FAMILY BUSINESS:

CONTROL AND CONCENTRATION IN EURO-AREA COMPANIES

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Abstract

Corporate governance architecture is central to the dynamics by which successful firms and economies improve their performance over time as well as relative to each other. We exploit an augmented version of the law of proportionate effect to estimate the impact of ownership structure on firm performance. Our results suggest that ownership concentration and family control are significant company growth determinants.

Introduction

This paper aims to combine the central topic of corporate ownership and control structure with the recent empirical research on growth determinants of firms, in line with the papers of Coluzzi et al. (2012) and Ferrando and Mulier (2013). Whereas the former studies the impact of financing constraints on growth for euro-area non-financial firms, the latter focuses on the effect of trade credit channel on growth. We exploit their econometric approach, which relies on an augmented version of the law of proportionate effect (LPE henceforth) as proposed by Goddard et al. (2002), however, we shift our focus from the effects of financial obstacles to those related to ownership and control structure on the performance of euro-area firms. Our study aims at shedding light on this topic since the literature to date has focused, to the best of our knowledge, on mapping the structure of ownership and control of firms, limiting the assessment of their impact on company performance.

Maury (2006) empirically examines how family-controlled firms perform in relation to firms with non-family controlling shareholders in western Europe. The results suggest that family control can lower an agency's problems between owners and managers, but also gives rise to conflicts between the family and minority shareholders. Furthermore, Pindado et al. (2012) shows that family control in western European corporations may be beneficial to minority shareholders.

Bianchi et al. (2010) and Di Donato and Tiscini (2009) provide an overview of the Italian corporate governance system. Like most European countries, it features a high concentration of direct ownership suggesting a limited degree of separation between ownership and control. These Italian firms are characterized by opaque relationships among companies that are often linked through extensive family cross-holdings, hampering the system's dynamism.

Analyzing a dataset of Finnish companies, Lappalainen and Niskanen (2009) find that managerial (venture capital funds) ownership decreases (increases) growth.

Furthermore, some studies have recently casted doubts on the belief that family firms underperform non-family firms.

In this context, we contribute to the existing literature by: (i) assessing the impact of ownership concentration on the performance of companies, (ii) estimating a previously uncovered relationship, between the effect of family control on a firm's performance depending on the degree of ownership concentration.

Data and Empirical Method

ORBIS-Bureau van Djik (BvD henceforth) database is the main source of information of the current work. We focus on companies located in the euro-area over the period 2006-2014.

We estimate a LPE model through a dynamic GMM (Blundell and Bover, 1998) with a governance dimension, due to three main reasons: the dynamic nature of added value growth, possible unobserved firm-specific effects, and endogeneity of the explanatory variables. The baseline specification is:

$$\text{growth}_{i,t}^{ta} = \beta_0 + \beta_1 \text{growth}_{i,t-1}^{ta} \qquad (1)$$
$$+ \beta_2 \text{growth}_{i,t-1}^{sales}$$
$$+ \beta_3 \text{bankloans}_{i,t-1}$$
$$+ \beta_4 \log(\text{size})_{i,t-1}$$
$$+ \beta_5 \log(\text{age})_{i,t-1}$$
$$+ \beta_6 OC_i + u_{it}$$

where the error term $u_{it} = \gamma_i + \gamma_t + \varepsilon_{i,t}$ consists, respectively, of an unobserved firm-specific component, a time component to filter out business cycle effects, and an idiosyncratic component. The dependent variable is the growth rate of (real) total assets ($growth^{ta}$). Specifically, one of the explanatory variable is the sum of short term and long term bank loans scaled by total sales ($bankloans$), since access to bank loans is an important driver of firm growth (Coluzzi et al., 2012). Furthermore, we add sales growth ($growth^{sales}$) to account for possible good economic performance, while log of total assets

(*log(size)*) and age (*log(age)*) ensure that any impact of the ownership type on growth is not driven by these variables. Two dimensions represent the governance and the control structure: the ownership concentration OC_i and family control $Family_i$. The former is measured by two distinct variables: a) *%owner_i*, a dummy equal 1 if the ultimate owner holds more than 50% of the stakes, and *independence_i*, an indicator built by the ORBIS-BvD that captures the degree of a company's independence regarding its shareholders, distinguishing the existence of four main groups (A-B-C-D) of firms with a descendant intensity of independence. We use the first category *A* as reference, and we aggregate *C* and *D*, since both implies full (direct or total) control. $Family_i$ is a dummy variable equal 1 if the ultimate owner is "one or more named individual or families". To check for the effect of family control, we estimate the following specification[1]:

$$growth_{i,t}^{ta} = \beta_0 + \beta_1 growth_{i,t-1}^{ta} \qquad (2)$$
$$+ \beta_2 growth_{i,t-1}^{sales}$$
$$+ \beta_3 bankloans_{i,t-1}$$
$$+ \beta_4 log(size)_{i,t-1}$$
$$+ \beta_5 log(age)_{i,t-1} + \beta_6 OC_i$$
$$+ \beta_7 Family_i + \beta_8 OC_i$$
$$* Family_i + u_{it}$$

Results

Table 1 shows the results for the dynamic GMM of specification 1 and 2, while Table 2 displays the same exercise within each country, confirming the estimated impact of ownership[2].

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[1] We estimate Specification 2 excluding the interaction of *independence* with *Family* since there are no observations when *A* and *Family* simultaneously equal 1.

[2] Results in Table 1 are obtained with (*t-2*) and further lags. We perform the within-country estimation with different set of instruments across countries. This confirms that the need of different lag structures might be due to the different growth dynamics within each country, and could explain the rejection of Hansen test in all country-estimation.

In line with Ferrando and Mulier (2013) we reject the LPE hypothesis of growth not depending on past performance, and we confirm the impact of size, age, firm opportunity and access to bank loans on a firm's growth.

We find that a high degree of ownership concentration (or a low degree of independence) has a negative effect on economic performance (with both ownership concentration variables, see Table 1 column 1 and 4). This supports the strand of literature assessing the possibility that shareholder's behavior comes at the expense of a firm's overall efficiency. Our results are confirmed also by all the within-in-country estimations, with the exception of Belgium and Finland (see Table 2), who are not sensitive to the choice of ownership concentration measure (see Table 1 column 4 and 5). In line with the literature, we found that in cases where the family is the ultimate owner, independently on a capital structure, they economically underperform relative to non-family companies (see Table 1 column 3).

However, these results are different when including the interaction between *%owner* and *Family*, as in Specification 2 (see Table 1 column 2): firstly, there are no significant differences between the performance of concentrated and dispersed owner-type firms. Its impact may be positive or negative, depending on the ownership structure, i.e. the type of ultimate owner.

Secondly, our results suggest that the involvement of the family as ultimate owners in management is detrimental to growth only if the family has more than 50% of ownership. This result has relevant implications: on the one side, when the ownership is not fragmented (i.e., *Family=1* and *%owner=1*), a strong and enduring family control can regulate ownership issues by restricting the trading of shares or paying relatively low dividends. The latter can be used to increase capital and add value without diluting family control. Furthermore, the too-close firm management may imply strategies that favor the family's objective, while the scarce legal protection of shareholders can generate internal conflicts. On the other, if the family is the ul-

timate owner but holds less than 50% of the stakes, that corresponds to fragmented ownership (*Family=1* and *%owner=0*), companies perform better. Indeed, the accountability of non-family relevant shareholders limits the previously mentioned self-advantages of family behavior, bringing the main feature of family firms to light, (i.e. a higher capacity of aligning owners and management objectives) despite the inter-generational risk of potential conflicts between family and business needs when the management passes from one generation to the next. Therefore, this kind of corporate governance architecture can favor economic performance reducing costs that stem from owner-management conflicts.

Conclusion

In this paper we apply a dynamic GMM in a LPE framework to investigate the effect of corporate ownership and control structure on growth dynamics of the euro-area's companies from 2006 to 2014. Our findings suggest that a high degree of ownership concentration (low independence) is detrimental to growth and that the family impact depends on the control structure, i.e., whether the family has more than 50% of the stakes.

Table 1: Results for All Countries

	(1)	(2)	(3)	(4)	(5)
$\textbf{growth}^{\textbf{ta}}_{\textbf{i,t}-1}$	-0.153**	-0.175***	-0.156**	-0.211**	-0.232**
	(0.0736)	(0.0661)	(0.0733)	(0.0920)	(0.0953)
%Owner$_i$	-3.702***	0.528	-3.524***		
	(0.385)	(0.977)	(0.379)		
IndependenceB$_i$				-7.006***	-16.46***
				(1.175)	(3.568)
IndependenceC/D$_i$				-2.927***	-13.19***
				(0.706)	(2.761)
Family$_i$		3.489***	-0.323*		-0.904**
		(0.899)	(0.169)		(0.413)
%Owner$_i$*Family$_i$		-4.373***			
		(1.029)			
$\textbf{growth}^{\textbf{sales}}_{\textbf{i,t}-1}$	0.154***	0.163***	0.159***	0.201***	0.239***
	(0.0399)	(0.0371)	(0.0397)	(0.0568)	(0.0613)
$\textbf{bankloans}_{\textbf{i,t}-1}$	0.0135***	0.0107**	0.0160***	0.0319***	0.0340***
	(0.005)	(0.005)	(0.005)	(0.00491)	(0.00452)
$\textbf{log(age)}_{\textbf{i,t}-1}$	-0.588***	-0.595***	-0.576***	-0.686***	-0.686***
	(0.0587)	(0.0551)	(0.0580)	(0.100)	(0.0931)
$\textbf{log(size)}_{\textbf{i,t}-1}$	-0.151***	-0.189***	-0.163***	-0.232***	-0.390***
	(0.0236)	(0.0245)	(0.0240)	(0.0688)	(0.0715)
N	234,930	234,930	234,930	347,948	291,761
Number of firms	44,022	44,022	44,022	64,836	54,614
AR(2)	0.785	0.990	0.792	0.770	0.731
J	0.000	0.000	0.000	0.000	0.000

Notes: The estimates are robust to heteroscedastic standard errors. All specifications were estimated with time dummies. J and AR(2) are p-values of the Hansen test and serial correlation in the error terms respectively. Column (1) and (4) displays results for specification 1, while (2), (3) and (5) for specification 2. Standard errors in parentheses. *** p<0.01, ** p<0.05, * p<0.1

Table 2: Results by country

	(1) Belgium	(2) Germany	(3) France	(4) Spain	(5) Portugal	(6) Italy	(7) Finland
$\text{growth}_{i,t-1}^{ta}$	-0.337***	-0.294***	-0.373***	-0.184***	-0.176***	-0.396**	-0.203**
	(0.107)	(0.0405)	(0.116)	(0.0108)	(0.0175)	(0.162)	(0.0975)
%Owner	0.333	-1.040**	-1.393*	-5.434***	-2.828**	-2.717***	0.0358
	(0.331)	(0.509)	(0.804)	(1.352)	(1.338)	(0.993)	(0.182)
$\text{growth}_{i,t-1}^{sales}$	0.139**	0.201***	0.534**	0.114***	0.0737***	0.365*	0.275**
	(0.0607)	(0.0511)	(0.252)	(0.00936)	(0.0172)	(0.197)	(0.136)
$\text{bankloans}_{i,t-1}$	0.0288***	0.0509***	0.0144*	0.0681***	0.0457***	0.00741	0.0404***
	(0.0101)	(0.0163)	(0.00807)	(0.0153)	(0.0170)	(0.00660)	(0.0134)
$\log(\text{age})_{i,t-1}$	-0.500*	-0.420**	-0.613***	-0.583**	-0.743***	-0.447***	-0.187*
	(0.258)	(0.212)	(0.223)	(0.270)	(0.169)	(0.136)	(0.105)
$\log(\text{size})_{i,t-1}$	-0.0350	-0.230*	0.00143	0.155	-0.163***	-0.141***	0.00414
	(0.0526)	(0.128)	(0.0482)	(0.111)	(0.0578)	(0.0544)	(0.0214)
N	4,929	5,853	12,642	104,006	28,147	76,634	2,719
Number of firms	853	1,053	2,232	19,473	5,118	14,809	484
AR(2)	0.138	0.153	0.433	0.132	0.794	0.192	0.505
J	0.172	0.603	0.130	0.378	0.000	0.413	0.475

Notes: The estimates are robust to heteroscedastic standard errors. All specifications were estimated with time dummies. J and AR(2) are p-values of the Hansen test and serial correlation in the error terms respectively. Standard errors in parentheses. *** $p<0.01$, ** $p<0.05$, * $p<0.1$

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