

# The family: part II

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# Family ties and family business

- Family business: a family holds control of a company, either by not trading it publicly or by holding majority stake if it is a publicly traded company
- Many examples of very successful family company (but you do not hear as much about the failed ones!)

# Pros and Cons of family firms

- 1) managing for the long terms. Long horizon. But: excessive risk aversion?
- 2) substitution for lack of trust. Trust the family only. But: this is a second best solution for an economic structure lacking diffuse trust.

# Pros and Cons of Family Firms

- 3) Human Capital: you may train your sons/daughter to learn the business. But: restricted access to others, is there a positive or negative correlation between managerial ability across generations?
- Also tendency to nepotism in hiring

# Pros and Cons of Family Firms

- 5) Political connections: family firms may have a better chance at getting insiders' help through personal connections with the political world. But: again this is a second best solution, the first best would imply no political connections

# Pros and Cons of Family ties

- Family firms may be especially influenced by the desire to leave legacies and may make decisions influenced by local inheritance laws and these decisions may be in contrast with the long terms profit maximizing and growth interests of the firm.

# Empirical Evidence

- Several studies for many European and Latin American countries show that family firms are on average less well performing than non family firms.
- Family transmission of managerial positions does not perform particularly well.

## Bertrand and Schoar JEP 2006

- Do family ties affect the share of family firms?
- Yes. Proxy for family firms:
- Self employment; establishment size; number of firms over/population;



## More...

- Proxy for financial structure: fraction of firms in sectors that typically rely more on external source of financing; share of market capitalization owned by top 5 families (for a subset of countries)

# Results

- Strength of family ties typically associated with those measures of family capitalism

# Criticism

- Cross country evidence very prone to a criticism of reverse causality.
- Example: underdevelopment of financial market may lead firms to find it difficult to rely on external finance and family firms became the only way to self financing.