

Maintaining the Entrepreneurial Orientation in Family Businesses

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Abstract

The subject of this paper is the family businesses and their specific relation to entrepreneurship. Entrepreneurship, as a modern and appropriate way of action of enterprises in turbulent environments, from the companies requires special treatment for its development. This treatment stimulates specific issues for family businesses, their willingness to undertake entrepreneurial ventures, the attitude towards taking risks, degree of innovation etc. that depend on the internal structure of the enterprise and the way it governances. Republic of Macedonia is country in which this question is current, but the status of family business is still not formally defined. For this purpose, first we will determine the nature of family businesses and make a comparative review of family and non-family enterprises to determine the similarities and differences between them; we will identify the major issues concerning this type of enterprises and etc. The theoretical views on this issue will be backed up by statistic for family businesses. However the main focus is identifying the dimensions that reflect the entrepreneurial orientation of family businesses and making recommendations on how it should be maintained.

Keywords: Entrepreneurship, family businesses, entrepreneurial orientation.

1. Introduction

For a more successful development of entrepreneurship as a way of functioning of enterprises and a response to the contemporary business environment, a thorough study of this process which would include all stakeholders is needed. First we would need to address the nature of the carriers of this process- enterprises and entrepreneurs. Generally, what connects enterprises with each other is having the same goal- making profit, but from this shared commitment arise all further differences. It's a question of the ways to make profit and taking its share on the market, which can be numerous and varied. Certainly the activities of

enterprises are partly determined by its characteristics, size, work, and what will specifically focus in this paper is the impact of ownership structure and composition of companies whereby we will divide them in family and nonfamily businesses.

2. Definitions and Preliminaries

2.1 The Nature of Family Businesses

In scientific literature there are many attempts to define family businesses in order to determine the exact features that separate the family from the nonfamily businesses, and thereby recognize the specificities of the relation that these two types of enterprises have in the develop of entrepreneurship. In many of the definitions an attempts is made for closer and more precise definition of separate specific pints relating to family businesses, but what emerges as common is the claim that family companies is the most general sense are those enterprises that are owned and controlled by members of the family and employing two or more family members. Research conducted by the European Commission on EU member states said that in a third of surveyed countries family businesses are considered and registered as self-employed/one-person enterprises, while registered as a sole proprietor are considered as family businesses almost in all EU countries.

As regards to the specifics of family businesses, the first and most notable difference which appears in the structure of family firms opposite nonfamily firms are the three recognizable structural elements: family, business and ownership¹. Based on these three elements Tagiuri & Davis have developed “3-circle” model of family businesses in which the segment of property gives the main difference between family and nonfamily businesses.

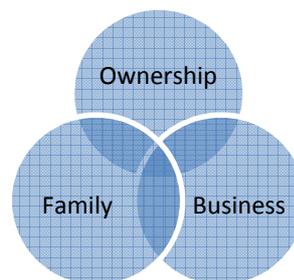


Figure 1: “3-circle” model of family business (Tegiuri& Davis, 1982)

As to the importance of the family businesses do not doubt, not only because of what they represent to the economy, but also because of their commitment to local communities, the stability which they bring in longer periods, the responsibility they feel like owners and the values they cherish. What is their relevance to certain countries, it may be best seen if it is traced across the state figures. In the USA 90% of registered businesses belong into the area of family businesses². These include companies of various sizes, starting from the smallest companies up to the big companies. They generate almost half of the gross domestic product and more than half of total pay. To them belong 60% of total employments in the USA and 78% of new jobs. Similar is the situation in the European Union. EU family businesses account for over 60% of total companies that include micro enterprises as local entrepreneurs, and large international companies. However most of them relate to the SME sector.

¹Burggraaf, W., Floren, R., Kunst, J. (2008) “*The Entrepreneur & the Entrepreneurship Cycle*”, Van Gorcum, Assen, p. 301

²Bowman-Upton, N. (1991) “*Transferring management in the family-owned business*, U.S. Small Business Administration”, Texas, p. 2

2.2 Entrepreneurial Behavior of Family Firms

How much an enterprise is entrepreneurially oriented we can determine by five different dimensions suggested by Lumpkin and Dess's³:

- Proactive action- this action involves the ability to predict in advance the possible problems and changes that may occur. This kind of action opens up new perspectives and opportunities for new ventures and innovative activities.
- Willingness to take risks- involves borrowing and commitment to high level of resources in projects with uncertain results, as well as entering new markets.
- Innovation- refers to the tendency of companies to generate new ideas and support creative processes and experiments from which may arise new products, services or technological processes.
- Autonomy- is related to the independence of individuals or teams to generate new ideas and executing them. This operation requires a flexible organizational structure and the opportunity for open communication.
- Competitive aggressiveness- related to the way of action of enterprises that directly and intensely challenge the competition in order to achieve market entry or to improve the already acquired position.

These five dimensions are somehow seen as indicators of how a company behaves entrepreneurially. Basically, they are characteristics of entrepreneurship. Although separate they are interrelated. Each company can vary on these dimensions, so as an example we have companies that are differing in the degree of innovation; some companies are more inclined to take risks than others, further there is the aspect of autonomy and so on. Often these dimensions are determined by the context. As contextual factors with potential influence on the entrepreneurial orientation can be considered the type of the company, size, ownership, etc... It is these contextual factors that come to light in the area of family businesses, and as crucial is the impact on the relation family- business. Family interest often conflict with business interests, especially when it comes to making decisions with a high degree of risk, conflict may arise between the active and inactive members of the family and all this can have a negative impact on the entrepreneurial orientation of the enterprise. The climate of strong family relationships may negatively affect the ability to create and sustain entrepreneurial capabilities of the enterprise and therefore it is determined that family business take risks, but in terms of a nonfamily business it's a much lower percentage.

Itself raises the question of the duality of the two included dimensions family and business, which are intertwined and their impact on enterprise performance. What is obvious is the achieving high performance of family businesses is necessary to establish the right balance and alignment between these two dimensions. Given their nature what immediately highlights is the need to achieve not only financial goals but also non-financial goals. Moreover, when we talk about achieving high performances there is a choice which of these two dimensions will the enterprise strive to reach the highest achievements. Good performances in terms of the family dimension indicate a company with high accumulation of emotional capital and good business performance of companies show high accumulation of financial capital. Exactly for this question a special matrix is developed that considered four possible variations of the performance of family businesses⁴.

³Landström, H., Crijns, H., Laveren, E., Smallbone, D. (2008) "Entrepreneurship, Sustainable Growth and Performance: Frontiers in European Entrepreneurship Research", Edward Elgar Publishing Limited, Cheltenham, p. 94

⁴Poutziouris, Z. P., Smyrnios, X. K., Klein, B. S. (2006) "Handbook of research on family business", Edward Elgar Publishing Limited, p.28

Figure 2: Performances of family business

		FAMILY DIMENSION	
		Positive	Negative
BUSINESS DIMENSION	Positive	I Warm hearts-deep pockets <i>(High emotional and high financial capital)</i>	II Pained hearts-deep pockets <i>(High financial, but low emotional capital)</i>
	Negative	III Warm hearts-empty pockets <i>(High emotional, but low financial capital)</i>	IV Pained hearts-empty pockets <i>(Low financial and low emotional capital)</i>

- *Warm hearts-deep pockets.* Quadrant 1 of the matrix represents the most successful entrepreneurs. It is the highest level at which a family firm can aim which means financial and nonfinancial goals. This is an example for enterprises that succeeded to establish adjustment between the family and business dimension and thus to achieve the highest performance.
- *Pained hearts-deep pockets.* In quadrant 2 are located companies that put an emphasis on achieving financial targets and to this end led to neglect of the emotional dimension. They have achieved business success, but on account of disturbed family relations, here you can recognize large enterprises, that in order to achieve global expansion and profit neglected and violated the family relationship. To maintain the good business here as a central issue is the mutual relations because good relations can overcome bad business decision, but the opposite is impossible. Viability in longer terms in these enterprises depend on the development of the helping mechanism to improve mutual relations that will positively reflect on business dimensions and thus firms will move to those described in quadrant 1.
- *Warm hearts-empty pockets.* In quadrant 3 are found the firms that develop strong relations between family members, even though their business has low scores. Characteristic for such enterprises is that after a certain period of this state comes to pauperization of the accumulated resources and that reflects on family relationships, despite the low financial capital an impoverishment comes also to the emotional capital.
- *Pained hearts-empty pockets.* Companies in quadrant 4 are failed enterprises in terms of both dimension. They failed to make any emotional or financial capital. The owners of these enterprises can use the failure of this business attempt as an experience from which they can benefit for future business beginnings.

As it can be seen from what has been explained by far family businesses fall into a specific group of enterprises which comes to intertwining of the two dimensions of *family* and *business* and as a consequence of that many specifics occur regarding the activities of enterprises. It is a vulnerable group of companies where the smallest deviations of represented dimensions can cause visible changes in the performance of enterprises. The segment of the family and its involvement in business certainly has its consequences on development and on practice on entrepreneurial behavior in these enterprises. In the scientific literature can be found opinions that these companies are less entrepreneurial tuned unlike nonfamily businesses, because the reserved terms that they have for risk taking in the sense that family businesses are more careful of when to make decision of this kind.

2.3 Reflection of the Duality Family/Business over the Management of the Family Business

In this paper we will refer to the survey conducted in the Netherlands where for confirmation of this purpose the 5000 largest companies in the countries were examined, and from 39 set variables a total of 15 differences were identified that exist between family and nonfamily businesses⁵. Here we will focus on a few of them that are considered the most obvious and widespread. These differences clearly indicate what is the reflection of the family dimension in the running of the business.

Recruitment of the fresh graduated staff: As a result of the shown distrust only 32% of companies employ fresh graduates, unlike nonfamily businesses where this percentage is higher and is 46%. This difference is more pronounced if the CEO is a member of the family, even in 50% of these enterprises the employment opportunities of graduates are almost minimal.

The application of effective system for evaluating employee performance: Only 51% of large family businesses apply an effective evaluation system, while this percentage in nonfamily enterprises is much higher and it's a total of 81%. There are also differences that exist regarding the treatment and performance of employees. It was found that in the Netherlands only 18% of large companies pay salaries to family members employed in the enterprise that are not equal to the remuneration that would have been received as employees of the same position in nonfamily businesses.

The role of spouses of executives: In family businesses the tendency spouses of executives to be involved in business and have their share of ownership is much more pronounced. For example, only 63% of family firms prefer spouses to be employed in the enterprise, unlike nonfamily where this phenomenon is represented only by 25%. As regard to the shares of the firm 40% of spouses own stocks (have a share) of the company in family businesses, which is much higher compared with 17% of nonfamily enterprises.

Duration of the function of the management: In 62% of family businesses a current outbreak can be found where the current management runs after 8 years or more, unlike nonfamily enterprises where this phenomenon is only in 44% of the cases.

Generally, there are numerous differences between family and nonfamily businesses, but it is interesting that some things are perceived differently in these two types of enterprises. For example, in nonfamily businesses the interests of employees are different from those in family businesses in terms of flexibility of working time and deviation from the estimated number of hours especially during increased workload. Further differences are felt in terms of willingness to complete the task, the quality and coverage of absent workers. In family businesses all these activities are completed with greater harmony which provides higher quality. An advantage of family businesses can be considered the motivation of family members to work hard. Harmony in work, encouragement of one another, undefined working hours, replacing the absent worker, etc... in nonfamily firms are considered as a demotivation. Unlike family businesses, in nonfamily businesses if the relation manager-employee is disturbed it can lead to decreased creativity and inventiveness among employees. This relation in family firms is usually deserted and the tasks are performed by those who fit them most.

⁵Flóren, H. R. (2002) "Crown princes in the clay: an empirical study on the tackling of succession challenges in Dutch family farms", Koninklijke Van Gorcum, p. 82

As a difficulty in nonfamily firms appears the fact that the owner of the company must pay employees according to the agreed no matter if he learned enough or not, while in the family business this is more flexible. But family businesses also have numerous weaknesses that make them vulnerable in longer terms such as poor management, problems related to access to finance for further development, inadequate cost control, etc.

3. The State of the Family Business in the Republic of Macedonia

When talking about the definition of family businesses in a national context, the case with the Republic of Macedonia is interesting, as a candidate of EU membership it is also included in the review of the European Commission⁶. We can freely say that in Macedonia there is no consensus on what can be considered as a family business. Practice shows that in the Macedonia one-person enterprises can be considered a family business only if companies whose activity is agriculture, whole sale and retail trade, hotel services and restaurants, catering and related economic sectors, which provide engaging family members without their formal employment. Another important prerequisite is that this individual has a major role in the finances of the family. Sole proprietors, can also be regarded as family businesses, but only when most family members are employed in the enterprise. Interestingly, in the legislation in Macedonia there is no law that relates specifically to family businesses as a specific type of enterprises that by their nature are different and require special treatment. The current classification of enterprises in Macedonia was made in 2004 by making changes in the Law for trade company based on the criteria of the European Union which include number of employees, annual address and value of business assets, with the first criterion (number of employees) are used identically as in the EU, while the other two are adapted to the conditions of the economy in Macedonia. According to this classification Macedonia formally distinguishes only micro, small, medium and large enterprises. In Macedonia 95% of registered enterprises belong to the SME sector. Given the fact that family businesses in general and usually cover most of the SME, (although in the world they also apply to large enterprises in Macedonia is a rare event), it can be concluded that this type of enterprise is represented in the country and certainly the specifics of their functioning also affect Macedonia.

4. Recommendations for Successful Maintenance of Entrepreneurial Orientation of the Family Business

It is more than obvious that the organizational context of family businesses because of the specificity of the relation between family, enterprise and individual pints out as special. The negative effects that arise from this relation on development of enterprises are indentified, but the question is how to derive the benefits that could arise from this duality? We already discussed the confrontations business-family, but these tensions can be used as favorable for business. For an example of duality in the field of entrepreneurship is to say taking risks versus the calculated behavior, in terms of management here is centralized despite from the decentralized management and so on. The innovative challenge from this duality does not result from choosing one of these opposites, but the success is in the managing in their simultaneous existence.

Previous experience shows that a family firm is to be considered entrepreneurial and to achieve the desired results is not mandatory to achieve high results in all five listed dimensions. To the contrary the desired results are in direct dependency with the context in

⁶European Commission (2009) *“Final report of the expert group, Overview of Family-Business-Relevant Issues: research, networks, policy measures and existing studies”*, p. 2-6

which they occur. As far as family businesses important types of dualism that occur as a product of their nature and features are⁷:

- *the traditional/new way of action*
- *dependence/independence* and
- *formality/informality.*

These are the dualities that have the most evident impact on the achievement of entrepreneurial orientation on family businesses. Innovation, risk taking, autonomy, proactiveness and competitive aggressiveness can occur in different combinations and different degrees all in direct dependency with the contextual conditions and the impact of duality. Entrepreneurial orientation is associated with the context in which organizational activities occur.

With this way of setting things and practicing the principle of duality, in fact shows that the family nature and entrepreneurial orientation within family businesses should not necessarily be contradictory to each other. On the contrary to sustain entrepreneurial orientation and support the development of entrepreneurship through the generations, family firms need to properly manage the existing dualism. Thereby to maintain the tension on a required level some of the dimension of entrepreneurial orientation will be more present and more exploited unlike others.

The question is how to maintain the required level of tension?

Namely family firms in particular should be aware of the nature and presence of the family dimension in all parts of functioning and accordingly to this to plan their steps. It involves the creation of appropriate management strategies and acceptance of existing dualism. Simply told the management of dualities involves simultaneously pulling on both ends and maintaining the tension through simultaneous strengthening of the two opposites instead of forcing and reliance on only one side of the duality.

What this means in terms of already identified three dualities characteristic for family businesses?

- This means that the manager team should cherish the traditional way of functioning that already led to faceless achievements and results, but also find new easy of acting and adapting to the current environment.
- In the part of formality versus informality it should be noted that as a consequence of causing growth companies have the need to introduce formality in terms defining the structure and introducing order into the functioning, but also need to preserve the necessary degree of informality that is favorable for the development of flexibility and the maintenance of creative climate, which is extremely important for entrepreneurship.
- About duality dependence/independence the management should practice independence in the area of action while simultaneously aims to create greater dependence (followers) to his views by members of enterprise which are not family members.

⁷Landström, H., Crijns, H., Laveren, E., Smallbone, D. (2008) “*Entrepreneurship, Sustainable Growth and Performance: Frontiers in European Entrepreneurship Research*”, Edward Elgar Publishing Limited, Cheltenham, p. 112

5. Conclusion

Due to the high level of representation, national economies have an interest in finding appropriate way of managing with this type of business and finding solutions for their adaptation to entrepreneurial type of behavior. The entrepreneurship is an imperative for survival in the modern environment. In that direction that paper gives an overview of family businesses including their definition, structure, the impact of the family dimension on entrepreneurial behavior etc. The analysis shows that the essence of family businesses lays the principle of duality because of which actually comes to a different way of functioning of this type of enterprises and the difficulties in the development of enterprising habits. By introducing the nature of this duality actually shows that the family nature and entrepreneurial orientation within family businesses should not necessarily be contradictory to each other. In that direction are the recommendations to maintain the entrepreneurial orientation of family firms across generations consists in the acceptance and proper managing of the existing dualism.

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