Family Management and Profitability in Private Family-owned Firms: Introducing Generational Stage and the Socioemotional Wealth Perspective

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Extant research has investigated the relationship between family management and firm's profitability with the help of several theories like, agency theory, stewardship theory and the resource-based view. However, these studies have resulted in contradictory findings. In this article, the authors examine the relationship between family management and firm profitability from the socioemotional wealth perspective. The study covered 233 Italian family firms and was based on data collected on profitability ratios, family management (i.e. percentage of managers who were also family members) and the leading generation. This summary succinctly presents the research formulation, key findings and their implications for family businesses.

Socioemotional Wealth Perspective

Socioemotional Wealth (SEW) refers to the non-financial factors that influence decision-making in a family firm. These include the owner family's emotional needs like that of identity, status, influence and control, and continuity of family legacy. The SEW literature suggests that decision-making by family managers is often driven by their need for preserving SEW than being only rooted in financial/ business rationale.

The authors argue that the effect of family management on firm profitability is influenced by the family managers' SEW aspirations. Those with ***high SEW aspirations*** are oriented more towards ***non-financial (socioemotional) goals*** while the ones with ***low SEW aspirations*** are more focused on ***financial goals***.

Generational Stage

The authors further argue that the family firm's generational stage (i.e. the generation that leads the firm) is the contingency factor that influences the family manager’s need for SEW preservation and hence moderates the relationship between family management and firm profitability. The authors suggest that the ***need to preserve SEW*** is likely to be ***high in the earlier generational stages*** as the founder or co-founders strongly identify with the firm and are emotionally attached with the business.

However, in later generational stages, different family branches emerge. These branches may start pursuing different agendas leading to weakened family ties and commitment to business. Furthermore, their emotional attachment with the firm may also weaken due to family conflicts. In addition, after years of experience gained over generations, the firm establishes formal governance mechanisms, institutionalizes knowledge management and adopts objective decision-making systems. These objective mechanisms are more likely to keep the firm's decision-making anchored to the business/ financial rationale. Thus in ***later generational stages***, the family managers ***may not have a strong need to pursue SEW preservation***.

Key Findings

The results supported the authors' hypothesis. The key findings were:

1. ***Family management*** was found to have a ***positive interaction*** with ***generational stage*** (in both earlier and later generation stage firms).

2. ***Family management*** had a ***higher positive affect on*** firm ***profitability*** (measured by return on equity: ROE) for firms ***at later generation stages*** (High GS) compared to that on firms at earlier generational stage (Low GS), (see figure 1).

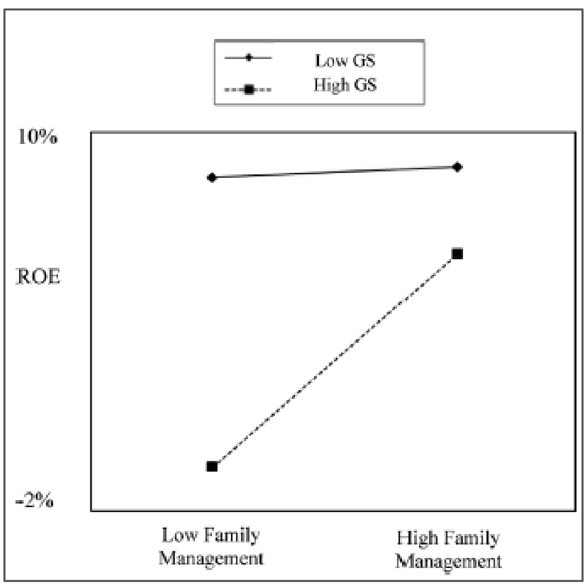

Figure1. Relationship between family management, generational stage (GS) and profitability (ROE).

The findings show how SEW (i.e. the firm's generational stage) differently influences the family manager's goals (i.e., more financial than socioemotional goals) and profitability in later generation family firms. The introduction of SEW perspective in the relationship between family management and profitability, ***explained the cause for*** the ***conflicting results in extant research*** that used other theoretical perspectives.

Practical Implications

The study has important implications for family businesses and practitioners. The extant literature suggests hiring non-family managers and reducing dependence on family managers as the firm grows older. However, the findings of this study suggest that family managers may contribute positively to firm performance even at later generational stages. What is more important is the introduction of objective governance and decision-making mechanisms that may keep the managers focused on financial goals. This will ensure improved financial performance. Thus, even in later generation family firms there is no need to exclude family members from the firm's management as they can have a positive impact on firm profitability.

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