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AN ASSESSMENT OF THE COMPETITIVENESS OF CHINESE FAMILY FIRMS

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Abstract

There is phenomenon that from clogs to clogs is only three generations in China, on the contrary, Japanese family business always exited more three generations. So it is significant to find out Chinese firms' competitiveness. In this paper, we introduce the family firms as the one of the company organization form in the word, then through the external and internal factors, we analyse both the disadvantage and advantage of family business. Consequently, it is valuable for the firms to balance the merit and shortcoming in order to develop the business. On the basis of the findings, study concludes that Chinese family business does have a number of advantages, which could help improve the firms operation, especially in the early stage of the company. However, it is hard to make a conclusion that whether or not it has same advantages in the long-term period due to the short history of mainland Chinese family business.

Keywords: China, family business, firms, competitiveness

INTRODUCTION

Family business is one of the popular company patterns in the world. In terms of family business, it usually refers to those companies established by founders, and the entrepreneurs and their families play an important role in the decision-making process, company management and financial issues（Poutziouris et al. 2002; Martinsons and Westwood, 1997）.

There is an indication that family business takes up more than 75 per cent of all the companies all around the world (Leenders and Waarts, 2003). Among these companies, Chinese family businesses, especially the overseas Chinese family firms, play an important role in East Asia. In terms of the Chinese family enterprises, there is a host of controversy on it. Some argues that Chinese family has a series of disadvantages, such as too much emphasis on familism, nepotism, paternalism, the rejection of formal management, and difficulties of external capital access (Whyte, 1996; Zhang and Ma, 2008; Kanamori and Zhao, 2004). Others, however, also indicate that family firms actually have their own ways to address financial problems because their establishment and accumulation of personal network. And familism, paternalism, and top-down governance structure might also have positive influence on family-owned companies (Leenders and Waarts, 2003; Yu, 2001). Therefore, this essay aims to exploit the advantages and disadvantages of family business and then draw a conclusion on it.

DISADVANTAGES OF FAMILY BUSINESS

External factors

Broadly speaking, Chinese family business, like other kind of domestic private enterprises, also has a problem to get access to external financing. It should be mentioned that the capital operation of Chinese private companies largely depends on retained profits rather than lending money from outsiders, such as bank (Tanaka and Molnar, 2008; Garnaut, 2001). In particular, private enterprises found that it was increasingly difficult for them to get access to formal loans in the second half of 1990s (Garnaut, 2001). In this case, it is obvious that Chinese private enterprises, including family business, are still confronted with difficult access to external capitals. But why are Chinese private firms, including family firms, generally difficult to get access to bank loan? It might be attributed to the Chinese financing environment, especially the financing environment faced by small and medium enterprises (SMEs). One thing should be mentioned is that the majority of private companies in China are SMEs which took up around 99 per cent of the total companies in 2004 (Kanamori and Zhao, 2004). Although private companies, including family enterprises, have contributed largely to China's economy, they actually have difficulty in getting access to bank sectors, SMEs in particular (Kanamori and Zhao, 2004). To begin with, the limited discretion of domestic banks could be one of the external contributors. In effect, their authority to issue a loan was largely subjected to the national policies (Tanaka and Molnar, 2008). Historically speaking, there was no possibility for Chinese private enterprises to obtain formal loans from domestic banks until they were formally acknowledged in 1988 (Garnaut, 2001). In other words, government policies could be an obstacle to the discretionary loan provisioning of banks. Furthermore, the risk management could also be the contributor. There is an indication that the system of risk management was not adopted by the Chinese banks until 1999, which means that the system is not well-utilized by the banks due to insufficient skills or knowledge (Garnaut, 2001). In particular, why Chinese banks had not improved their skills towards exposure management can be attributed to that there was no need for them to do risk evaluation (Tanaka and Molnar, 2008).

Based on the former contributors, state-owned enterprises therefore could be an important factor affecting the competitiveness of Chinese family business. Compared with private firms, domestic banks preferred state-owned enterprises rather than private enterprises and were more willing to issue long-term lending to state-owned firms (Tanaka and Molnar, 2008). This could be partially related to the relatively lower risk of state-owned firms because of its competitive government guarantee (Tanaka and Molnar, 2008). Namely, banks were more likely to issue loans to state-owned companies but not the private companies, such as family firms. According to a survey by State Administration for Industry and Commerce, less than 10 per cent of private companies easily got access to bank loan and the lack of collaterals was the most common obstacle for the companies to gaining bank loan (Tanaka and Molnar, 2008). Meanwhile, it suggests that nearly all the private enterprises have to provide collateral as the only way to get access to bank loans (Garnaut, 2001). But many of the private companies actually do not have sufficient capability to provide corresponding collaterals (Garnaut, 2001). At the same time, private companies often faced the embarrassing situation that it could be difficult for them to get the amount of capital they want, especially the long-term loans (Tanaka and Molnar, 2008). It should be noted that a lot of private companies, including family business, have an urgent need of short-term capital while the banks are unwilling to loan (Garnaut, 2001). As such, neither short-term loan nor long-term loan is easily obtained by private enterprises, including family firms.

Internal factors

Apart from the general external contributors, some internal ones should be exploited as well, with respect to the drawbacks of family business. Firstly, nepotism and distrusting outsiders could be a disadvantage. Nepotism, being commonly used by Chinese enterprises in favor of family members, plays an important role in employment, promotion and delegating control (Tan and Fock, 2001). Distrust of outsiders is widespread among Chinese enterprises and family businesses in China generally prefer cooperation basing on friendship or kindred (Zhang and Ma, 2008). This could be, on the one hand, attributed to the shortage of social trust and be related to the protection of sensitive business secrets on the other hand (Zhang and Ma, 2008). Besides, lacking of social trust, the enterprises therefore are reluctant to utilize professional managers, which means that the nepotism could be further enhanced (Zhang and Ma, 2008). In other words, no matter how competitive the non-family employees are, the discrimination against non-family employees is more or less existed among family companies (Whyte, 1996). In this case, if the company often favors family member rather than non-family employees, those outsiders, particularly the capable ones, will be easier to leave the company, especially when they get a better job opportunity (Whyte, 1996). Furthermore, if a family enterprise is highly family-oriented, it could be more difficult for them to solve internal problems when conflicts happen between the family members (Leenders and Waarts, 2003). According to research, the family companies with weak nepotism and strong professional management could conduct better, in terms of addressing internal contradictions (Leenders and Waarts, 2003). Namely, too much emphasis on nepotism would do harm to the company, especially when conflicts cannot be well handled.

Secondly, familism could be a disadvantage as well. There is a suggestion that familism, containing strong family ties, plays a dominance role in Chinese family business while it is actually at the cost of other social relations (Tan and Fock, 2001). Even though familism could have an effective influence on the early stage of a family enterprise, neither further rule-based management nor future development could benefit from it (Kim and Gao, 2010). On the one hand, this is because that non-family-member managers could be regarded as a threat to the control of the family enterprise (Kim and Gao, 2010). Namely, recruiting a manager from outside, according to many family business owners' understanding, could have a negative influence on the decision-making process and the high centralization of management (Kim and Gao, 2010; Zhang and Ma, 2008). On the other hand, excessive focus on relationship with family members and inadequate company structure and decision-making process actually lead family enterprises to a shortage of higher skilled stuff, such as professional manager (Kim and Gao, 2010). And this shortage could negatively affect the further extension of the company (Kim and Gao, 2010). For example, when a family enterprise is experiencing business enlargement, it could be easier for them to run out of the existing family-member-based human resources and it is difficult for them to develop further (Wong, 1993). Namely, the family-oriented recruitment structure of family enterprises would be an obstacle to the company's further extension due to inadequate human resources supply, compared with other kind of companies, such as SOEs or foreign companies.

In terms of paternalism, it could be a vulnerability of family business and is associated with high control of the company. Actually, paternalism has a close relationship with the Confucian-based Chinese culture, which underlines the order as an importance tool to maintain the stability of society (Poutziouris et al., 2002). And it stresses the importance of father figure, who is often the owner or the founder of the enterprise, in the company and patriarch is normally related to high company governance and tight decision making (Zhang and Ma, 2008; Poutziouris et al., 2002; Ahlstrom et al., 2004). Broadly speaking, the simple decision-making structure of family business allows orders to be delivery directly from the top leaders and allows the entrepreneur to control the important business information tightly (Ahlstrom et al., 2004).

Nevertheless, excessive control of information could pose a negative impact on the fast growing industries, though it to some extent has a positive influence on traditional industries (Ahlstrom et al., 2004). This is because that fast information sharing is vital component in the high growth industries, such as high technology sectors (Ahlstrom et al., 2004). Moreover, paternalism might lead to low efficiency. According to a number of cases, even a general material has to gain approval from the top leader of the company because of the management and decision-making process is highly centralized (Ahlstrom et al., 2004). Additionally, paternalism could be a potential problem to family business. It is not only difficult for these tight-controlled firms to bring or recruit trustworthy outsiders as professional managers, but it also has a negative impact on the top leaders and their companies. This can be attributed to entrepreneurs' limited energy and the company will be in a mess if the entrepreneur passes away (Tan and Fock, 2001). Consequently, too much emphasis on one's authority might be positive to the company in the short-term, but could lead the company to an unstable governance situation in the long-term.

ADVANTAGES OF FAMILY BUSINESS

Although family business has a series of disadvantages, it actually has a number of merits. In terms of strong family tie, it does have a positive influence on family-controlled business and is based on family trust. By positively influencing the decision-making process, family-based trust enables family firms to quickly adapt the changing market (Yu, 2001). Actually, familism could help the company to solve the lack of work force. For example, it could be very difficult for the company to recruit extra work force during the boom season, but family members could offer temporary labor force during this period and they are more willing to work overtime, compared with workers from outside (Yu, 2001). In this case, it is true that the flexible utilization of family member is actually a competitive and reliable human resource to family-controlled enterprises, especially during the peak season. Moreover, the emphasis on familism could also help family business to survive in certain environment. For example, during the depression, the capital pool shared by family members could help the company get through the difficult time (Whyte, 1996). Besides, compared with non-family employees, family employees are more loyal to the company and such loyalty could be a positive force to motivate employees to devote themselves into the company (Whyte, 1996).

Paternalism also has a number of advantages. To begin with, paternalism is often related to certain advantages of leadership. For example, the relative stabilized and long-lasting leadership enable family-owned companies to accumulate competitive advantages, such as the accumulation of guanxi as well as deeper knowledge of certain industries (Redding, 1995). Beside, the relatively stabilized ownership is seldom challenged by the internal system, since its unique features, such as top-down governance structure by patriarch and high centralization of power, reduce such possibilities (Redding, 1995). Note that the business strategies could also benefit from the stable leadership. This is because that a long-lasting and stable leadership enables the company to focus on long-term strategies of company development, compared with other kinds of company that have to meet the demand of the short-term profits made by share holders or outsiders (Tung, 2010). Moreover, decision making process could benefit from paternalism. There is an indication that the centralization of power and governance enables family-controlled company to accelerate the process of decision making and further allows them to grab a number of business opportunities, adapting in the fast changing market (Tung, 2010). Additionally, the possibility of speculative activities could be reduced by paternalism due to the centralized decision-making process and leadership (Yu, 2001).

Although Chinese family-controlled firms are facing strictly limited access to the bank loan, they have effective strategies to solve problems related to external financing. Reducing transaction costs could be one of their strategies. Carney (2005) argues that social capital, as a personal asset and has an important relation with guanxi, helps family firms decrease a number of transaction costs, such as the costs of searching useful information, filtering crucial commercial massage, commercial adjustment, and implementations of contract. Also，cost leadership strategy could be an important tool for family business to offset problems resulted from external financing. This is because that family firms tend to focus on localization and limited-scope markets in order to achieve cost reduction and survive in the market (Carney，2005). Simultaneously, the reason why Chinese family business has a competitive cost advantage can be related to their preference for manufacturing. Carney (2005) indicates that the advantages of family firms in manufacturing, such as low market access, relatively low labor cost, simple management process, top-down supervision, allow them to compete with other kinds of companies. Moreover, the self-financing capability and small size of the majority of Chinese family business offer opportunities to these firms to reduce the costs of start-up and allow them to more flexibly respond to the fast changing market (Whyte, 1996). Also, small business size, the simple governance structure and paternalism help family firms overcome the shortage of external capital because these characteristics enable family enterprises to maintain flexibility while decreasing commercial risks (Poutziouris et al., 2002). Note that guanxi, which would be exploited in the next paragraph, also has a positive influence on addressing the problem of external financing by getting access to private loan and reducing the business costs.

Guanxi could also be a significant advantage to family business. Guanxi, which refers to a close and strong association between people, have a positive influence on commercial transactions (Kiong and Kee, 1998). To some extent, guanxi could help family business to solve problems of external financing. Not only can it be extended to establish a relatively reliable business relationship in the uncertain business environment, such as China, but also enables Chinese family businesses to get easier access to private capital than bank loan (Whyte, 1996). More importantly, guanxi could help family firms to reduce business costs. For example, basing on relative trustful business relationships and personal ties, guanxi gives firms a chance to reduce a number of possible business conflicts, such as internal disputes, litigations, and contractual contradictions (Whyte, 1996). Meanwhile, guanxi benefits the growth of family-controlled firms. Family firms could utilize guanxi as a tool to expand their market share through external relationships establishment and competitive market positioning (Park and Luo, 2001). Brunswick and Gables (2001) also indicate that guanxi is an essential tool for family business in transition economies because it brings chances for these firms to improve market share by enhancing relationships with governments or developing cooperation with competitors. One thing should be mentioned is that interpersonal relationship could help entrepreneurs decrease the risks of uncertainty in business while improving the commercial security (Kiong and Kee, 1998). Also, social capital of family firms could benefit from guanxi as well. In fact, the exploitation and accumulation of social capital is actually based on guanxi (Park and Luo, 2001). Compared with Chinese family-run firms which could survive and thrive in an uncertain environment, other kinds of company, such as Western ones, are suffering from market entry barriers because getting used to uncertain political environment and obtaining effective commercial information through guanxi-oriented networks are large challenges to them (Redding, 1995). Namely, a family-controlled enterprise can utilize guanxi as a tool to solve a host of external and internal issues.

CONCLUSION

As mentioned above, family business does have a number of competitive advantages. For example, the capability of reducing transaction cost and guanxi, to some extent, help firm-controlled firms to offset problems caused by the difficult access to external financing. Besides, even though guanxi has a series of vulnerabilities, such as expensive cultivation and maintenance (Park and Luo, 2001), it, to some extent, positively affects the family firms. For example, guanxi is actually an effective tool to be used by family enterprises to survive and develop in an uncertain environment as China, and also helps the company to cope with the relationship with government (Ahlstrom et al., 2000). Moreover, family business has a relatively stable and longer leadership, which would ensure the fulfillment of long-term business strategies, because of paternalism. In this case, family business is quite competitive, according to its advantages.

Although familism has a number of drawbacks, it actually has positive influences on family-owned companies. As mentioned above, it helps the company to address the financial problems through family members' common sharing capital, especially during the depression. Meanwhile, in terms of nepotism, it has been mentioned above that family employees are more loyal than non-family member. Nevertheless, familism and nepotism would be obstacles to the adoption of professional management. There is an indication that the extension of Chinese family companies is unavoidable, since the gradual growth and reform of Chinese economy would be driving forces for the further development of their business (Kim and Gao, 2010). In this case, it is necessary to properly address the disadvantages of family companies in order to improve the competitiveness of these companies.

Hence, it is hard to say that whether or not the advantages of family business surpass the disadvantages. The entrepreneurs of family firms should carefully balance the merits and the drawbacks mentioned above, and then properly utilize these features as tool to develop their companies. In short, Chinese family business does have a number of advantages, which could help improve the firms operation, especially in the early stage of the company. However, it is hard to make a conclusion that whether or not it has same advantages in the long-term period due to the short history of mainland Chinese family business.

Currently, the study of Chinese family businesses are mostly concentrated in economics, management science fields , mainly for family heritage , problem management innovation and talent to explore the use of other aspects , the factors leading to the development of Chinese family businesses have a lot of bottlenecks , and overall competitiveness often be ignored . Our future competitiveness above also need a more detailed study in order to find problem solving strategies

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