Family Succession and Firm Performance among Malaysian Companies

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Abstract

Family succession is one of the prevalent topics discussed in family management. However, there is lack of research on the issue of succession in Malaysia despite the fact that about 70% of listed companies in Malaysia are owned by family related business. Thus, this study aims to examine the relationship between family succession attributes and firm performance. This study adopted balanced panel data analysis for 975 companies listed on Bursa Malaysia for the year 2003 to 2007. The findings indicate that some of the family succession attributes do influence firm performance. Family ownership was found to be positively related with firm performance. Families are motivated to work efficiently when more shares were in their hands. Furthermore, the results reveal that successors-managed firms have better firm performance than founder-managed firms. The findings provide evidenced that Malaysian family firms do plan for their successions. More importantly, it opens up the possibilities for further study of family succession, both in Malaysia and on global basis.

Keywords: Family succession, performance, Malaysia.

1.0 Introduction

One of the most prevalent topics in the family business management literature is succession planning (Chua, Chrisman & Sharma, 2003). Succession planning should be initiated at a very early in the offspring's life (Davis, 1968; Stavrou, 1999). A proper succession process affords family firms the opportunity to select effective leaders who are capable of rejuvenating their firms (Ward, 1987). But it is a difficult tasks to accomplish. Usually, founders either fail or refuse to plan for the succession of the family business (Danco, 1982; Ward, 1987). It is also difficult to find a competent family member who is willing to take over the control of the family firm, or the offspring of family managers may be reluctant to join the firm (Blotnick, 1984).

Other reasons that contribute to failure in succession are that founder's reluctance to plan for succession, founder's strong sense of attachment to the firm (Kets de Vries, 1993), fear of retirement and death, lack of other interests by the offspring (Levinson, 1971; Starvou, 1999), offspring life stage (Ward, 1987), gender and birth order (Goldberg & Wooldridge, 1993), the offspring competency, involvement in the family firm (Davis, 1968) and personality traits (Goldberg & Wooldridge, 1993).

Moreover weaning children to take over the wheel of a firm has become a lot more challenging. There will be a tough challenge for family firms seeking to pass the torch to their children in the future (Gabriel, 2007). For instance, the Khind Holdings Bhd Group Chief Executive Officer (CEO) Cheng Ping Keat, who is the son of the company founder, also admitted that keeping a family business alive is the toughest management job on earth (Damodaran, 2006).

There is a Chinese saying that claimed "wealth does not endure three generations". This statement may be a coincidence or not, but many Asian family firms tend to suffer from this phenomena (Ngui, 2002). Wong (1985) argued that a Chinese family firm could seldom last longer than three generations because of the offspring would take their propensity for granted and lack of motivation to sustain the firm. For examples, Tan Chong Motor Holdings Bhd and the Hong Leong Group were firms that faced this kind of conflicts in their second generations. In Tan Chong case, the two Tan brothers (Tan Sri Tan Yuet Foh and Datuk Tan Kim Hor) have established the Tan Chong Bhd in 1958. Later the conflicts started when Datuk Tan Heng Chew, the eldest son of Yuet Foh, openly clashed with his uncle and cousins in a legal tussle in the Malaysian courts. As a result, family wealth had been divided. Tan Heng Chew was awarded 16.7% stake in Tan Chong Consolidated Sdn Bhd (TCCS), the private holding company for Tan Chong Motor Holdings Bhd. His uncle and family patriarch Datuk Tan Kim Hor was given a smaller 10.29% stake. However, Heng Chew's brothers, cousins and mothers were also shareholders of TCCS. Heng Chew was also the chairman of two listed firms within the group: APM Automotive Holdings Bhd and Warisan TC Holdings Bhd. The court judgements strengthen Heng Chew's position at the expense of the other family member (Datuk Tan Kim Hor).

Many of the third-generation in the West has also evolved into managerial corporations. But among Asian families, total professional management in a family company is rare. Nevertheless, the move towards hiring professionals into the family firms is gaining popularity. Therefore, Malaysian family firms have started considering bringing professionals in managing the family firms. For example, Lee Kong Chian, who founded Lee Rubber-OCBC Bank Holdings Ltd, was one of the first family patriarchs to incorporate professional managers in their family firm. That was way back in the 1940s and 1950s. Today, a largely professional team runs the OCBC Bank with little influence by the Lee family, although family members still sit on the board. Another case is that of Public Bank Bhd which is controlled by Tan Sri Teh Hong Piow. The bank is now professionally managed by Teh and his team of managers. Although Public Bank is seen as Teh's creation, but none of his children hold significant positions within the group. Thus, based on the above discussion, are Malaysian family companies ready for succession planning? Does family succession affect the firm performance?

Thus, the issue of family succession has motivated the researchers to carry out this study. In Malaysia, a study by Shamsir Jasani Grant Thornton (2002) has briefly discussed on succession planning. However, the study only provides a brief review on the current practice of family succession descriptively without analyzing the impact of the succession planning and other important business issue such as business financial performance. Hence, this factor has enthusiastically motivates the researchers to carry out this study.

The objective of this study is to examine the family succession attributes with firm performance for family firms. This study aims to find out the answers whether there is any association between firm performance and succession attributes.

In term of the contribution, this study is expected to increase the level of understanding with regards to family business firms especially in Malaysia. Particularly, this study uses sample of Malaysian public listed firms and the findings may be useful to Malaysian family businesses and the comparison can be made with family firms in other countries. Next, there is a lack of study carried out on family succession in Malaysia and elsewhere. Therefore the findings may explain the current situation on succession planning in Malaysia. It can also provide signals and guidance to the owners of family firms on the readiness of succession planning in Malaysia.

In term of the organization of this paper, it is structured as follows. In the introduction section, an overview on family successions is discussed. This is followed by the discussion on the motivation, objective and contribution of the study. The next part discusses the theoretical framework and hypothesis developments. Then research methodology is then explained in the next section. Next, sections that elaborate on results and discussions. The last section concludes and provides the implications of the study on academic and practice.

2.0 Theoretical and Hypothesis Development

2.1 Family Succession

Family firms need to plan ahead in making sure the family firms will sustain for next generations. In planning for succession, factors such as family ownership, hiring professional manager or family director, successor's education level, founder/successor's age and gender need to be considered in ensuring a successful family business succession.

Family ownership

Based on the agency theory, family ownership is claim to be efficient in minimising agency problems because shares are in the hands of agents who have special relations with other decision agents that allow agency problems to be controlled without separation of the management and control decisions. Further, family members have many dimensions of exchange with one another over a long horizon, and therefore, have advantages in monitoring and disciplining the agents (Fama & Jensen, 1983).

In family firms, ownership is concentrated in the hands of family firms, therefore the risk of free riding is likely to diminish (Shleifer & Vishny, 1997). Jensen and Meckling (1976) and Fama and Jensen (1983) supported that a family's involvement in ownership and management could shun the problem of possible exploitative behaviour of the agent towards the principal, and minimise the supervision costs. While Gorriz and Fumas (1996) evidenced that agency costs are minimized when shares are concentrated in a few owners and these owners do all the decision process.

According to stewardship theory, ownership and control concentration is one of the factors that influence the effects of family relationships in family firms. Indeed, this variable helps explain the motivation for members to act as stewards of the firm versus their propensity to act destructively (Corbetta & Salvato, 2004). Researchers believed that family ownership do motivate directors to work in line with firm's objectives, thus maximise the shareholder wealth. Family directors are also able to avoid the exploitative behaviour of the agent. Therefore, family ownership may influence firm performance in a positive way. Thus, we hypothesize that:

> *H_1: Ceteris paribus, family directors that hold higher percentage of share ownership encourage higher firm performance than family directors with lower percentage of share ownership.*

Owner or Professional Manager

Studies have found that family-owned and managed firms reach higher performance than those that are professionally managed (Monsen, Chiu, & Cooley, 1968; Daily & Dollinger, 1992). Previous studies also showed that the agency costs are significantly higher when professionals manage the firms (Ang et al., 2000). Nevertheless, professional directors play an important role in the family firms (Ibrahim et al., 2001). The professionals may have particular knowledge of the firm that may be proved to be valuable in mentoring of future-generation leaders, or filling in the leadership role (Lee et al., 2003). In larger firms, professionals have been found to play a critical role in strategic decision-making in family firms (Chua et al., 2003). Studies by Lauterbach and Vaninsky (1999) in Israel and Chittoor and Das (2007) in India found that management succession to a professional manager has a positive impact on the performance. Based on the above literatures, there were mixed results although the majority of studies showed that family managers outperform professional managers. Hence, this study hypothesizes that:

> *H_2: Ceteris paribus, family firm that is managed by family CEO has higher firm performance than family firm managed by professional manager.*

Successor Education

Education background of the CEO that manages the company is also vital in ensuring the survival of the family firms. Today, the trend for enhancing successor education level has changed. Future prospective successors have been sent abroad by their parents for education. Successors also are opting for college in addition of working with someone else. In the past, families CEOs were found to posses fewer academic credentials (Brockhaus & Nord, 1979). Instead, the informal training received by children within the family may be a substitute to formal managerial training received through educational institutions (Lentz & Laband, 1990). Nowadays family firms need to give more attention to successor's education in ensuring the survival and growth of firms in the globalised world (Ibrahim & Ellis, 1994). Based on the above arguments, researchers expected that education to play a vital role in the family firm survival. Family firms need to have successors that are well educated, knowledgeable and well-equipped with current business situations. Then only the family firms can sustain in this competitive business atmosphere. Therefore, we hypothesize that:

H_3: Ceteris paribus, successor with higher education level enhance firms' performance than successor with lower education level.

Founder/Successor Age

Brockmann and Simmonds (1997) argued that managerial success is positively correlated with age. It is argeud that when the manager is older in age, thus the chances of firm's managerial success is higher as compared to younger manager. This may also be due to the level of experience that the manager's possess. Older executives also tend to be more risk averse than younger executives (Carlsson & Karlsson, 1970). According to Smith and Amoako-Adu (1999) in Canada, the stock market reacts negatively to the appointment of young family successors. This reaction showed that due to successor's young age, investors seem to have less confidence and it also reflects a lack of management experience in the successors. Thus, age is also an important element in succession planning. Based on the arguments, it is hypothesize that:

H_4: Ceteris paribus, founder/successor that is more matured in age lead to higher firm performance than founder/successor that is young in age.

Gender

The successor's gender is also being a debated issue in family succession. Who shall be the next leader in the family firm? Most companies would prefer to select male compared to female successor. Alcorn (1982) suggested that family firms are similar to monarchies in which the eldest son becomes the uncontested successor. A study carried out by Kuratko (1993) in Korea found that for succession purposes, firms prefer a son to take over the firm. Kets de Vries (1996) observed that some family firms in the US still see the choice of a daughter as rather undesirable. In Chinese family business, male is also preferred more than female because the male successor will carry the family name. Moreover, male managers tend to be more competitive, have larger networks, more supportive, tough and able to faced competition. There is also a perception that male perform better than female. Moreover, male gets more supports from families such as from parents and wife.

Female successors, on the other hand are more nurturing, supportive in the work environment, do not focus on the financial performance as an important element for firm survival, but they are more likely to focus more on the primary objectives of the firm (Butner & Moore, 1997). Dumas (1989) and Hollander and Bukowitz (1990) suggested that the father-daughter relationship is more harmonious and different in nature. Daughters willingly assumed the role of caretakers for both of the father and the business. They are less likely than sons to be in conflict with their fathers. A study by Fahed-Sreih and Djoundourian (2006) found that more than two-thirds of the Lebanese firms favor female CEOs in managing the family firms. The daughter-father relationship appears to be more mutually supportive and daughters appear to prepare more thoroughly than sons to take the control of the family business (Hartman, 1987).

Nelton (1998) stated that daughters and wives are rising to leadership positions in family firms more frequently than in the past, and that the occurrence of daughters taking over businesses in traditionally male-dominated industries is increasing rapidly. Since the arguments about gender and performance are mixed, we hypothesize (in null form) that:

H_5: Ceteris paribus, there is no difference in performance between male and female successor.

Generations

Planning need to been made in ensuring that companies do have potential successors that can manage the firms for the next generation. Previous studies have claimed that family members often commit deeply to the mission of the firms, treasure its employees, stakeholders and feel motivated to do their best for the family and the organizational as a collective decision makers (Davis, Schoorman, Mayer & Tan, 2000; Miller & Le Breton-Miller, 2005). However, Morck and Yeung (2003) argued that the successor is likely to be less able to manage the firms when corporate control passes from the founder to the next generation. A study by Rodsutti and Makayathorn (2005) evidenced a strong influence of the founder when the firm was in the first generation, but not in later generation. Firm performance also increased when founding family members were involved in the management (Lee, 2006).

McConaughy & Philips (1999) evidenced that the founder-controlled firms grow faster and invest more in capital assets and research and development. While the descendant-controlled firms generate more profit because of the experience of earlier generation. Therefore, based on the above arguments, researchers expected that later generation to have less impact on firm performance as compared to the founder generation. Moreover, in the later generations, family firms have already been established and there was plenty of capital. Thus, successors do not need to work hard from the scratch to create the image, reputation and market shares of the firms. With plenty of capitals and stable businesses, some successors may spend the business money excessively without proper planning. Therefore, we hypothesize that:

H_6: Ceteris paribus, founder (first generation) managed firm have higher firm performance than successor (later generation).

3.0 Research Method and Design

3.1 Sample Selection

This study utilised secondary data on the Malaysia public listed firms. The sample size used in this study were 975 Malaysian family firms listed on Main Board and Second Board of Bursa Malaysia (excluding banking and finance, and insurance sectors)[1] over the period of 2003 to 2007. In determining the family firms, the data on family directors' profile, ownership, qualification, education level, age, gender, generation are obtained from the annual reports, company announcements and business magazines. All the data was hand collected. The financial data was gathered from the Thomson Financial Datastream Advance. A cross-checking is done with the annual reports to make sure the reliability of the data.

3.2 Research Model and Measurement

The research model is discussed as below.

$$FPERF_{it} = b_0 + FAMOWN_{it} + PROF_{it} + DIREDUC_{it} + DIRAGE_{it} + GENDER_{it} + GEN_{it} + DEBT_{it} + FAGE_{it} + FSIZE_{it} + v_i + e_{it}$$

[1] The industry is regulated under The Banking and Financial Act (BAFIA), 1989. The BAFIA (1989) allow Financial Institutions (FIs) to make portfolio investments in non-financial business up to a maximum of 20% of a FIs shareholders' funds and up to 10% of the issued share capital of a company in which the investment is made. The FIs are not allowed to assume any management role to take up a board position (Chu & Cheah, 2004).

Where:

FPERF	= Tobin's Q
FAMOWN	= Family managerial ownership
PROF	= Professional non-family member
DIREDUC	= Successor education level
DIRAGE	= Founder/successor age
GENDER	= Successor gender
GEN	= Generation
DEBT	= Debt
FAGE	= Firm age
FSIZE	= Firm size
v_i	= Specific error
e_{it}	= Idiosyncratic error

3.3 Model Specification

The dependent variable Tobin's Q is defined as the market value of common equity plus book value of preferred shares and debt divided by book value of total assets (Yeh et al., 2001; Wiwattanakantang, 2001; Chu & Cheah, 2004; Chen, et al., 2005; Maury, 2006; Villalonga & Amit, 2006; Martinez et al., 2007; Ibrahim et al., 2008). Family firm was measured using dummy variable (0,1) to differentiate between family and non-family firm. The definition of family firm is in line with the previous studies (Villalonga & Amit, 2007; Anderson & Reeb, 2003). Family managerial ownership was measured using a continuous variable (percentage of direct and indirect shares). For succession variables, family manager/professional hired manager, successor education level, founder/successor age, successor gender and generations were measured using dummy (0,1) variables. The control variables were debt, firm age and firm size. Debt was defined as the book value of long-term debt divided by total assets. Firm age was defined as the number of years since incorporation. Firm size was measured as natural log of book value over total assets.

4.0 Results and Discussions

4.1 Univariate Tests

Insert table (1) about here

Based on Table 1, 33.3% of family firms in Malaysia involved in industrial products. The second highest is the consumer products sector with 20% involvement. The next sectors are the properties (12.8%), trading services (12.3%), constructions (10.3%) and plantations (7.7%). Others sectors such as technologies, hotels, properties and infrastructure projects have seen a small involvement by the family firms.

Insert table (2) about here

Table 2 explains the mean for Tobin's Q is 79.9%. ROA only show a smaller mean of 3.2% as compared to Tobin's Q. For family ownership, the average shareholdings by family members are around 43%. Interestingly, about 24% of Malaysian family firms have started to hire professional managers in managing the family firms. This indicates that family firms have considered accepting ideas and outside manpower in making sure that family firms will sustain for the future years. In term of founder or successor age, the average age is about 50 years. In term of generations, most of Malaysian family firms are in the second generations and only few companies that are in third generations.

Insert table (3) about here

Based on the t-test results, Table 3 reveals that there is a difference between family ownership and firm performance when Tobin's Q was used as the performance indicator. Other variables FAMOWN, PROF and GEN also shown a significant different with firm performance.
The result shows that the higher the percentage of ownership owned by family managers, the higher the firm performance. This is because the interests of the managers are in line with the incentives that they deserved. Also, result shows that professional manager do enhance firm performance. However, this study found that Malaysian family firms do favour younger generations in managing the firm than the older generations. The young generations may be able to take higher risk, more creative, innovative and their ideas are in line with the current business environment.

Insert table (4) about here

Table 4 reveals the results from this study using panel data regression approach. Interestingly, the results from this study do support hypotheses H_1, H_3 and H_4. However H_2, H_5 and H_6 were not supported. In this analysis, Tobin's Q was used as a firm performance indicator. It was found that family ownership do positively relate with firm performance. This finding supported previous studies that family ownership minimized the agency costs in the firms positively affect firm performance. Moreover, family managers were stewards of the companies, so they worked seriously to maximise the shareholders wealth. Thus, the firm value was enhanced (Fama & Jensen, 1983; Shleifer & Vishny, 1997; Gorriz & Fumas, 1996; Corbetta & Salvato, 2004).

Next, result also indicates that director's education is negatively related with firm performance. This finding contradicts with previous literatures. In term of successor age, it was found to be significant, but in the opposite direction. It shows that younger successors perform better than older. Perhaps, younger managers are more energetic and eager to show their potential to their family members and hence this increases the firm performance level. Young managers were claimed to be more aggressive as compared older owners (Carlsson & Karlsson, 1970). Control variables (debt, firm size and firm age) were found to be significantly related with firm performance. In term of debt, the higher the debt value, the higher the firm performance. Also, result found that older the firms operated in the business have higher firm value. But in term of the firm size, large firm do have lower firm value as compared to small firm size.

5.0 Conclusion

Overall, family ownership do positively affect the firm performance. It shows that ownership is one of the mechanisms that help increase family firms performance. Younger managers were found to perform better than older managers. They are more energetic, visionary individuals and risk takers as compared to older managers. In term of the implication of this study, further studies can be research out on the topic of family succession because this issue is still new in Malaysian context. Clearly, Malaysian family businesses have started to plan for their succession in ensuring that firms sustain for next generations. Furthermore, standard setters and policy makers need to be aware that family firms do have certain characteristics (i.e. high familiness and strong family ties) that make them different from non-family firms. Thus, the implementations of rules and regulations need to consider these unique characteristics of family businesses.

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Table 1
Profile of the Sample Based on Sectors (n= 975)

	Frequency	%
Consumer products	195	20.0
Industrial products	325	33.3
Plantations	75	7.7
Trading services	120	12.3
Constructions	100	10.3
Infrastructure projects	5	.5
Technologies	20	2.1
Hotels	10	1.0
Properties	125	12.8
Total	**975**	**100.0**

Table 2
Descriptive Statistics for Variables (n= 975)

	Min	Max	Mean	SD
TOBIN'S Q	0.189	0.999	0.799	0.112
FAMOWN	.00	84.14	42.798	1 5.747
PROF	0	1	0.52	0.5
DIREDUC	0	1	0.56	0.496
DIRAGE	20	85	49.87	10.766
GENDER	0	1	0.96	0.194
GEN	0	2	1.28	0.461
DEBT	0	1	0.08	0.117
FSIZE	10.102	17.339	12.731	1.158
FAGE	0	53	7.79	9.536

Table 3
T-test for the Hypotheses Variables (n=975)

Variable	Tobin's Q
	t-value
FAMOWN	5.099***
PROF	4.95***
DIREDUC	-.039
DIRAGE	.296
GENDER	-.297
GEN	-2.558**

Note: For univariate analysis, FAMOWN is dischotomized by splitting the sample into high family ownership (.50%) and low family ownership (<50%). For DIRAGE, mature CEO is defined as those with the age of 40 years and above. Other variables are dummy variables.

Table 4
Panel Data Analysis Using Random Effect Model for Tobin's Q (n=975)

	Coef	**Std. Error**
Constants	1.087	.1336
FAMOWN (H_1)	.001***	.0002
PROF (H_2)	-.044	.0401
EDUC (H_3)	-.097*	.0572
AGE (H_4)	-.003***	.0019
GENDER (H_5)	.021	.0498
GEN (H_6)	.037	.0317
DEBT	.078***	.0298
FSIZE	-.016*	.0084
FAGE	.002**	.0009
F Stat (9, 771)		3.81
Prob > F		.0001