APPLYING AGENCY THEORY AND THE RESOURCE-BASED VIEW IN EXPLAINING PERFORMANCE DIFFERENCES BETWEEN FAMILY AND NON-FAMILY BUSINESSES

Uporaba agencijske teorije in teorije proizvodnih virov pri razlagi razlik v uspešnosti med družinskimi in nedružinskimi podjetji

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1 Introduction

Family businesses are an important part of the national economies of many countries (Mandl 2008), including Slovenia (Duh and Tominc 2006). Many authors (e.g., Habbershon et al. 2003) suggest that, in family-influenced firms, the interaction of the family unit, the business entity, and individual family members create unique systemic conditions and constituencies that impact the performance outcomes of the family business. In their comparative study, Daily and Dollinger (1992) found that family-owned and -managed firms do appear to achieve performance advantages over professionally run firms, whether performance is measured in terms of financially oriented growth rates or perceived measures of performance. In contrast to these findings, Chrisman, Chua and Litz (2004) found that family and non-family firms had similar economic performance as measured by short-term sales growth; similarly Duh and Tominc (2006) found no statistically significant differences in performance (measured by economic efficiency and value added per employee) between Slovenian family and non-family enterprises. An analysis of various other studies examining the performance (using different performance measures) of family firms versus non-family firms (Dyer 2006) indicates the existence of mixed results and conflicting opinions regarding the impact of family control on performance.

The current paper examines the applicability of different theoretical approaches for explaining and studying performance differences between family and non-family businesses. We limit our research to the agency theory and the resource-based view of the firm, which have recently received most of the attention in theoretical as well as empirical family business studies (e.g., Chrisman et al. 2004; Dyer 2006; Habbershon et al. 1999; Schulze et al. 2001; Sirmon and Hitt 2003). Therefore, the main research question is: What are the possible limitations of the agency theory and the resource-based view applied in explaining how and why family businesses behave, consequently performing differently than non-family businesses? The main objectives of the research are to analyse potential limitations of the agency theory and resource-based view in establishing family businesses' performance differences and propose implications of the theories studied for research on family business performance in order to improve our understanding of factors affecting family businesses performance. Performance in the context of this paper is defined broadly to refer to efficiencies in terms of the utilisation of resources as well as the accomplishments of organisational goals (e.g., Dyer 2006).

We argue that our research is important for at least two reasons. First, there are many conflicting findings have emerged regarding family businesses' performance differences in comparison to non-family businesses. Possible reasons for such conclusions are the different theoretical as well as methodological appro-

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Abstract

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This paper examines the applicability of different theoretical approaches in studying and explaining performance differences between family and non-family businesses. The main objective of the contribution is to analyse potential limitation of applied theories and make proposals regarding the implication of these theories in research on family business performance. We limit our research to agency theory and the resource-based view of the firm, which have recently received most of the attention in theoretical as well as empirical family business studies.

Key words: family business, agency theory, resource-based view, performance

Izvleček

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V prispevku raziskujemo uporabnost različnih teoretičnih pristopov k razlagi in proučevanju razlik v uspešnosti med družinskimi in nedružinskimi podjetji. Cilj raziskave je proučitev različnih teorij in oblikovanje predlogov za njihovo uporabo v raziskovanju uspešnosti družinskih podjetij. Raziskavo smo omejili na agencijsko teorijo in teorijo proizvodnih virov, ki sta v zadnjem času pogosto uporabljeni v teoretičnih in empiričnih študijah uspešnosti družinskih podjetij.

Ključne besede: družinsko podjetje, agencijska teorija, teorija proizvodnih virov, uspešnost

JEL Classification: D01, L25

aches employed (Dyer 2006), the lack of consensus surrounding the definition of a family firm, the exploration of family firms' characteristics and performance in isolation rather than in comparative studies, and the limited number of comparative studies that appreciate the impact of not controlling for demographic sample differences in research results (Westhead and Cowling 1997). Second, the findings of studies that would succeed in identifying factors affecting the family business performance and unique to family businesses are of great importance for owners and managers of family businesses. In today's turbulent and complex marketplace, it is difficult to achieve strategic competitiveness. These difficulties are compounded when leaders do not have a clear understanding of what affects a firm's performance. Research findings would also be of great importance for policy makers and creators of a supportive entrepreneurial infrastructure for family businesses.

The paper is structured as follows. The second chapter addresses the problem of defining a family business while the third chapter provides an overview of studies on family businesses' performance differences, emphasising agency theory and the resource-based view. In the subsequent three chapters, the agency theory (fourth chapter), the resource-based view (fifth chapter), and a combination of both theories (sixth chapter) are discussed. The paper concludes with a discussion of the applicability of theoretical approaches and proposals for future research studies.

2 Problems in defining a family business

Family businesses differ from non-family ones along important strategic and organisational dimensions. As the term *family business* implies, the most important differences have something to do with how a family influences the behaviour of a firm (Steier and Ward 2006). A family business has no commonly accepted definition (e.g., Mandl 2008; Sharma 2004). Numerous attempts have been made to articulate conceptual and operational definitions of a family enterprise; such efforts have also led to questions about the homogeneity of these enterprises. Empirical research has revealed that family enterprises vary in terms of the degree of family involvement (Westhead and Cowling 1998; Astrachan et al. 2002; Sharma, 2004). Attempts to capture the varying extent and mode of family involvement in enterprises have been directed in three general directions (Sharma 2004): articulation of multiple operational definitions of family enterprises (e.g., Westhead and Cowling 1998), development of scales to capture various types of family involvement (e.g., Astrachan et al. 2002) and the development of family firm typologies (e.g., Sharma 2002). One argument supporting the use of several definitions is that different configurations of family enterprises can be studied.

In the majority of definitions proposed, different combinations of the components of the family's involvement in the business are used—namely, ownership, governance, management, and generational succession. According to Chrisman, Chua and Sharma (2005), these definitions lack a theoretical basis for explaining why family involvement in a business leads to behaviours and outcomes that might be expected to differ from non-family businesses. The authors describe such an approach to defining a family firm as the components-of-involvement approach, proposing the more adequate essence approach (Chrisman et al. 2005), which is "… based on belief that family involvement is only a necessary condition; family involvement must be directed toward behaviors that produce certain distinctiveness before it can be considered a family firm.' In other words, two firms with the same extent of family involvement may not be family businesses if either lacks the intention, vision, familiness, and/or behaviour that constitutes the essence of a family business.

This short overview of family businesses' definitional approaches indicates that many questions remain regarding the definition of a family business. Achieving clarity in regard to the definition of a family enterprise may appear useless. However, the implications of such a conclusion are potentially problematic from a methodological perspective. As Handler (1989) pointed out, the lack of clear criteria for distinguishing family enterprises from other types of business makes research sampling very difficult. Thus, in this theoretical paper, a family business is understood in the context of the essence approach to defining a family business.

3 Overview of studies and underlying theories used in explaining family versus non-family businesses' performance differences

A number of scholars have attempted to compare the performance of family businesses with non-family businesses using various theoretical approaches to establish differences. Table 1 presents only those recent studies that used the agency theory or the resource-based view (RBV) as an underlying theory when investigating the performance of family businesses to compare it to non-family ones.

As Table 1 indicates, of the ten studies, five are based on agency theory, three on the RBV, one of the studies combines the agency theory and the RBV, and one applies the agency theory and the stewardship theory to explore the effects of the family on the firm's performance. Four of the ten studies are theoretical, while six contribute some empirical support. Research findings/results indicate the complexity of the researched phenomenon. In the continuation of the current paper, we discuss the applicability of the agency theory and the RBV in the studies of family versus non-family businesses' performance differences.

4 The agency theory

Traditionally, agency theory is employed to explore the relationship between a firm's ownership and management structure and its financial performance. Where a separation of ownership and control exist, agency control mechanisms are put in place to align the goals of managers (agents) with those of owners (principals). Agency costs represent the costs of all activities and operating systems designed to align the interests and/or actions of managers with the interests of owners. Family involvement in a business has the potential to both increase and decrease financial performance due to agency costs (Chrisman et al. 2004).

Given their family involvement in firm ownership and management, family firms may significantly reduce agency costs and potentially enhance firm performance because the goals of the firm's principals are aligned with its agents since they are typically one and the same (Chrisman et al. 2004; Dyer 2006); consequently, less monitoring of owners' agents is needed. Lower agency costs in family firms could be due to high trust and shared values among family members (Dyer 2006). In addition, those family firms that have some objective standards for monitoring the performance of family managers and are willing to enforce discipline may realise the advantage of lower monitoring costs (Dyer 2003).

On the other hand, family firms may incur significant agency costs due to the conflicts that accompany family involvement. Family members may have competing goals and values; different views within the family about the distribution of ownership, compensation, risk, roles, and responsibilities may lead to competition among family members (Dyer 2006). Governance arrangements of family firms need not remove nor even reduce agency costs due to altruism, which makes it difficult or even impossible for families to effectively monitor family members who work in the firm (Schulze et al. 2001; Schulze et al. 2003). Altruism—treating people for who they are rather than what they do—is often seen as the cornerstone value in family firms. Schulze and co-authors (2001) argue that altruism can cause parents to threaten their children with moral hazards, meaning that altruism on the part of parents undermines effective monitoring: "Because altruism partly stems from parents' desire to enhance their own welfare, parents have incentive to be generous even though that increased generosity may cause their children to free-ride … This agency threat is likely to be pronounced in family firms, because control over the firm's resources makes it possible for owner-managers to be unusually generous to their children and relatives … Altruism therefore adds a theoretically distinct set of self-control problems to the set of agency problems." Such altruism takes place in other familial relationships as well, such as those between siblings (Dyer 2003). Greenwood (2003) believes that the idea of altruism expands many of the problems family businesses face; arranging them into an analytical framework enables the assessment of their effects on performance. These problems are often accepted as characteristic of family firms; for example,

Table 1: *Studies examining family versus non-family businesses' performance differences*

Author(s) in alphabetic order	Underlying theory	Main results/findings	Empirical support
Chrisman, Chua and Litz (2004)	Agency theory	Family and non-family firms have similar economic performance measured by short-term sales growth. Strategic planning has greater positive impact on performance of non-family firms. Both findings suggest that family involvement may decrease overall agency problems.	Yes
Dyer (2006)	Agency theory and resource-based view (RBV)	Typology of family firms, based on agency costs, family assets, and family liabilities, providing a foundation for theorising regarding family firm performance.	No
Gomez-Mejia, Nuñez-Nickel and Guiterrez (2001)	Agency theory	Families are reluctant to strictly monitor, discipline, or fire family CEOs because they are family members. When family CEOs are replaced, the firm's performance improves significantly; such changes in command do not have any effect in non-family firms.	Yes
Habbershon and Williams (1999)	RBV	The bundle of resources that are distinctive to a firm as a result of family involvement is identified as the "familiness" of the firm. The familiness bundle of resources needs to be managed and maintained if it is to provide a competitive advantage.	No
Habbershon, Williams and MacMillan (2003)	RBV	Wealth-creating performance for family-influenced firms is a function of the 'distinctive familiness" generated by the family business system.	No
Karra, Tracey and Phillips (2006)	Agency theory	Altruism reduces agency costs in the early stages of the family business, but the agency problems increase when the business becomes larger and more established.	Yes.
Schulze, Lubatkin, Dino and Buchholtz (2001)	Agency theory	In privately held, family-managed firms, agency problems are more pronounced due to self-control and other agency threats engendered by altruism. Those family firms that adopt some internal governance mechanisms perform more effectively than those firms without such mechanisms.	Yes
Schulze, Lubatkin and Dino (2003)	Agency theory	Agency relationships in family firms are distinctive because they are embedded in the parent-child relationship found in the household and are characterised by altruism. These agency problems cannot be controlled easily with economic incentives; consequently, they may be more difficult to resolve than the agency problems facing non-family firms.	Yes
Sirmon and Hitt (2003)	RBV	The most important resource to a family firm is its human capital (e.g., knowledge); intangible resources are socially complex and difficult to imitate and therefore lead to competitive advantages.	No
Westhead and Howorth (2006)	Agency theory and stewardship theory	Firms associated with high levels of family ownership and management are not significantly associated with weaker firm performance. Family firms' ownership and management structures are associated with a focus on specific non-financial objectives.	Yes

family members may not be the best qualified for positions to which they have the inside track, family members make shirk their work responsibilities or get a free rise because they aware that discipline is not forthcoming, and owners may be unwilling to relinquish control even though they are no longer capable of effective management.

Some authors (e.g., Westhead and Howorth 2006) suggest that agency theory may not apply to closely held and managed family firms associated with little outside influence or representation, where the firm's objectives are entangled with family objectives. To protect "family agendas," family owners and managers may focus on non-financial objectives, which may ultimately retard the firm's financial performance. There may also be diminished economic performance but no agency cost if owners wish to divert resources to pursue non-economic goals and managers conform to such wishes (Chrisman et al. 2004).

5 The resource-based view

In the field of strategic management, RBV has been successfully used to explain long-term differences in firm performance that cannot be attributed to industry or economic conditions. Because family firms have been described as unusually complex, dynamic, and rich in intangible resources (e.g., Habbershon and Williams 1999), RBV gives family business researchers an appropriate means by which to analyse family/non-family business performance differences.

RBV asserts that firms are heterogeneous and that it is the idiosyncratic, immobile, inimitable, and sometimes intangible bundle of resources residing in the firm that gives the firm the opportunity for a competitive advantage and superior performance. RBV examines the links between a firm's internal characteristics and processes and its performance outcomes (Habbershon and Williams 1999; Chrisman et al. 2005). Sirmon and Hitt (2003) argue that family firms evaluate, acquire, shed, bundle, and leverage their resources in ways that differ from those of non-family firms. They believe these differences allow family firms to develop a competitive advantage. According to Dyer (2006), three types of capital (or assets)—defined as "family factors"—have been associated with the performance of family firms: human capital, social capital, and physical/financial capital. Certain family factors can lead to important assets and contribute to high performance, while other family factors are liabilities to firm performance and contribute to lower performance.

Based on some other cognitions (e.g., Barney 1991), Habbershon and Williams (1999) suggest the division of firm resources into four categories: physical capital resources (plant, raw materials, location, cash, access to capital, intellectual property), human capital resources (skills, knowledge, training, relationships), organisational capital resources (competencies, controls, policies, culture, information, technology), and process capital resources (knowledge, skills, disposition, and commitment to communication, leadership, and the team). According to the authors (Habbershon and Willimas 1999; Habbershon et al. 2003), the systemic influences generated by the interaction of the subsystems (family unit, business entity, and individual family members) create an idiosyncratic pool of resources and capabilities. These resources and capabilities have deeply embedded defining characteristics that the authors refer to as the "family factor" (*f* factor) and connote as resources$_f$ and capabilities$_f$. Any of the resources and capabilities that could be associated with a given firm might have an *f* factor influence, either positive or negative. The positive *f* factor influences are defined as "distinctive" and hold the potential to provide an advantage; the negative *f* factor influences are defined as "constrictive" and hold the potential to constrain competitiveness. Habbershon et al. (2003) define the "familiness" of the firm as the summation of the resources$_f$ and capabilities$_f$ in a given firm. This idiosyncratic familiness bundle of resources and capabilities provides a potential differentiator for firm performance and explains the nature of family influence on performance outcomes. It is "distinctive familiness" that holds the potential for providing firms with competitive advantage (advantages$_f$); the rent-generating performance for family businesses is a function of those advantages$_f$ that stem from distinctive familiness of a particular firm. Wealth creation is thus tied to the systemic influences in the system as they create an idiosyncratic bundle of distinctive resources for the firm.

Chrisman, Chua and Litz (2003) extended this concept to incorporate the substitution of value creation for wealth creation as the ultimate goal, adding non-economic benefits as a co-determinant of value creation. The authors argue that wealth creation is not necessarily the only or even primary goal of all family firms. Therefore, recognising and allowing for the possibility that family firms seek to achieve a variety of goals can make the concept developed by Habbershon and co-authors (2003) more widely acceptable.

6 Applying the agency theory and RBV in developing a family typology to explain "family effect" on firm performance

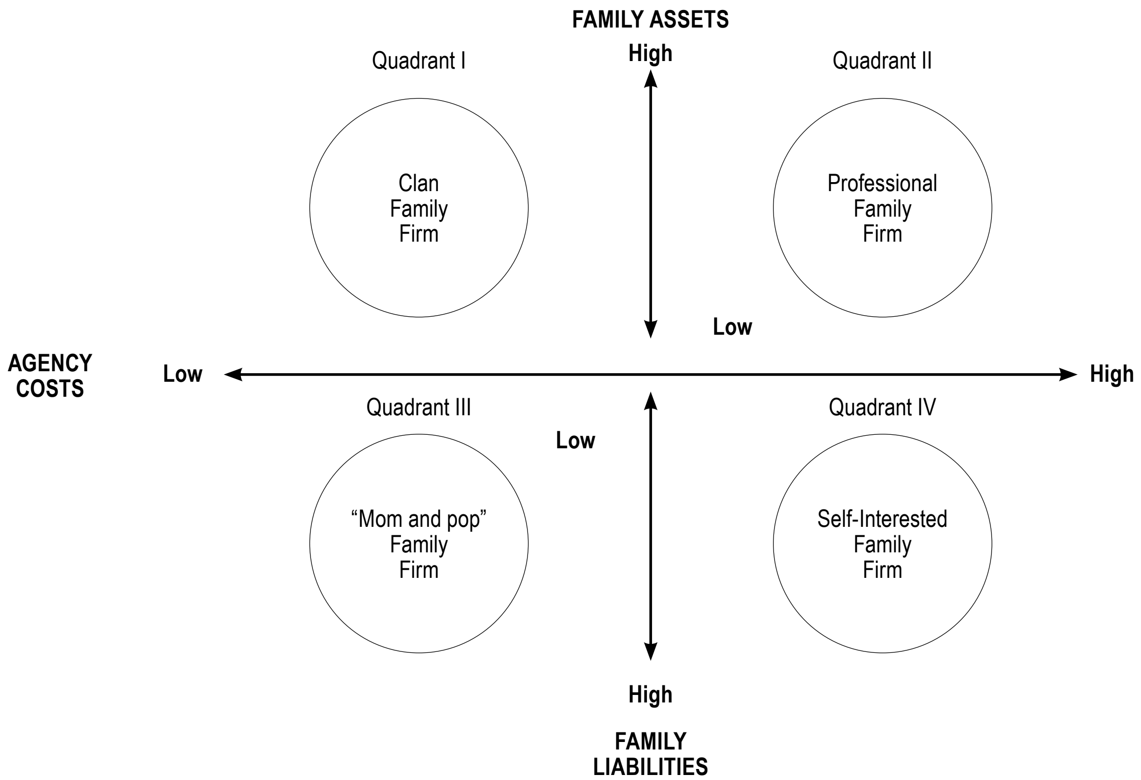
When researchers compare a sample of family firms versus a sample of non-family firms, they are likely to obtain a cross-section of the various family firm types in the sample. To the extent that the family firm sample contains a disproportionate number of any particular type, the results may be misleading. According to Dyer (2006), the right question for researches should be: What type of family firms leads to high performance? The author proposes four types of family businesses using the agency theory and RBV in the context of explaining family businesses; performance.

Figure 1 represents three dimensions—agency costs, family assets, and family liabilities, ranging from high to low—used to distinguish among various types of family firms. These three dimensions create four quadrants, suggesting four types of family firms (Dyer, 2006): (I) the clan family firm, (II) the professional family firm, (III) the "mom and pop" family firm, and (IV) the self-interested family firm. Certain agency costs and familial assets or familial liabilities are associated with each type. An example of the clan family firm (I) may be a small, first-generation family firm owned and managed by family members highly committed to the success of both the firm and the family. The benefits of low agency costs stem from the "clan control"; such clans have a high degree of trust, and behaviour is regulated by the group's shared goals, norms, and values. This type of a family firm relies on significant human capital (i.e., family members with skills and commitment needed for firm success). Family resources are also used to support the firm in difficult times.

Large family firms in which the family maintains significant ownership but relies on professional managers to run the enterprise are examples of professional family firms (II). Agency costs stem from the attempt to formalise control systems and monitor management. On the other hand, the formal monitoring mechanisms prevent the firm from opportunism and nepotism often found in family firms. Therefore, family assets are protected and can be developed in the professional family firm, much like in the clan family firm. The "mom and pop" family firms (III) are those family firms that may have been operated by a family for generations, but the owning family has not made an effort to cultivate family assets to help the firm to grow (e.g., family-owned restaurants or family farms). This type of family firm has the agency advantages of the clan family firm, inasmuch as the family does not have conflicting goals and behaviour is monitored largely through close family ties. However, this type of firm has certain liabilities stemming from family ownership. Family managers may not be trained or have the expertise needed to grow the business, especially if family values encourage nepotism. The family's physical or financial assets may not be utilised effectively to benefit the business. Finally, family firms comprised of multiple generations of family members that are often highly conflicted are examples of self-interested family firms (IV). Self-interested family firms are based on utilitarian and altruistic relationships; family members advance their self-interests at the expense of the firm and often other family members. Family assets may be squandered through opportunism, shirked responsibilities, and adverse selection—all of which are made possible by the lack of formal monitoring systems and self-interested nature of the family. Family ownership may be widely dispersed among family members who have different interests and goals; these differences may cause conflicts and self-interested behaviours (Dyer 2006).

Dyer (2006) developed several propositions regarding family as well as family/non-family businesses performance differences based on the types presented herein; the propositions are based on the ceteris paribus assumption, which means that the family effect on performance can be clearly delineated only by assuming that all other firm factors are

Figure 1: *Typology of family firms*



Source: Dyer (2006, 266)

held constant (e.g., industry, firm characteristics). One proposition stated that clan family firms will, due to significant family assets and low agency costs, perform better than the other three types of family firms. Another proposition is that professional family firms will have higher performance than self-interested family firms. Regarding performance differences between family/non-family firms, Dyer (2006) stated that non-family firms would be expected to perform more poorly than clan family firms (since non-family firms lack family resources and have higher monitoring costs) and professional family firms (since non-family firms have no familial resources and incur similar agency costs) but perform better than self-interested family firms since this type of family firms has significant agency costs and family liabilities.

7 Conclusions on applicability of theoretical approaches and proposals for future research studies

Explaining how and why family firms behave and perform differently than non-family firms has become the objective of many recent research studies, indicating that the study of family firm performance is becoming central in the family business study field (e.g., Sciascia and Mazzola 2008). Both the agency theory and RBV provide a useful framework for guiding theoretical as well as empirical studies on family firms' performance. Habbershon and co-authors (2003) made an important contribution in investigating the effects of family involvement by integrating firms' RBV with the system theory. The authors provided a theoretical basis for explaining how family businesses are different from non-family ones and how such differences might manifest in sustainable competitive advantages. Meanwhile, Dyer's (2006) work on family firm typology combined two theoretical approaches: the agency theory and RBV, whose practical value should be proved by empirical studies. The author considered the heterogeneity of the family business sector (e.g., Westhead and Cowling 1998; Astrachan et al. 2002; Sharma 2004), which is often neglected in empirical research. However, limits exist in the usefulness of a typology of anything as complex as family enterprises.

It is important that future studies based on the agency theory and RBV try to clearly differentiate the family influence from other variables (e.g., industry, firm characteristics, the firm's stage of development) that may influence firm performance; researchers should explore the "family effect" (Dyer 2006) or "familiness" (Habbershon et al. 2003)—namely, those attributes that a family brings to a firm that might affect its performance. Such approaches to studies will help better understand the determinants of family firm performance as well as provide policymakers and those concerned with encouraging wealth creation and job generation by providing empirical evidence of factors that have a negative (detrimental) or positive influence on firm performance.

Definitional clarity is also of great importance in the field of family business performance research. As pointed out herein, many divergent conclusions regarding the performance of family firms stemming from empirical research studies could be due to the lack of consensus surrounding the definition of a family firm. Such lack of clarity can lead to conflicting evidence surrounding performance and create a serious credibility gap, leaving the field of family business open to criticism from academics and business professionals. Therefore, researchers must clearly define the "group" of family businesses they research.

When establishing differences in performance, it is necessary to test for differences caused by family involvement in management and for those differences caused by family involvement in ownership. Empirical testing is needed to determine which type of agency costs (e.g., other than agency costs arising from separation of ownership and control, including those arising from asymmetric altruism) has the most detrimental impact on family firms' performance and to examine whether agency costs are more apparent in certain types (or groups) of family firms. Such testing would also bring some empirical support for Dyer's (2006) typology. Different internal governance mechanisms (e.g., strategic planning, executive pay, outside directors) and their influence on agency costs, and consequently on family business performance, should be studied as well. Empirical research is also needed to test the propositions on the links between performance and the idiosyncratic resources and capabilities that family firms possess. Future studies should ultimately be oriented toward differences in the combination and importance of the various resources and capabilities that constitute familiness, depending on the mix and importance of goals pursued.

Researchers should consider the limitations of agency theory in its explanatory scope since the economically self-interested actor of agency theory may not be the best portrayal of actors in family firms, where cultural norms may play a significant role (e.g., Greenwood 2003; Westhead and Howorth 2006). Therefore, other complementary theories should be considered in future research in order to provide a broader framework with which to explore the links between a family firm's ownership and management structure and firm performance. In particular, stewardship theory—which has recently gained much attention among family business researchers (e.g., Corbetta and Salvato 2004; Westhead and Howorth 2006; Greenwood 2003)—explicitly denies the narrow economic definition of human action and proposes that actors often identify themselves with a company and knowingly subjugate personal interests to the collective (Davis et al. 1997). Stewardship theory may provide greater insights (in comparison to agency theory) into ownership and management and its impact on performance of closely held and managed family firms that may exhibit an organisation-serving culture and focus on non-financial objectives. Such behaviour may retard firms' financial performance

(Westhead and Howorth 2006). These cognitions are especially important for studying Slovenian family businesses as well as family businesses in CEE transition countries since the majority of them can be described as "founder centric family businesses" (Duh and Tominc 2006) characterised by ownership concentrated in one individual who is also a manager.

The performance of family businesses (also versus non-family businesses) should be explored using "hard" performance measures as well as indicators of non-financial objectives/performance since profit maximisation is not the only (or prime) objective of a family business (e.g., Westhead and Cowling 1997; Westhead and Howorth 2006; Chrisman et al. 2003). Corbetta and Salvato (2004) also suggested that advantages related to family involvement should be measured over long periods given the long-term orientation of most family firms, since the main determinants of stewardship behaviours (trust, altruism, relational contracts, and non-financial family goals) take a relatively long time to exert their effects on firm performance.

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