodologies, study periods, and institutional settings that different scholars consider (Sacristán-Navarro, Gómez-Ansón, & Cabeza-García, 2011).

Our study contributes to the field of family ownership and performance by addressing several factors associated with family influence on firm performance that are not addressed adequately in previous work. These include the dimensions of family ownership, family management, and family governance as well as the separate effect of founders versus descendants on firm performance. We also establish the need to appreciate firm age and

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nonlinearities in the relationship between family ownership and firm performance (Anderson & Reeb, 2003). This study may contribute to an appreciation of a complex set of dynamics of family influence and strengthen our understanding of the family effect on firm performance.

Furthermore, our work draws data from the UK context, where the relationship between family influence and listed firm performance is still relatively under-explored. The UK exhibits an idiosyncratic institutional and regulatory business environment characterized by high shareholder protection (Dahya, Dimitrov, & McConnell, 2009; Franks, Mayer, & Rossi, 2005) and efficient monitoring (Franks et al., 2005). Another key contribution of this work is that it offers fresh evidence on the relationship between family involvement and firm performance from a different stock market context. The UK listed market can offer further insights on what has been reported to date on the effect of family involvement on firm performance. It could also help explore the similarities and differences between this context and other areas in which this relationship has been explored.

An econometric investigation that aims to offer a rigorous examination of the separate effect of family ownership and management on firm performance is undertaken.[2] We focus exclusively on the UK listed sector using financial, board, and ownership data of FTSE constituent firms from 1998 to 2008 in order to examine the impact of the family effect in terms of ownership and management involvement on business performance.

The rest of the article is organized as follows: "Theoretical framework and hypotheses" offers a review of the theories and outlines the development of our hypotheses. "Data" describes the UK database and offers summary statistics. "Empirical findings" discusses our empirical methodology and reports our results, examining the relationships between family ownership and involvement and firm performance. "Discussion and conclusions" offers a discussion of the present results, concluding remarks and implications.

Theoretical framework and hypotheses

Agency and stewardship theories

The theoretical base of the majority of investigations seeking to examine the effect of family on firm performance has been agency theory (Block et al., 2011; Dyer, 2006; García-Ramos & García-Olalla, 2011; Miller et al., 2007; Sacristán-Navarro et al., 2011; Sciascia & Mazzola, 2008), with an increasing number of studies also drawing upon stewardship theory (Miller & Le Breton-Miller, 2006; Uhlaner, Floren, & Geerlings, 2007).

Jensen and Meckling (1976) introduced the agency theorem to expound that the separation of ownership and management creates conflicting goals between principals (i.e., shareholders) and agents (i.e., managers). This divergence could arise from their variant utility functions (profits versus private gains) and information asymmetries about their views on growth, variant investment horizons, and different attitudes to risk diversification and external growth strategies (e.g., takeovers), inter alia. Stewardship theory, in turn, advocates that managers do not always seek to accomplish their own individual goals but rather act as stewards of the business (Davis, Schoorman, & Donaldson, 1997). This theory has been found very relevant within the family firm context, where owners are often managers of the same firm and may assume a stewardship role (Corbetta & Salvato, 2004). In this sense, family owner-managers can often become highly altruistic and forgo personal interests for business goals (Corbetta & Salvato, 2004; Eddleston & Kellermanns, 2007). In this sense, a collectivistic culture may be established in the business, which nurtures a pro-organizational behavior and willingness among family members to join efforts toward further business growth, profitability, and innovation. Stewardship is considered to be a distinctive feature of family firms. Because family members that own a business are also involved in its management, goal alignment is likely to occur between business owners and managers (Miller & Le Breton-Miller, 2006; Pieper, Klein, & Jaskiewicz, 2008), which suppresses agency costs (Corbetta & Salvato, 2004; Miller & Le Breton-Miller, 2006). Although not all family firms may exhibit a stewardship orientation, when family members see themselves as stewards of their family's business, then benefits can be expected for the business (Corbetta & Salvato, 2004; Eddleston & Kellermanns, 2007; Miller & Le Breton-Miller, 2006).

The present article advocates that a real understanding of family influence over firm performance needs to expound the principles and dynamics associated with agency and stewardship theories. In this section, the major empirical studies and theories are reviewed in order to guide the synthesis of the key hypotheses examined by this investigation.

Family involvement in ownership and firm performance

This study draws upon principles of agency theory (Anderson & Reeb, 2003; Dyer, 2006; Miller et al., 2007; Villalonga & Amit, 2006) and stewardship perspectives (Corbetta & Salvato, 2004; Miller & Le Breton-Miller, 2006; Uhlaner et al., 2007), which set the prospects of explaining the influence of family ownership on the performance of the family firm.

Studies drawing upon agency theory reveal mixed evidence regarding the role of family ownership. Certain agency theorists believe that family ownership maximizes agency problems and erodes firm performance (Barclay & Holderness, 1989; DeAngelo & DeAngelo, 2000; Gomez-Mejia, Nunez-Nickel, & Gutierrez, 2001; Morck, Percy, Tian, & Yeung, 2005; Schulze et al., 2003). Empirical evidence expounds the failure of family capitalism as a result of family oligarchic control (Morck et al., 2005) and altruistic nepotism (Schulze et al., 2003) that can lead to agency problems that erode performance. Family owners that build control mechanisms to exploit ownership rights in order to control management and substitute professionalism with nepotism and tolerate incompetence, entrenchment (Barclay & Holderness, 1989; Gomez-Mejia et al., 2001), and the expropriation of private benefits (DeAngelo & DeAngelo, 2000) end up disenchanting both 'insider' and 'outsider' shareholders, which triggers feuding (Barclay & Holderness, 1989). On the other hand, a number of agency theory-driven studies argue that concentrated family ownership in the hands of founding family owner-managers can, in fact, help minimize agency problems (both principal-agency type I and type II agency costs when there is a dominant family versus other owners) (Villalonga & Amit, 2006) and thus enhance performance and build shareholder value (Anderson & Reeb, 2003; Maury, 2006; San Martin-Reyna & Duran-Encalada, 2012).

This investigation has an explicit focus on the financial performance of listed family firms. Previous evidence illustrates that within economies in which stakeholder protection is sufficient, family ownership is likely to have a positive influence on firm performance. This is because conflicts of interest between minority shareholders and controlling families are reduced, and agency problems are minimized (Anderson & Reeb, 2003; Sacristán-Navarro et al., 2011). The present article draws data

[2] More recent studies have examined various aspects of family-controlled firms (see for instance the work of Croci et al. (2011), Masulis, Pham, and Zein (2011), and Brav (2009), among others.

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