Marketplace Flash

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Are Family Businesses More Successful?

According to my investment training, the definition of a security is any investment where the investor is relying on others to produce a return on the investment. This is why stocks in publicly held companies are called securities. For the investor, the question is which companies are most likely to perform the best.

An article titled "Family, Inc." in the November 10, 2003 issue of *BusinessWeek* provides some insight. The article reports the conclusions of a study of family businesses from 1992 to 2002. The study identified 177 of the S&P 500 as family business, which means that a founding family member is still involved either in senior management and/or as a director and/or as a major shareholder. Comparing the 177 family businesses against the balance of the S&P 500 using four metrics (i.e., average annual shareholder return, average annual return on assets, average annual sales growth, and average annual income growth), the study concludes that family companies outperform their non-family counterparts. Five key reasons are provided to explain why.

1. Born to lead – Passion is a key. The founders started with passion and tend to pass it on to their family members.
2. Quick decisions – Family businesses typically don't have extensive bureaucracy to impede decision speed.
3. Breeding loyalty – Blood is thicker than water. Family members tend to be more loyal and productive. Preserving family heritage and tradition is important to family members.
4. Investing in growth – Family businesses tend to be long term oriented and readily invest in the business. They tend to not play the Wall Street quarterly earnings game.
5. No absentee landlords – The interest of family members with large stakes in family businesses are aligned with investors. Holding management accountable is a key. Frequently, family members, who were raised in the business, are better equipped than the normal investor to both run the businesses and assess the performance of management.

So this empirical study suggests that family businesses are more likely to outperform non-family businesses. Why is this true? Christian philosopher Dennis Peacocke offers a possible answer ("Transforming People and Organizations", *Business Reform*, vol 4, no 2, pg 48-49). He argues that successful organizations are built relationally. That is, love should be the chief virtue of every organization. One of the greatest expressions of love is helping a person find his or her place in life. Therefore, the focus of an organization should be to find the right people and cultivate an environment in the organization that will enable each person to do what they are gifted to do with excellence. The *BusinessWeek* study suggests that family businesses may do this the best. Perhaps this is the way things were designed to work, and maybe this is the real reason why family businesses are more successful.