Bahavioral Characteristics of Entrepreneurs in the Gujrat, Gujranawala and Slalkot Industrial Clusters of Pakistan: A Comparisn of First, Second and Third Generation Family Firms

Shahid Qureshi, Faculty of Business Administration, Berlin Institute of Technology, Technical University Berlin, Wilmersdorfer Str 148, 10585 Berlin
Phone:0049-30-31478868
shahid@marketing-tromsdorff.de

Sarfraz A. Mian, S.U.N.Y. Oswego School of Business, 310 Rich Hall Oswego, N.Y. 13126
Phone: (315) 312-3154, Fax: (315) 312-5440
E-mail: mian@oswego.edu

Aif Iqbal Rana, Lahore University of Management Sciences Pakistan
E-mail: arif@lums.edu.pk

Abstract

This exploratory research focuses on the transition in entrepreneurial management practices among subsequent generations of family firms in Pakistan.. A random sample of several hundred SMEs lead by their first, second and third generation family entrepreneurs reveal a more conservative approach in terms of the inclusion of non-family members, females, enhanced team management, conflict resolution methods, succession plans, and the use of outside consultant for strategic planning and financial management. The research results add to the family business and international entrepreneurship literature at the same time providing better insights for the family entrepreneurs and consultants alike.

Key Words: Behavioural Characteristics, Family Entrepreneurs, Pakistan SMEs

1. Introduction

The entrepreneurial clusters of Gujarat, Gujranwala and Sialkot are the backbone of Pakistan’s economy. Together, they constitute 25 to 30% of the SMEs in the country and significantly contribute to much needed national exports. The management of majority of these industrial enterprises have already entered from first generation to second and then third generation entrepreneurs. This study is a replication of an earlier US study conducted by Matthew C. Sonfield et al, (2004) and adds to entrepreneurship literature by investigating the similarities and differences among first-, second-, and third – generation family businesses, as was suggested for further research by a number of authors. A random sample of 600 firms was selected from the published listings of several thousand firms from the chamber of commerce. Out of these, about 120 firms who strictly qualified as family businesses agreed to be surveyed. A detailed questionnaire was administered to CEOs of each company.

Hypotheses dealing with subsequent generations of family firms in terms of the inclusion of non-family members, females, enhanced team management, conflict resolution methods, succession plans, and the use of outside consultant for strategic planning and financial management, were tested. One-way ANOVA compared the questions among the three generations of entrepreneurs. Chi-square was used to compare the use of debt to equity by generations and ANCOVA was employed to test for spurious relationships.

The findings of this study are different as compared to the US study. The hypotheses supported in our case are the use of team management style and the degree of influence by original business objective and methods of the founder. A better understanding of these similarities and differences might enable family firm researchers to focus their future investigations into these three generational categories as separate entities.

This focus might also strengthen the effectiveness of advisors, consultants, and others who assist family firms by allowing them to differentiate, as needed between their first second and third generation family business clients. This will again assist family business owner/managers in their understanding and self analyses of their businesses for enhanced / sustained profits and better discharge of responsibilities.

Moreover, a comparison of the Pakistani and US based family firms shed some light on the cross-national differences in the behavioral characteristics of these firms.

2. Theoretical Foundation

Dyer and Sanchez (1998) have thoroughly analysed articles published during the first decade of Family Business Review journal. This review provides a clear relevance of prevailing directions in family business research. Some of the most frequent topics of articles published during this period are: interpersonal family dynamics, succession, interpersonal business dynamics, business performance and growth, consulting to family firms, gender and ethnicity issues, legal and fiscal issues, and estate issues. In terms of types of articles published, Dyer and Sanchez found that, the proportion of articles involving the use of quantitative research methodology increased, while articles specifically describing the art of helping family businesses declined over the decade.

Even with this maturity of the field there are a variety of definitions of the family business reported in the literature. The definition adopted for this study is the one used by (Sonfield & Lussier, 2004, p. 190). A family business is one in which family members dominate the ownership and management of a firm and perceive their business as a family business. This definition is consistent with that of many prior studies (Chua, Chrisman & Sharma, 1999; Dreux & Brown, 1999; Gersick, Davis, Hampton & Lansberg, 1997.

First, Second and Third Generation Family Firms and Hypotheses formation

The study investigates the changes which occur as family firms move beyond the first generation of family member ownership and explores any significant differences between first, second and third generation family firms. Sonfield & Lussier, (2004, p. 190) have defined the various generation family firms as follows: The First Generation Family Firms (1GFF) are defined as family owned and managed firm with more than one family member involved, but only of the first and the founding generation of the family. A 2GFF and 3GFF are defined as firms in which the second and third generation of the family firms are also involved in the ownership and the management of the company. In the second and third generation family firms the founders and the other members of the founding team may be retired from the firm or deceased. This definition is consistent with the previous studies on generational issues in family firms by several authors (Beckhard & Dyer, 1983, Davis & Harveston , 1999, Dyer 1998, Hershon, 1975 and Schein, 1983).The objective of this study is to examine three generations of family businesses found in the entrepreneurial clusters of Gujarat, Gujranwala and Sialkot of Pakistan. To explore this major Pakistani family business context the following hypotheses derived from the family business literature have been tested in the paper.(Sonfield & Lussier, 2004, p. 194)

Hypothesis 1: *Subsequent generation family firms are more likely than the first generation family firms to include nonfamily members within top management.*

Schein (1983) suggested that subsequent generations of family firms exhibit a greater tendency to utilise more professional forms of management. Dyer (1988), found that 80% of the first generation firms had a paternalistic management style and culture, where as 75% of the succeeding firms adapted a professional style of management. Paternalistic management meant hierarchical relationships, top management control of power and authority, close supervision and lack of trust on outsiders. On the other hand professionalism meant inclusion and importance of nonfamily managers. McConaughy and Phillips (1999) conducted a study on large publicly-owned family controlled firms and report that descendent controlled firms were more professionally run as compared to founder controlled firms. All these writers postulate that first generation family business managers are entrepreneurs with a special technical or business background necessary for the creation of their business, but the descendants often face the challenge of expanding the business, thus requiring the help of non family managers.

Hypothesis 2: *Subsequent generation family firms are more likely than the first generation family firms to have women family members working in the firm.*

Nelton (1988), studying gender issues reported that more women are rising to leadership positions in family business as compared to the past. Cole (1997), focusing on the societal trends rather than family firm generational issues found that the number of women in family businesses were increasing.
The same is evident by the recent formation of women chambers of commerce in the Pakistani context to support the women managers in family businesses (CMER 2004).

Hypothesis 3: *Subsequent generation family firms are more likely than the first generation family firms to use a "team management" style of management.*

Dyer1(988) found that decision making was highly centralised in the first generation of family firms than in descendents. Aronoff (1988) stated that in the subsequent generations the management style was more dominant, with parents, children and siblings having participative involvement in important decision making. Aronoff further reported that 42% of family businesses are considering co-presidents in the future.

Hypothesis 4: *Subsequent generation family firms are more likely than the first generation family firms to have conflict and disagreement between family members.*

Interpersonal relationships such as conflicts and disagreements among family members have been a major focus of family firm research. There is a low chance of conflict in the first generation family firms as there are few people in the management of the firm, however, it increases in the subsequent generations with the inclusion of other family members. Beckhard and Dyer (1983) reported that conflict among family members increases with the number of generations involved in the firm.

Hypothesis 5: *Subsequent generation family firms are more likely than the first generation family firms to have formulated specific succession plans.*

Another important area of research in family business is succession. The various issues involve the transfer of power and control to the next generation, the lack of leadership preparation in the next generation and the need of succession planning. Fiegener and Prince, (1994) compared successor planning and development in family and non family firms and reported that family firms favour more personal relationship oriented forms of successor development, while non family firms utilise more formal and task oriented methods. Stavrou, (1988), developed a conceptual model to explain how successor managers are chosen in family firms.
This model involves four factors that define the context for succession: family, business, personal, and market. As the need of succession planning is well established, it is expected that subsequent family firms are more likely to recognise the importance of succession related research.

Hypothesis 6*: Subsequent generation family firms are more likely than the first generation family firms to use outside consultants, advisors, and professional services.*

Hypothesis 7: *Subsequent generation family firms spend more time engaging in strategic management activities than first generation family firms.*

Hypothesis 8: *Subsequent generation family firms are more likely than the first generation family firms to use sophisticated methods of financial management.*

The research on family firms reports that as these firms age and move towards subsequent generation, they also progress from one form of management to another. The informal, subjective and paternalistic styles of leadership become more formal, objective and professional. (Aronoff, 1998; Cole & Wolken, 1995 ; Coleman & Carsky, 1999; Dyer, 1998; Filbeck & Lee, 2000; McConaughy & Phillips, 1999; Miller, McLeod, & Oh, 2001; Schein, 1983).Professional management may include 1) the use of outside consultants, advisors and professional services 2) more time engaged in strategic management activities, and 3) the use of more sophisticated financial management tools. These conclusions lead to the above mentioned hypotheses.

Hypothesis 9: *Top management style and decisions in subsequent generation family firms are neither more nor less likely than in first generation family firms to be influenced by the original business objectives and methods of the founder.*

Davis and Harveston (1999) raised an interesting issue of generational shadow in family business. In a multigenerational family firm, the shadow of the firm has a strong impact on the organisation and the processes. This shadow can have a positive and negative effect on the performance of the firm. It can be positive by providing a clear set of values, direction, and standards for subsequent firms.
(Kelly et al., 2000) proposed that family founder' original business objectives will influence the strategic behaviour of succeeding firms managers in a positive and a negative way. Davis and Harveston (1999) investigated generational shadow and reported a mixed conclusion regarding its impact.

Hypothesis 10: *Subsequent generation family firms are more likely than the first generation family firms to have considered going public.*

As the family firms move into next generations and grow in size, they need more resources and skills to capitalise the opportunities. The family business may not be able to provide the required managerial and financial resources for growth and may look for outside ownership. McConaughy (1994) found that 20% of the BusinessWeek 1000 firms are family controlled.

Hypothesis 11: *Subsequent generation family firms are neither more nor less likely than first generation family firms to use equity financing rather than debt financing.*

Capital structure decisions are also important for family businesses. The literature does not support in a given direction. Bork, Jaffe, Jane, Dashew and Heisler (1996) and Gerisick et al., (1997) have reported that first generation family businesses mostly use equity financing. Cole and Wolken (1995) and Coleman and Carsky (1999) found that older and larger firms (subsequent firms) use more equity financing and less debt financing than younger firms. Thus the literature points that both first and subsequent generations mostly use equity financing.

3. Research Methodology

(a) Sample

A random sample of 600 firms was selected from the published listings of several thousand firms from the chamber of commerce. Out of these, about 120 firms who strictly qualified as family firms were selected. Due to the chances of a very low response rate of the mailed survey, direct interviews of the owners of the family firms were conducted. Ten teams of final year MBA students conducted the survey. Out of the 120 firms selected, 106 were available for a detailed interview. Data from six firms was incomplete and was not used in the analysis. Identifying family firms from published listings results in a convenience sample rather than a pure random sample. However, this smpling methodology is consistent with other family business researchers, which face the constraint of a lack of a national database of family firms. (Chua et al, 1999; Teal, Upton & Seaman, 2003)

(b) Variables Measured

All of the variables measured are taken from the literature. The primary independent variable is the number of generations involved in the operations of the family business. The nominal measure is one, two or three generations involved in business. The dependent variables to test the Hypotheses 1-11 are as follows. 1) Does the firm have non family managers? i.e., the percentage of family to non family managers. 2) The percentage of male and female family members involved in the operations of the firm.

Hypotheses 3-10 used the Likert interval scales of : "Describes our firm" 7, to 1 "Does not describe our firm". 3) Full family involvement in decisions. 4) Level of family conflict. 5) Formulation of succession plans. 6) Use of outside advisors. 7) Use of long range planning. 8) Use of sophisticated financial management tools. 9) Influence of founder. 10) Going public. 11)

The use of debt or equity financing was a nominal measure of one or the other. Descriptive statistical data included number of years the firm was in business, the number of employees, industry (product or service) and form of ownership.

(c) ANOVA (Analysis of Variance)

The Hypotheses 1-10 compared the dependent variable among the three generations (independent variable) using one way ANOVA. Chi square was used to test Hypothesis 11 as it was a nominal measured variable. Debt to equity was compared within the three generations.

(d) Control Variable ANCOVA

Covariance explains how one variable changes in relation to another. ANCOVA (Analysis of Covariance) was used to test for spurious relationships i.e. the variance in the dependent variables being explained by a variable other than generation (number of employees, service/manufacturing, years of operation and legal form of business)

4. Results

(a) Descriptive Statistics

A summary of descriptive statistics is given in Table 1. Out of a sample of 100, the number of first generation family firms was 31, second generation family firms was 51 and third generation family firms was 18. The mean years the sample family firms were in business were 21 (1GFF=14, 2GFF=23, 3GFF=31). As the number of generations increase, the longer the firm is in business. The mean number of employees was 76 (1GFF=54, 2GFF=88, 3GFF=78). More businesses (56/44%) provided a service in the first generation family firms. The subsequent generation family firms are however more involved in manufacturing. Very few firms evolved into a corporation.

Most of the 1GFFs (58%) and 2GFFs (71%) were in the form of sole proprietorship, while most of the third generation firms 64% were in the form of a partnership.

(b) Hypotheses ANOVA Testing

ANOVA was carried out. Two hypotheses were supported. H3- there was a significant difference ($p=0.032$) in the use of team management style in the Pakistani context between the first generation and the subsequent generation family firms. H-9- was significant ($p=0.033$) showing that there was an influence of the original business objectives and methods of the founder on the top management styles and decisions.

(c) Hypotheses ANCOVA Testing

As discussed, ANCOVA was run to determine if spurious relationships existed. ANCOVA was run to test each hypothesis with regard to four control variables 1) number of employees, 2) service/manufacturing, 3) years of operation and 4) legal form of business. This analysis found no spurious relationship inconsistent with the hypotheses.

5. Discussion

Similar to the study conducted by Sonfield et al (2004) much of the existing literature regarding possible generational differences among family firms is not supported by the current study. In most respects 1GGFs, 2GFFs, and 3GFFs share the same characteristics and behavioural patterns. It apparently seems that the force of the family ties and the system of the family firm are stronger, even in subsequent generations, than is the influence of non family firm forms of management thinking and behaviour. Thus these findings generally do not support the conclusions of previous researchers (Aronoff, 1998; Beckhard and Dyer, 1983; Cole and Wolken, 1995; Coleman and Carsky, 1999; Davis and Harveston, 1999; Dyer, 1988; Mconaughy and Philliphs, 1999; Miller et al 2001, and Schein, 1983), all of whom postulated generational differences among family businesses.

In support of the generational findings of the earlier literature, it was found that in our case the second generation family firms (2GFFs) exhibit more usage of the team-management style, in comparison to the first generation family firms (1GFFs). This finding, however, is in contrast to the US study, which did not find support for this hypothesis.Our hypotheses also support the literature that decision making is more centralised in the first generation family firms than in subsequent generation family firms and therefore they are less likely to engage in team management. However the subsequent family firms are more likely to engage in team management, with parents, children and in the firm having a participative involvement in important decision making, even if one family member is the nominal leader of the business.

Moreover in support of the literature all of the three generation family firms (1GFFs, 2GFFs, and 3GFFs) were all equally influenced by the original business objectives and methods of the founders of the firm.
Generational shadow and the legacy centrality as described in the literature, remain in force beyond the first and even the second generation of a family firm. This finding is consistent with the conclusions of Davis and Harveston (1999) and Kelley et al. (2000). Another observation regarding the form of ownership is that most of the 1GFFs and 2GFFs are sole proprietorships and as they become more established they evolve into partnerships to arrange more financial and managerial resources. The tendency to become a corporation is very low in the Pakistani context.

Comparison with the US study

The research on Pakistani family firms data reveal some similarities and differences with the US study. Both of the studies do not support a majority of the hypotheses, indicating that there are a lot of commonalities among them The results, however, differ in the following aspects:.

- Hypotheses H-3 (Subsequent firms are more likely to observe a team style).
  The Pakistani study supports this hypothesis, while the US study does not support it. The apparent reason seems to be the cultural aspects in the Pakistani families to work in a team style. Family owned firms are a mode of organisation, where the primary source of management expertise, finance and market information comes from within the family. Therefore, it is necessary for them to have a much wider network based on trust and shared ideals of the members, where the members extend to uncles, aunts and cousins. Although this definition is also applicable to the Western World. There are some factors reported that make the Pakistani family firm different from the US firms. An important differentiating factor is that of family involvement, which also extends to distant relations like second and third cousins and close family friends. Similar to other countries in the South Asian region, an important way to expand businesses has been through intermarriages (Rida Zaidi & Ahmad Aslam, 2006,p.5).

- Hypotheses-H5 (Subsequent GFFs are more likely to formulate succession plans as compared to 1GFFs) difference is significant. The US study supports this hypothesis, while the Pakistani study does not support it. The apparent reason seems to be the competitive environment in the US forcing them to plan for the succession to ensure continuity in the business. Afghan and Tayyaba (2007) report that succession planning and documented procedures for developing and grooming successor were less observed in their study. However the successful family businesses were moving away from kinship culture towards professionally managed business operations and eventually listing themselves on the stock exchange to stop the division of the business during the succession phase.

- There is another significant contrast in terms of Hypotheses H-11 (Use of equity financing rather than debt financing). The US data shows that only first generation family firms (1GFFs) used about 40% of equity funding and then this amount reduced drastically in the subsequent generations firms to 12% and 33 %. In other words the subsequent 2GFFs and 3GFFs resorted for debt financing. In contrast the Pakistani data reveal that the use of equity funding is on the rise as the businesses transition from the first generation to subsequent generation family firms.

- Another difference is in the involvement of women in family businesses. According to the US data about 30% of the women family members are working in the firm. In contrast the figure is much low in Pakistan (less than 3%). The apparent reason for this is cultural traditions of the subcontinent.

- Due to dominance of males in the society, female involvement is very little within the family firm. Their role is restricted to a silent share holder, i.e. they usually have equity holdings in the firm but hold no executive position. This skewed structure is however changing in recent years, where more family members are being appointed to directors and executive positions. (Rida Zaidi & Ahmad Aslam, 2006, p.6).

- Both of the studies support the Hypotheses-H9 (The founders influence on the top management styles and decisions in the 1GFFs and subsequent GFFs) in a similar manner. Therefore, generational shadow and the legacy centrality as described in the literature, remain in force beyond the first and even the second generation of a family firm in both of the studies.

6. Conclusion

Since most of the prior studies carried out on the examination of generational issues were only a small part of the broader family firm issues, the hypotheses used for this study provide limited research conclusions. This lack of existing empirical research literature is a limitation to this study. These current findings indicate a need for more extensive analysis of similarities and differences among different generation family firms and their managerial implications in other contexts. The replication of the US study highlights the similarities and differences of the two cultures and helps in comparing the family business issues in developing and developed nations.A better understanding of these similarities and differences might enable family firm researchers to better focus their future investigations into these three generational categories as separate entities. This focus might also strengthen the effectiveness of advisors, consultants, and others who assist family firms by allowing them to differentiate, as needed between their first second and third generation family business clients. This will again assist family business owner/managers in their understanding and self analyses of their businesses for enhanced / sustained profits and better discharge of responsibilities. Moreover a comparison of the Pakistani and US based family firms shed some light on the cross-national differences in behavioural characteristics of their respective family firms.

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Table 1: Descriptive Statistics

Variable	1GFF	2GFF	3GFF	Total
Generation	31	51	11	100
Years in Business (mean)	14	23	31	21
Number of employees (mean)	54	88	78	76
Service Sector (%)	56%	44%	0%	
Manufacturing Sector (%)	44%	56%	100%	
Ownership: Corporation %	3	0	0	
Ownership: Partnership %	39	29	64	
Ownership: Sole proprietorship %	58	71	36	

Table 2: One Way ANOVA Hypotheses Comparison by Generation (n= 100)

Hypotheses	1GFF	2GFF	3GFF	F	p
1. Use of non family members within top mgt (% non family)	36	33	31	.078	.925
2. Women family members working in firm (% of women)	0.15%	0%	0.17%	2.447	0.092
3. Use of team style (7-1)*	4.36	5.3	3.9	3.558	.032
4. Having conflict between family members (7-1)	3.0	3.8	4.2	1.984	.143
5. Formulation of specific Succession Plans (7-1)	3.8	4.5	4.3	.905	.408
6. Use of outside consultants, advisors, and professional services (7-1)	3.2	3.5	2.7	.751	.475
7. Time spent in strategic management activity (7-1)	4	4.2	4.25	.073	.930
8. Use of sophisticated methods of financial management (7-1)	2.9	2.9	2.5	.552	.578
9. Degree of influence by original business objective and methods of the founder (7-1)	5.4	5.1	3.75	3.542	.033
10. Consideration of going public	1.24	1.64	1.42	1.147	.322
11. Use of equity financing rather than debt (proportion)**	62/38	76/34	88/12	1.38	0.255

*Likert Scales- Mean of describes our firm 7 6 5 4 3 2 1 does not describe our firm.

**Chi-Square, not F Value.