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Do Family Firms Behave as Long-Termist? The Role of Performance Feedback

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Abstract: Long-term orientation is often regarded as the rational why family firms could gain superior performance. However, there is very little empirical evidence. This article examined whether and when Chinese family firms were more long-term oriented than non-family firms, combining socioemotional wealth theory and performance feedback perspectives. Analysis on the samples from Chinese Private Enterprise Survey provided support for family firms' long-term orientation and when the more performance exceeded from historical aspiration, the better family firms performed in the long-term investments than non-family firms. While social performance aspiration has no significant moderating effect, indicating self historical aspiration is a key reference point in family firm decision making.
Keywords: family business, long-term orientation, performance feedback, socioemotional wealth.

INTRODUCTION

Berle and Means [2] proposed that dispersed ownership would become the dominant form of modern corporate structure in the future. However, as La Porta [1] and Claessens [3] have noticed that no matter in developed or developing countries, family-owned or family-controlled firms are still very common for business organizations. Developed economies, such as Germany and Italy have wider family coverage than US. While in emerging economies, such as China, family firms are rather popular, reaching up to more than 80% of the private enterprises. For a long time, people have been discussing family firm's pros and cons, without agreement on the conclusion. Numbers of studies have tested the performance differences between family businesses and non-family businesses, using samples from different countries, different scales, and even different definitions of family firms. Although there is no unanimous conclusion, strong long-term orientation is always regarded as the unique advantages of family businesses [4]. Anderson [5] believes that the reason why United States firms are falling behind German and Japanese companies largely lies in that US managers behave short-termism. With too much concern about the short-term profits rather than future investments on long-term development.

We should learn the US story. Especially in the context of China's transitional economy, the wealth accumulated by hard working is much smaller than the return on capital operation and financial investment. So, more and more industrialist began switching to be investors. The launch of the GEM(Growth Enterprise Market Board, *Chuangyeban in Chinese*) makes multiple entrepreneurial families short-termism, caring too much about short-term gains and ignoring long-term investments. In the modern era, short-termism seems to become the dominant value for Chinese entrepreneurs. Do family firms still have foresight? Under the conditions of rapid changes, can family firms achieve the dream of family business continuity? Specifically, we investigate the questions: Firstly, Whether the family-controlled businesses have stronger long-term orientation? Although many studies have pointed out that the strong long-term orientation is an important explanation for family firm high performance [6], however, empirical, especially large-scale quantitative data is very rare. Secondly, how does the performance feedback shape firm's long-term investment decisions? Performance provides the decision situations for firm strategic change. When firms get positive and negative performance feedback, they behave differently. Based on the Socioemotional Wealth (SEW) and performance feedback theory, we use the Chinese Private Enterprise Survey in 2010 to examine the long-term oriented behaviors between family and non-family firms, analyze the performance feedback situations and draw some implications for family business practice and temporal research in the future direction.

LITERATURE REVIEW AND RESEARCH HYPOTHESES

Family business literature argues that family businesses are more long-term oriented than non-family firms [7,8], and perform better in profitability [9], efficiency [10] and sales growth [11]. Long-term orientation is also considered as an important source of family business uniqueness and competitive advantage

[12].

Time is a key reference element in firm strategic decision-making. The long-term orientation question relates more with firm inter-temporal decision. Short-termism is often regarded as more related to tangible and intangible assets, and the preference for short-term performance may cause long-term damage to firm value [13]. Some scholars emphasized the importance of long-term value. However, certain level short-term performance is often the prerequisite to survive [14]. For the family business, the balance between short-term and long-term is an eternal topic.

According to the SEW theory proposed by Gomez et al. [7], family firms strive to pursue the best protection of their SEW. Compared to non-family firms, what family firms care more are not financial wealth but the SEW. In studies, Anderson and Reeb [4] pointed out that family shareholders have a longer investment horizon in relation to the other shareholders and may be willing to invest more in long-term projects. Based on this, compared to other types of shareholders, family shareholders have more patient capital, and more willing to consider some investment decisions of non-short-term results. Extant stewardship research also indicates that family owners are more likely to act as stewards rather than agents [15,16]. In management, family business executives also tend to have a longer tenure [17], which weaken the short-term performance assessment stress. Additionally, Block [18] found that only when the family members serve as chairman or CEO, will the family business invest more long-term projects than non-family businesses. Based on the SEW theory and extant evidence, family firms are more likely to put efforts on the long-term investments to pursue the long-term benefits, such as family continuation, family dynasty and family reputation. Besides, the SEW of family firms are not formed by one night, but an accumulation process. Thus, family firms would perform more decisions supporting long-term development. Therefore, we propose that:

Hypothesis 1:

Family firms perform more long-term oriented investments than non-family firms.

Performance feedback studies propose that when firm performance lower than aspiration level, firms would like to perform strategic changes to eliminate performance aspiration gap, while performance higher than aspiration level, firms would behave more conservatively [19]. Based on SEW theory, when family firms come into the condition with performance lower than aspiration level, family firms would be threatened of losing family control, which is detrimental to family business SEW. For family firms, no SEW or non-economic benefits exist once family firms disappear.

In general, when performance is higher than firm aspirations, firms would prefer to reduce the entrepreneurial investments to cope with uncertainty. While in non-family firms, better performance than aspiration may be more likely seen as the achievement sourcing from professional CEOs and they would largely reduce the risky investments in long-term developments to preserve the good image in the market. As for family firms, they will also cut down entrepreneurial investments, such as in research and development for keeping solidity and expecting for growth in the long-term run. But family firms do not bear so much stress as non-family firms, and they may reduce less investments than non-family firms.

When performance is lower than aspirations, firms would search solutions to fill the performance gap. In SEW perspective, when face with challenges on firm control and survival, family firms would care more about firm survival and emphasize both the family and non-family objectives. Compared to non-family firms, family firms would make trad-off between family and non-family goals and invest more on entrerpreneurial activities. Thus, we hypothesize that:

Hypothesis 2:

Performance feedback moderates the long-term orientation difference between family and non-family business. Specifically, when firm performance aspiration gap is higher, the difference between family and non-family firms investments on long-term orientation is larger.

METHODOLOGY

Data collection

The raw data of this article comes from the 9th National Private Enterprise Survey database that Chinese private enterprise research team conducted in 2010. The respondents of this survey are private entrepreneurs from all over the country. This survey aims to gain further understanding of the situations of private enterprises. Totally 4614 companies participated in the survey, distributing over country-wide provinces and regions and diverse industries. According to Chinese Private Enterprise Development Report, by the end of 2009, the registration of the private sector reached 7,401,500, and it accounted for 70% of the total registered enterprises in China. Among the private sector, the case of family firm is much common. In different aspects of business ownership, board of directors or management positions, families have varying approaches to control. Although research team takes strict control of the process of the investigation and seeks to improve data integrity and authenticity,

still some data are missing as it has a high sensitivity of information relates to corporate ownership structure and real performance. To ensure the accuracy of the analysis, this article excluded part of the sample that has too much missing values. Finally, 2275 firms eventually are included in the subsequent analysis.

Measurement

Dependent Variables

Long-term orientation. Based on the recommendations from Block [18], we measure firm long-term oriented investments from the R&D investment and employee training. Two variables are represented in the form of the proportion of sales revenue and computed into one (LTO) by principal component analysis. Specific operational indicators are illustrated in the Table 1.

Independent variables

Family Firm. Chrisman, Chua, Pearson, & Barnett [20] calls for an essence based approach to define family business. Family ownership and family's intention for the trans-generational sustainability of control have been used to define family firm and potential proxy for socioemotional wealth for the family [7,20]. In this study, we define the family firms as those that the entrepreneur and his/her family own at least 50% ownership of the firm and have the trans-generational intention to pass the firm. The survey provides relevant information for us to identify family firms. There are three questions on this: (1) What's your equity ownership of the firm? (2) What's your family member's equity ownership of the firm? (3) How do you think about the succession issue of the firm? The first two are for ownership standard and the third question is about trans-generational succession intention. According to our classification, family business captures 21.3% of the whole dataset and is codified as a dummy variable (FAMILY, 1 stands for family firm).

Table-1: Variable definitions

Concepts	Variables	Definitions
Long-term orientation	LTO	Principle component for ratio of firm investment in R&D and employee training on sales.
Family business	FAMILY	Dummy variable, 1 for family firm and 0 for non-family firm
Performance aspiration gap	PSGH	Positve Historical Performance Aspiration Gap, computed as the ROS difference between year 2008 and 2007. If the difference is negative, PSGH is coded as 0.
	NGGH	Negative Historical Performance Aspiration Gap, computed as the absolute value of the ROS difference between year 2008 and 2007. If the difference is positive, NGGH is coded as 0.
	PSGS	Positve Social Performance Aspiration Gap, computed as ROS difference between year 2008 and the industry mean in year 2007. If the difference is negative, PSGS is coded as 0.
	NGGS	Negative Social Performance Aspiration Gap, computed as the absolute value of the ROS difference between year 2008 year 2008 and the industry mean in year 2007. If the difference is positive, NGGS is coded as 0.
Firm age	FIRMAGE	The difference between the year 2010 and the founding year.
Firm size	LNEMP	The nature log of firm employee numbers.
Industry	IND	Industry dummied into 19 binary variables, according to National Statistics Classification.
Market development	MARINDEX	Market development index, from Fan and Wang(2013).
Leverage	LEVERAGE	Firm debt/assets
Prior Performance	ROS8	Profit/Sales in 2008
Entrepreneur age	AGE	The difference between the year 2010 and the entrepreneurs' born year.
Entrepreneur gender	GENDER	A binary variable, 1 indicates male.
Entrepreneur human capital	EDU	Entrepreneur's education level, 1= primary school, 2=junior middle school, 3= senior middle school, 4=junior college, 5=undergraduate, 6= master.

Moderators

Performance aspiration gap. We constructed performance aspiration gap in historical and social dimensions, according to the different referents in comparison and consistent with Chirisman and Patel [21], Tyler and Caner [22]. The historical performance aspiration gap is measured by performance (Return on Sales, ROS in this study) difference between the prior two years (year 2008 minus year 2007, in this study). Historical performance aspiration gap can be positive or negative and is divided into PSGH and NGGH two variables. In the same way, the social performance aspiration gap is measured by performance (Return on Sales, ROS in this study) difference between the firm performance in prior year and the industry peer performance in the year before prior year. Social performance aspiration gap can also be positive or negative and is divided into PSGS and NGGS two variables. Details are provided in Table 1.

Moreover, according to previous studies, this paper included the business characteristics that may affect business inter-temporal choice decisions in the model as control variables, such as firm age, size in terms of employee number, industry, the market index of location city. Entrepreneur demographics are also examined in the analysis, including entrepreneur age, gender and human capital reflected by education. Sources and specific design of each variable are shown in Table1.

RESULTS AND DISCUSSION

Descriptive statistics

Table 2 demonstrates the mean, standard deviation and correlation coefficients of the key variables. In view of firm characteristics, the average age of our sample firms is 9.4 and the leverage ratio is about 21%. As to the entrepreneur demographics, we found the mean age of entrepreneurs is 46 and 87% are male, indicating young male entrepreneurs dominate Chinese private enterprise sample. For the entrepreneur human capital, we see the average education category lies in 3.16, meaning most of them entry into entrepreneurship without university education.

Concerning for the correlations, family firm identity is positively correlated with firm long-term orientation, initially supporting the long-termism of family firms. When coming to the performance feedback, positive historical aspiration gap and social aspiration gap both are significantly and positively related with firm long-term orientation. Large firm and prior good performance are also ppromoting more long-term oriented investments, while firm age and entrepreneur education have negative impacts on firm long-term orientation. To exclude the possible effects of firm and individual level variables, we included firm characteristics and entrepreneur demographics as control variables.

Regression analysis and hypotheses testing

To test the theoretical hypotheses proposed in the prior section, we used OLS regression and included the interaction term to examine the moderating effect. The results are reported in Table 2. Specifically, Model 1 is the basic zero model for reference, just including the control variables. Model 2 further added family business identity variable *FAMILY* to testify Hypothesis 1. Model 3 to Model 6 are corresponded to Hypothesis 2. In specific, Model 3 and Model 4 are for positive and negative historical aspiration gap(*PSGH* and *NGGH*), while Model 5 and Model 6 are for positive and negative social aspiration gap (*PSGS* and *NGGS*).

Model 2 shows that family business identity is positively related with firm long-term orientation (β=0.136, t=2.24), indicating family firms are really performing more long-term oriented investments than non-family firms. Thus, Hypothesis 1 is supported. To examine the performance feedback effect, Model 3 and Model 4 evidenced the role of historical performance aspiration gap. The coefficients for the interaction variables are both positive and significant(β=0.608, t=6.11 for *FAMILY*PSGH*, in Model 3;β=0.376, t=2.73 for *FAMILY*NGGH*, in Model 4) , supporting the strengthening effect of historical performance aspiration gap. The direct effect of *PSGH* and *NGGH* are both positive and interesting, which implies that firm long-term investments would increase when firm performance deviates from historical aspirations, revealing a different mode of performance feedback. Additionally, Model 5 and Model 6 examined the role of social performance aspiration gap. The coefficients for the interaction variables are insignificant(β=0.005, t=0.3 for *FAMILY*PSGS*, in Model 5;β=-0.304, t=-1.43 for *FAMILY*NGGS*, in Model 6) , not supporting the strengthening effect of social performance aspiration gap. Therefore, Hypothesis 2 is partially supported.

On the control variables, firm leverage and entrepreneur education are persistently and negatively related with firm long-term orientation, while firm prior performance has positive influence on firm long-term investments. Other control variables are mostly insignificant in the models.

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Table-2: Descriptive statistics and Correlations

	LTO	FAMILY	PSGH	NGGH	PSGS	NGGS	FIRMAGE	LNEMP	AGE	GENDER	EDU	MARINDEX	LEVERAGE	ROS8
LTO	1.00													
FAMILY	0.04	1.00												
PSGH	0.23	-0.01	1.00											
NGGH	0.01	-0.01	0.00	1.00										
PSGS	0.27	0.02	0.78	0.00	1.00									
NGGS	0.00	-0.01	-0.01	0.99	-0.01	1.00								
FIRMAGE	-0.01	0.15	0.01	-0.02	0.01	-0.01	1.00							
LNEMP	0.05	0.02	0.05	-0.03	0.05	0.00	0.18	1.00						
AGE	0.01	0.23	0.01	-0.02	0.02	0.00	0.22	0.22	1.00					
GENDER	-0.03	0.02	0.01	0.01	0.01	0.01	0.05	0.09	0.07	1.00				
EDU	-0.08	0.16	-0.03	0.00	-0.04	0.00	0.02	-0.20	0.16	0.02	1.00			
MARINDEX	-0.02	0.03	-0.01	-0.01	-0.02	0.00	0.07	0.09	0.06	0.06	0.02	1.00		
LEVERAGE	-0.05	0.03	0.02	0.03	0.01	0.04	0.05	0.29	0.10	0.09	-0.08	0.14	1.00	
ROS8	0.25	0.02	0.71	-0.43	0.90	-0.44	0.02	0.05	0.02	0.01	-0.03	-0.01	-0.01	1.00
MEAN	-0.06	0.21	0.06	0.08	0.26	0.33	9.4	3.98	46.26	0.87	3.16	8.61	0.21	0.26
STD.DEV.	1.07	0.41	1.09	2.21	5.57	2.69	4.29	1.51	8.46	0.34	1.1	2.19	0.28	6.2

Notes: N=2275. Coefficients larger than 0.03 is significant at 0.1 level.

Table-3: OLS Regression of long-term orientation on family business and performance feedback

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
FIRMAGE	-0.006	-0.007	-0.007	-0.007	-0.007	-0.007
	(-1.05)	(-1.27)	(-1.27)	(-1.18)	(-1.21)	(-1.24)
LNEMP	0.023	0.024	0.026	0.026*	0.026	0.026
	(1.44)	(1.51)	(1.63)	(1.67)	(1.63)	(1.62)
AGE	0.003	0.001	0.001	0.002	0.001	0.001
	(0.88)	(0.43)	(0.48)	(0.63)	(0.42)	(0.45)
GENDER	-0.073	-0.072	-0.076	-0.078	-0.077	-0.076
	(-0.91)	(-0.91)	(-0.96)	(-0.98)	(-0.97)	(-0.96)
EDU	-0.051**	-0.057***	-0.056***	-0.060***	-0.055***	-0.055***
	(-2.47)	(-2.84)	(-2.79)	(-3.10)	(-2.72)	(-2.73)

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MARINDEX	-0.011	-0.011	-0.010	-0.009	-0.009	-0.009
	(-1.09)	(-1.09)	(-1.01)	(-0.98)	(-0.97)	(-0.96)
LEVERAGE	-0.237***	-0.242***	-0.262***	-0.262***	-0.257***	-0.257***
	(-3.07)	(-3.14)	(-3.45)	(-3.44)	(-3.38)	(-3.38)
ROS8	0.042***	0.042***	0.006	0.052***	0.001	0.052***
	(3.43)	(3.42)	(0.81)	(6.83)	(0.37)	(6.59)
FAMILY		0.136**	0.125**	0.112*	0.135**	0.223**
		(2.24)	(2.06)	(1.87)	(2.23)	(2.36)
PSGH			0.164***			
			(2.68)			
FAMILY*PSGH			0.608***			
			(6.11)			
NGGH				0.066***		
				(7.02)		
FAMILY*NGGH				0.376***		
				(2.73)		
PSGS					0.048***	
					(2.81)	
FAMILY*PSGS					0.005	
					(0.30)	
NGGS						0.051***
						(6.45)
FAMILY*NGGS						-0.304
						(-1.43)
_CONS	0.244	0.305	0.290	0.272	0.290	0.267
	(1.15)	(1.42)	(1.35)	(1.28)	(1.35)	(1.25)
R2_A	0.094	0.097	0.112	0.117	0.109	0.110
F	3.225***	3.785***	351.015***	5.298***	1420.062***	4.943***

Notes: N=2275. t statistics in parentheses. * $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$

CONCLUSION

The difference between family and non-family firms has been a common topic in family business research, ranging from performance, governance to strategic behaviors. Though performance implications of family influence are not sure due to sampling and definition issues, long-tem orientation is often cited as the rational for family firm behaviors. This study empirically tested the long-term orientation hypothesis of family firms and examined the moderating role of performance feedback, employing the Chinese Private Enterprise Survey. The results show that family firms generally perform more long-term oriented investments than non-family firms in China. As to the performance feedback effect, we found only historical performance aspiration gap moderated the difference between family and non-family firms. It indicates that when firm performance deviates from historical not social aspirations, family firms will show more long-term orientation than non-family firms.

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