An Empirical Study on the Succession Performance of Family Business

Yanshuang LI *

School of Economics and Management, Hebei University of Technology, Tianjin, China

KEYWORDS
Family business, Succession plan, Succession performance, Family performance, Business performance

ABSTRACT
The succession performance discussed in this paper is measured by two constructs: family performance and business performance. The succession plan is divided into five aspects: formalization degree of succession plan; successor selection and training; process control; retirement plan and business strategy after succession. A total of 308 questionnaires were sent to family businesses in Zhejiang Province and 258 companies responded, of which 219 are valid. Research results based on SPSS and LISREL analyses indicate that 7 out of 10 proposed hypothesis are supported.

1 Introduction

Statistics in the literature show that the average longevity of family business in western countries is about 24 years, that more than one third of the family businesses are successfully passed on the ownership to the second generation, and that less than ten percent family businesses pass their businesses to the third generation (Astrachen and Allen, 2003). According to a survey executed by China Democratic National Construction Association in 2010, the average longevity of small and medium companies, most of which are family controlled, is only three-five years. Gersick (1997) concluded that the reason for the high failure rate of intergenerational transition is lack of succession plan. In China, 52% of family businesses never consider succession issues and only 19% of the businesses have timely selected successors and offer training, whereas in the US 93% of family businesses have their own strategic succession plan. In China, the establishment and development of family businesses strongly depend on founder’s knowledge and expertise, social relationships, and leadership endeavour. Due to the unavailability of succession plan, if the founder is involved in any urgency or passes away, significant adjustments would occur to the leadership and ownership of the family business. Conflicts may break out between descendants, causing problems for the business survival. Sometimes the business has to liquidate itself or sell it off in the market. Therefore, outlining a succession plan in Chinese family businesses becomes essential. This paper aims to find out factors influencing succession plan, and explore the relationship between succession plan and family business performance.

* Corresponding author.
E-mail address: lilicathy@163.com
2 Succession Plan and Succession Performance

2.1 Succession plan

Many scholars (Ward, 1987; Babicky G, 1987; Wang, et al., 2004; Sharma, et al., 2003) have emphasized the importance of succession plan for the success of succession, and presented four regulations of formulating the succession plan: distinguishing the succession plan and the replacement program, determining the effectiveness of staff from the behaviour perspective, understanding the limitations of the unique skills, and designing the pragmatic and visionary process. Sharma (2004) indicate that the role of the founder after retirement should also be considered. Parmodiat, Chua, Chrisman & Sharma (2003) divided the succession plan into following dimensions: degree of formality, selection criteria, resource allocation, and process control.

Based on the above discussion, we divide the succession plan into five aspects: the formalization degree of succession plan, successor selection and training, process control, the development strategy after succession, and the retirement plan of the founder.

2.2 Succession performance of family business

Family business is one of the most unique, complex and dynamic entity in the society, since it combines two completely different systems: family and business. The business system is often performance-oriented and the family system is often full of emotion. Therefore the mixture of the two systems often causes confusion and conflicts. Each system has its own priority objectives and complex driving factors. Family system relies on blood relations and feelings to maintain, while business system needs to be constrained by the relevant norms and rules (Wang and Ahmed, 2010).

According to the above analysis, we divide the succession performance of family business into family performance and business performance. Family performance is mainly measured from the special resources, family relationship, family income, family status, family members’ target and achievements. A total of 12 questions using Likert 5 point scale to measure; There are 10 indicators to measure business performance, such as innovation capability, market share, profitability, stakeholders’ satisfaction and so on, all the questions used Likert 5 point scale to measure.

3 The Presentation of Hypothesis and the Structure of the Model

Base on the five aspects of succession plan and the two systems of family and business performance, this paper presents the following hypothesis:

H1a: The formalization degree of succession plan and family performance are positively related;
H1b: The formalization degree of succession plan and business performance are positively related.
H2a: The successor selection, training plan are positively related with family performance;
H2b: The successor selection, training plan are positively related with business performance.
H3a: Process control level and family performance are positively related;
H3b: Process control level and Business performance are positively related.
H4a: The development strategy after succession and family performance are positively related;
H4b: The development strategy after succession and business performance is positively related.
H5a: The retirement plan of founder and family performance are positively related;
H5b: The retirement plan of founder and business performance is positively related.

4 Empirical Analysis

In this research, 308 questionnaires were distributed face to face to the family business in Zhejiang province in China. 258 responses were received and the response rate is 83.8%. By carefully screening of the replied questionnaires and removing the questionnaires that do not meet the requirements obviously, we obtain 219 valid questionnaires, and the effective rate is 84.9%. The persons who compiled this questionnaire include former head officers, successors, business leaders and senior managers of family business.

4.1 Reliability and validity test of the questionnaire

By calculating the Cronbach coefficient of internal consistency, we find that both the succession plan and the succession performance have higher reliability in the questionnaire. The overall Cronbach’s Alpha of the reliability testing of succession plan and succession performance is 0.914, 0.965, this means that the internal structure of the questionnaire is good and should be retained.

To test the validity of the questionnaire, we use the exploratory factor analysis method. Firstly, we test the correlation among variables by KMO and Bartlett's spherical test, the result shows that the data is suit for factor analysis. Secondly, we use principal component and max-variance rotation method to make the exploratory factor analysis, and eventually we get 7 factors that can explain 71.898% of the variation.
4.2 Model analysis

The precondition of using SEM (Structural Equation Model) is that the data variables must be normally distributed. Hence, we calculate the skew values and the kurtosis values of the observed variables. The results show that skew values are less than 3, and the largest of the kurtosis values is 1.452, totally meet the criterion of normally distribution. By running LISREL8.7 statistical software, we make the first-order and second-order factor analysis of the succession plan model, the fitting indexes and values in the second-order factor analysis of succession plan factors is shown as Table I. Table I shows that the structure of succession plan factors is reasonable and can be used in the subsequent studies.

<table>
<thead>
<tr>
<th>Index</th>
<th>χ²/df</th>
<th>RMSEA</th>
<th>GFI</th>
<th>AGFI</th>
<th>NFI</th>
<th>NNFI</th>
<th>CFI</th>
<th>IFI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>1.658</td>
<td>0.065</td>
<td>0.94</td>
<td>0.91</td>
<td>0.95</td>
<td>0.89</td>
<td>0.93</td>
<td>0.85</td>
</tr>
</tbody>
</table>

Using the same method, we get the results that the structure of succession performance is reasonable and can be used in the subsequent studies.

Table II Fitting measurement of the model of succession plan (second-order)

Table II Succession plan factors, T values and hypothesis verification

<table>
<thead>
<tr>
<th>Path</th>
<th>T value</th>
<th>Hypothesis confirmation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Formalization ---&gt; family performance</td>
<td>1.21</td>
<td><strong>H1a is not supported</strong></td>
</tr>
<tr>
<td>Formalization ---&gt; business performance</td>
<td>2.15</td>
<td><strong>H1b is supported</strong></td>
</tr>
<tr>
<td>Successor selection and training ---&gt; family performance</td>
<td>3.24</td>
<td><strong>H2a is supported</strong></td>
</tr>
<tr>
<td>Successor selection and training ---&gt; business performance</td>
<td>4.12</td>
<td><strong>H2b is supported</strong></td>
</tr>
<tr>
<td>Process control ---&gt; family performance</td>
<td>3.24</td>
<td><strong>H3a is supported</strong></td>
</tr>
<tr>
<td>Process control ---&gt; business performance</td>
<td>4.23</td>
<td><strong>H3b is supported</strong></td>
</tr>
<tr>
<td>Development strategy after succession ---&gt; family performance</td>
<td>1.48</td>
<td><strong>H4a is not supported</strong></td>
</tr>
<tr>
<td>Development strategy after succession ---&gt; business performance</td>
<td>4.92</td>
<td><strong>H4b is supported</strong></td>
</tr>
<tr>
<td>Retirement plan ---&gt; family performance</td>
<td>3.12</td>
<td><strong>H5a is supported</strong></td>
</tr>
<tr>
<td>Retirement plan ---&gt; business performance</td>
<td>1.02</td>
<td><strong>H5b is not supported</strong></td>
</tr>
</tbody>
</table>

Note: When |T| ≥ 1.96, *p<0.05, it shows at 5% significantly related; when |T| ≥ 2.576, **p<0.01, it shows at 1% significantly related; when |T| ≥ 3.25, ***p<0.001, it shows at 0.1% significantly related.

5 Conclusion

By using LISREL8.7, we test the conceptual model of family business succession plan factors and succession performance factors, and supported or denied the hypothesis presented in the paper. The results show that the successor selection and training and the process control has significant positive impact on both family performance and business performance, while the retirement plan has significant impact on family performance but not on business performance. The reason may be that family members care more about the life arrangements of the founder after the retirement, and the activities of the retired founder will affect the family performance. The results that formalization and development strategy after succession do not influence family performance may be due to two reasons: one is that the family members are all familiar with the succession plan, though it is not a formalized one; the other is that the benefits of family members may have been assured before the succession, so there are not too many conflicts between the family and the business.

Succession plan is often used as a tool to help family business achieve inter-generational transmission in western countries. However, to the majority family businesses in China, succession plan has not yet been universal, experts who are able to carry out business consulting in this area are rare. Hence, it is necessary to make future research on family business succession. Such as the detailed content of succession plan, the succession time, the succession method, and the communication between the founder and the successors and so on. In addition, the identification and evaluation of family performance also need further research.

About the Author:

LI Yanshuang, professor, School of Economics and Management, Hebei University of Technology. Research interests: family business management.
E-mail: lilicathy@163.com.
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