Firms in developing countries

Lecture 10/2: Family firms

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Overview

- Characteristics of family firm
- concentration of ownership, control and key management position among family members
- Family businesses are very common in Latin America, Africa and the Middle East, Asia (except Japan), and in parts of western Europe.
- Why are family firms so prevalent? whether family firms evolve as an efficient response to the institutional and market environments, or whether they are an outcome of cultural norms
- ??family ownership and management are utility-maximizing for founding families rather than value-maximizing (profit)

Why family firms?

- Family control creates comparative advantage for firms, achieving better outcomes over nonfamily firms
- Many family firms operate in longevity and become very successful.
- They view their family firms as trust and legacy they are responsible for, rather than something they own.
- Trust between family members can be a substitute for missing governance and contractual enforcement, especially in countries with weak legal structures.
- When human capital is transferred within family and when there is strong within-family managerial talent, it is more beneficial in doing business with family involvement.
- Family firms' connections may help preferential access to public resources, especially in high levels of corruption economy.

What do the data say?

- How much systematic evidence is there for the economic superiority of family controlled business?
  - Family firms underperform relative to nonfamily firms.
  - But, the result maybe be subject to many possible omitted variable and selection biases.
- Countries where family is generally regarded as more important have lower levels of per capita GDP, smaller firms, a higher fraction of self-employed, fewer publicly traded firms, and a smaller fraction of total market value controlled by families.
- Data from the World Values Survey

Family values and economic development

- Countries with stronger family ties have lower GDP per capita.
  - Controlling for human capital weakens the effect of family values on GDP.

Table 2

GDP Per Capita and Family Values

	Dependent variable: log(GDP per capita) in 1990									
	(1)	*(2)*	*(3)*	*(4)*	*(5)*	*(6)*	*(7)*	*(8)*	*(9)*	*(10)*
Strength of family	−.37	−.15							−.34	−.15
	(.06)	(.06)							(.07)	(.07)
Log(schooling)		1.11	1.35	1.33	1.07	1.16	1.43			1.08
		(.20)	(.17)	(.18)	(.21)	(.19)	(.17)			(.21)
(Un)importance of family			2.36							
			(1.12)							
Parental duty to child				−1.41						
				(.88)						
Respect for parents					−1.87					
					(.69)					
Obedience of child						−1.62				
						(.64)				
Independence of child							.07			
							(.48)			
Trust								3.01	.50	.31
								(.74)	(.85)	(.70)
R^2	.47	.70	.68	.66	.69	.69	.64	.25	.47	.70
N	51	52	46	46	46	46	46	52	51	46

Notes: The unit of observation is a country. All family values, except "strength of family," are country means directly computed from the World Values Survey. "Strength of family" is the first component from a principal component analysis of the 5 family values described in Table 1. "Schooling" is defined as average schooling years in the total population over age 25 as of 1985. Ordinary least squares estimations; standard errors are reported in parentheses.

Family values or Trust?

- Putnam (1995) and Fukuyama (1995) support that trust will help countries to develop the large-scale organizations in a modern economy.
- Knack and Keefer (1997) and La Porta et al. (1997) explored cross-country data and found a positive correlation between trust and economic development.
- Table 2 column 8-10 explain how much of the correlation between GDP and family values can be explained away if we include trust as an additional control.
  - coefficient on family values in col. 9-10 barely changes compared to that in col.1-2.
  - The importance of trust for economic outcomes is a function of family values in a society. the family variables might be a better proxy for trust.

Family values

- Table 4: Family norms are fairly stable over the short to medium run. It does not likely appear that family values.
  - Need longer data for long-run analysis
- Table 5 shows moderate support to the idea that stronger family values should be mainly interpreted as a reflection of weak formal institutions