ECONOMICS & Sociology

Saidat, Z., Bani-Khalid, T., Al-Haddad, L., & Marashdeh, Z. (2020). Does family CEO enhance corporate performance? The case of Jordan. *Economics and Sociology*, *13*(2), 43-52. doi:10.14254/2071-789X.2020/13-2/3

DOES FAMILY CEO ENHANCE CORPORATE PERFORMANCE? THE CASE OF JORDAN

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ABSTRACT. There is a high level of family ownership among Jordanian firms, which is perceived to be the reason why family members are often appointed as CEOs. Advantages and drawbacks of having a family CEO, who tends to concentrate corporate control within the family and minimize ownership dispersion, continue to be debated widely. This study adds to this debate by focusing on the under-researched Jordanian context, where family companies are prominent. A sample of 56 Jordanian listed family firms and 392 firm-year observations for 2009 to 2015 have been used to determine that overall family CEOs are negatively related to corporate performance. This finding is applicable to both accounting-based and market-based performance, stemming from the ROA and Tobin's Q test results. Further analysis shows an increased negative effect in family firms where non-family shareholders have greater ownership. The study concludes that increases in the level of ownership concentration leads to devaluation among Jordanian family firms.

Received: December, 2019
1st Revision: March, 2020
Accepted: June, 2020

DOI: 10.14254/2071-789X.2020/13-2/3

JEL Classification: D02, O17, P31

Keywords: family business, family CEO, financial performance, multivariate pooled-OLS regression, Jordan.

Introduction

Chief Executive Officer (CEO) is the most powerful position in any management team (Linck et al., 2008), so it has long been in focus of research in finance and management studies. CEO decides on a strategy for a firm, allocates capital according to firm's priorities and supervises senior executive team. CEOs are seen to be on par with the board of directors, even though they are appointed by the board (Allen, 1974). Appointment of CEO is an important organizational decision, which has significant implications for firm effectiveness (Kaplan, Klebanov & Sorensen, 2012). Papadakis and Barwise (2002) determined that strategic decision- making process and firm performance are greatly influenced by CEO.

Given the importance of CEOs, their role and appointment within family firms has also garnered great interest. Family members often have both ownership and executive management roles in a firm, which is viewed as reducing agency costs (e.g., monitoring and bonding costs) for managers and shareholders. James (1999) found that family managers have a clearer and more profound understanding of firm operations as compared to non-family managers, so relieving the difficulties involved in separation of ownership and control. They further argue that a firm may benefit from business and political networks created by the family CEO. Fahlenbrach (2009) argued that family CEOs spend more on research and development, have higher capital expenditures and are more interested in mergers and acquisitions. Morck et al. (1988) concluded that a family CEO is normally an expert in business and so adds value to a firm.

In contrast, Barth et al. (2005) argued that same family ownership and management can have a negative impact on firm's performance as they may choose family members as managers even though they are ineffective and unqualified to fill managerial positions. Added to this, a family CEO can involve themselves more in the selection of board members, further entrenching their position irrespective of the CEO's actual share in the firm (Morck et al., 1988). Such arrangements would reduce firm's productivity (Burkart et al., 2003).

A family CEO is the norm in Jordan. Family owners generally appoint a member of their own family as a CEO, and 55% of companies are family owned (Saidat et al., 2019). This study seeks to understand such practices and appears to be the first to study these issues in Jordanian context.

1. Literature review and hypothesis development

There has been extensive research on impact of family CEOs and non-family CEOs on corporate performance, including CEO founders and CEO descendants with a variety of findings. In a sample of 336 firms from the Fortune 500 database, 1992 to 1996, Adams et al. (2009) found that founder CEOs positively affect firm performance with their ability to influence firm performance and decisions. Furthermore, the involvement of CEOs in the board of directors was found to have no significant impact on financial performance. Anderson and Reeb (2003) also found that family CEO positively affects the firm, in terms of its accounting-based performance and showed a positive relationship between CEO founder and share market. This positive impact was not found for CEO descendants; though they concluded that family CEOs are good for financial performance in both old and young companies. However, Morck et al. (1988) found that a family CEO only improves market-based performance in younger companies, arguing that a family CEO is more a sign of entrenchment than success in older companies.

McConaughy et al. (1998) examined the operational efficiency and the worth of U.S. family firms where either the founder or their descendants are the CEO and determined that both CEO founders and CEO descendants have more positive impacts on firm performance than non-family CEOs. A study by Barontini and Caprio (2006) on the impact of founder and descendants in running the business identified positive associations for family members as CEO and firm valuation. Villalonga and Amit (2006) found the same, except for a lesser positive impact by CEO descendants. Using a sample of French companies, Sraer and Thesmar (2007) further supported these positive findings, with family CEOs performing better than publicly traded companies in terms of administrative practices.

In line with these studies, Fahlenbrach (2009) identified a higher valuation and improved stock market performance in companies run by family CEOs, with a large sample of US films for 1992-93. Overall, many studies, covering a wide range of sample data identify positive impacts on firm performance associated to the presence of a family CEO (Palia and Ravid, 2002; Polsiri and Wiwattanakantang, 2004). Meanwhile, there are a number of studies evidencing a negative relationship between family CEO and firm performance. Barth et al. (2005) found that family CEO firms are less productive than non-family controlled firms in a study of 438 Norwegian firms for 1996. Pandey et al. (2011), studying large family owned firms in India, found that a family CEO negatively impacts on firm performance.

Bertrand et al. (2008) studied family CEO impact in Thailand, including a CEO son of the founder on firm performance. They identified a negative relationship for family CEO on performance, worsening further for firms where the founder was dead, and the son was now CEO. Other studies have also shown the disadvantages of having a family CEO for firm performance (e.g., Pérez-Gonzáles, 2006; Bennedsen et al., 2007). Some of the advantages of non-family CEOs include more experience and education than family members with greater capacity to introduce professional management practices (Bennedsen et al., 2007; Sonfield and Lussier, 2009).

The literature is ambiguous on family CEO impact on firm performance. From many studies of firms in a variety of geographical contexts different results have been reached on the role of a family CEO in improved performance (see Table.1). So, currently, the relationship between performance and family CEO is an unresolved and ongoing research issue which benefits from further exploration. A strong family relationship is one of the most important characteristics of Jordanian society. Caring for family, family relationships and reputation equally play key roles in business in Jordan. A family member CEO will have these additional issues in mind in the business role, and developing the company will develop the family reputation and the CEOs own status within the family. Overall, these factors mean a family CEO will be more committed to the success of the company. This is in line with common beliefs in Jordan that a family member will be a better executive manager due to their knowledge and experience of the company and their personal sense of belonging. Such practices sustain and promote high ownership concentration which, according to agency theory, can negatively affect the rights of small shareholders, as it augments the conflict of interest between small and large shareholders (Baydoun et al., 2013; ROSC Jordan, 2004). Large shareholders hold the power to appoint their family members, so these appointees have multiple motivations to favor the interests of large shareholders at the expense of the small. This is both reflected in and supported by the common practice of favoritism in senior appointments by large shareholders (Al-Jazi, 2007). Undoubtedly, such practices can adversely affect firm performance. Therefore, building upon the current literature, this hypothesis can be formulated:

$\boldsymbol{H_1}$: *There is a negative relationship between family CEO and firm performance.*

Table 1. Summary of studies on the relationship between Family CEO and Performance

Authors/ Year	Country	Sample & Period	Performance	Findings
Morck et al. (1988)	Fortune-500 firms	371 firms (1980)	Tobin's Q	Positive relationship
Anderson and Reeb (2003)	S&P 500	2,713 firm-years (1992)	ROA and Tobin's Q	Positive relationship
Villalonga and Amit (2006)	Fortune-500 firms	508 firms (1994-2000)	ROA and Tobin's Q	Positive relationship
Sraer and Thesmar (2007)	France	2,973 Observations (1994 – 2000)	ROA, ROE and Market to Book	Positive relationship
Bennedsen et al. (2007)	Denmark	5,334 CEO successions in Danish firm, 1994-2002	OROA	Negative relationship
Adams et al. (2009)	USA	336 firms from the Fortune 500 database (1992 – 1999)	Tobin's Q and ROA	Positive relationship
Fahlenbrach (2009)	USA	2,327 large companies (1992 and 1993)	Stock Market Performance	Positive relationship
Kowalewski et al. (2010)	Poland	217 Polish companies (1997 - 2005)	ROE and ROA	Positive relationship
Pandey et al. (2011)	Indian	131 biggest family firms (2008)	Tobin‘s Q	Negative relationship
Kalyanaraman (2015)	Indian	288 Indian firms, 2009-2014	MTB	Negative relationship

2. Data and Methodology

A sample of Jordanian family firms listed in the ASE between 2009 and 2015 is used in this study with the same criteria as previous studies, where firms that did not survive during the study period due to liquidation, merger or other are dropped from the sample (Yermack, 1996; Cheng et al., 2008). The definition of a family firm based on 10% cut-off level was adopted, leading to the selection of 56 family firms with 392 family firm year observations.

Data was collected from several secondary sources. First, CEO duality and family CEO data was manually collected from annual reports. Second, ownership concentration data (large shareholders) was manually collected from the company websites, the Thomson One database and the ASE Annual Company Guide. Third, data related to firm size and leverage variables came from firms' financial statements at the Securities Depository Centre (SDC).

Financial Performance Measurements

This study follows previous studies which have used Tobin's Q and ROA as proxies for corporate financial performance (Anderson and Reeb, 2003; Denis & Denis 1994). The accounting-based measure (ROA) is calculated by dividing the net income by the total assets of the company. Tobin's Q, the ratio of the book value of total assets minus the book value of equity, plus the market value of equity to the book value of assets is used as a market-based measure.

Control Variables

CEO duality and ownership concentration were used as control variables based upon previous studies. Braun and Sharma (2007) found that duality itself does not have any influence on the performance of family businesses, but the division of roles does help to resolve conflict of interest between family owners and non-family shareholders. Further, they found that the proportion of equity holdings of the family posed a risk in the relationship of duality and performance. Shleifer and Vishny (1986) assert that ownership concentration positively impacts on firm value, where concentrated ownership is higher and large shareholders have the motivation and ability to monitor managers. Maury (2006) identified very useful firm-specific characteristics when assessing corporate performance, firm size and firm leverage. Firm size is the natural logarithm of total sales and is expected to be positively associated with financial performance because of the accessing of outside funds and economies of scale (Ng, 2005). Firm leverage is measured as the ratio of total debts to total assets and is expected to be negatively associated with financial performance as proposed by pecking order theory.

Table 2. Variables definitions and explanations

Variables	Symbol	Definition
CEO Duality	*CEODUALITY*	A dummy variable takes 1 if the CEO being chairman, and 0 otherwise.
Family CEO	*FAMCEO*	A dummy variable takes 1if the CEO being family, and zero otherwise.
Concentrated Ownership	*OWNCON*	The total of shares that are owned by shareholders who own 5% or more in the company
Firm Size	*FSIZE*	Natural Log of Total Assets
Leverage	*LEVERAGE*	Total debt / Total assets.
Return on Assets	*ROA*	(Net Income / Total Assets) × 100
Tobin's Q	*TOBIN'S Q*	(Equity Market Value + Liabilities Market Value) / (Equity Book Value + Liabilities Book Value)

The study also uses pooled regression with panel data in its model. Set out below is the formula for the analysis of the relationship between family CEO and financial performance.

$$\text{Financial Performance} \sim f\,(\text{FAMCEO, CEODUALITY, OWNCON, FSIZE, LEVERAGE}).$$

As financial performance is measured by ROA and Tobin's Q. Two separated equations are formulated as follows:

$$\text{ROA} \sim f\,(\text{FAMCEO, CEODUALITY, OWNCON, FSIZE, LEVERAGE}).$$

And,

$$\text{TOBIN'S Q} \sim f\,(\text{FAMCEO, CEODUALITY, OWNCON, FSIZE, LEVERAGE}).$$

3. Analysis and results

This section shows the analysis of data including; descriptive statistics and the analysis of data using multiple regression.

Table 3. Descriptive statistics

Variable	N	Mean	Min	Max	Std. Dev.
CEODUA	392	.2321429	0	1	.4227392
OWNCON	392	.6544612	.168172	.988425	.2068144
FSIZE	392	7.224641	6.21101	8.48071	.4933972
LEVERAGE	392	.2931973	.017231	.906591	.2066389
ROA	392	.0004915	-.004491	.13655	.0069402
Tobin’s Q	392	-.0127072	-.012877	-.012265	.0001457

3.1. Multivariate Analysis

This section explains the main results which were drawn from pooled-OLS regression analysis of the relationship between financial performances as a dependent variable measured by ROA, Tobin’s Q and corporate governance mechanisms as independent variables. However, before discussing the results, some assumptions (such as, multicollinearity and heteroscedasticity) need to be tested.

Firstly, we consider the problem of multicollinearity which indicates that two or more variables have a high or perfect correlation (Hair et al., 1998). The variance inflation factors (VIFs) is used to detect the existence of multicollinearity. According to the results of the VIF, multicollinearity was not found to be a problem in our model as all variance inflation factors less than 10 ranged from 3.75-1.2. Secondly, we use the Durbin-Watson statistic to check if the variables are serially correlated in all conditions. Velnampy (2011) argues that the Durbin-Watson statistic should be between 1.5 and 2.5 to indicate that there is no autocorrelation. As shown in table (4) below, the Durbin-Watson test reveals that our models do not suffer from autocorrelation. This study also conducted a Breusch-Pagan test to ensure a lack of heteroscedasticity. The figure in table (4) show that the p-value is smaller than 0.05, then the null hypothesis constant variance is rejected and there is evidence of heteroscedasticity. In this case, we employ the robust-cluster standard errors estimator through Stata software aiming to control for heteroscedasticity problems. Using this cluster standard error estimator, we supposed that observations should be independent across clusters (Thompson, 2011).

Table 4. Results of OLS assumptions tests

Tests (Stata)	ROA	Tobin’s Q
Durbin Watson statistic for autocorrelation	1.991	2.019
Breusch-Pagan/CookWeisberg test for heteroscedasticity (p-value)	6.95 (0.008)	85.07 (0.000)

The following table presents the overall results for the effect of corporate governance on financial performance measured by ROA and Tobin’s Q as independent variables. The results are jointly significant at 1%, 5% and 10% of significance. It should be noted that R-squares for the ROA is 5%, while 9% for Tobin’s Q.

Table 5. The impact of Family CEO on Financial Performance (ROA)

Financial Performance (ROA)		
Variables	**Coef.**	**P(Sig)**
CEOFAM	-.011	0.348
CEODUA	.000	0.803
OWNCON	-.036	0.353
FSIZE	.018	0.121
LEVERAGE	**-.014**	**0.015****
R-squares	0.0559	
Prob> F, chi2	0.000	

** Significant at 5%. *** Significant at 1%.

Table 6. The impact of Family CEO on Financial Performance (Tobin's Q)

Financial Performance (Tobin's Q)		
Variables	**Coef.**	**P(Sig)**
CEOFAM	**-.025**	**0.010*****
CEODUA	**.014**	**0.044****
OWNCON	**-.063**	**0.000*****
FSIZE	**.087**	**0.891**
LEVERAGE	**-.091**	**0.540**
R-squares	**0.0984**	
Prob> F, chi2	**0.000**	

** Significant at 5%. *** Significant at 1%.

4. Discussion

From the discussion in section two, there is no clear conclusion to be drawn on the impact of the family CEO on firm performance. Different studies conducted in various geographical locations have reached different results about the role of a family CEO in improved performance. Accordingly, the association between family CEO and financial performance is an open empirical issue needs further exploration. Based on the market measure (Tobin's Q) for family firms in table 5, the finding shows that family CEO has a negative significant impact on Tobin's Q. This result is consistent with other studies such as Barth et al. (2005), Bennedsen et al. (2007), Sonfield and Lussier (2009) and Pandey et al. (2011). Barth et al. (2005) suggested that the ownership and management of the firm by the same family may have a negative impact on the performance of the firm because they are too biased to choose managers from the family, where these managers may be ineffective and unqualified to fill managerial positions. Moreover, the involvement of family CEO in selecting board members provides an opportunity for the CEO to become more entrenched, regardless of his/her percentage of share in the firm (Morck et al., 1988). This situation can lead to a decline in the firm's productivity (Burkart et al., 2003).

Furthermore, according to Anderson and Reeb (2003) the founding family CEO positively affects the performance of a firm, but not with following generations of family CEOs. Bertrand et al. (2008) also investigated the impact of family CEO, including founder's son on firm performance, and found the negative effect of family CEO on performance, and this effect becomes worse when founder's son is CEO and the founder was dead. For that reason, we investigated the company's annual reports and found that most CEO positions are held by founder's son in the context of listed family companies in Jordan (Saidat et al., 2019)

With respect to accounting measures (ROA), the findings also show that the coefficient signs are negative but insignificant between family CEO and corporate performance. The negative relationship between family CEOs and firm performance measured by ROA is in line with agency theory which argues that family CEOs can lead to agency problems between majority and minority shareholders. According to agency theory, family CEOs may expropriate minority shareholders' interests by using their power to preferentially benefit the interests of their family (Burkart et al., 2003; Lansberg, 1983). Therefore, a possible explanation for this result may be that in Jordan, investors realise that family members hold the CEO position as part of family's excessive control over the company and therefore react negatively to the situation.

Furthermore, Table 5 clearly shows a positive significant relationship between CEO duality and Tobin's Q in the family firms. This finding is consistent with the view that firms in which the CEO and Chairperson roles are combined. Such firms are more likely to have better efficient governance mechanisms, which should contribute to improved performance. Conversely, however, when performance is measured by ROA, the result shows an insignificant relationship between CEO duality and corporate performance. It can be also observed from Table 5 that the OWNCON coefficient is negative and highly significant in relation to the Tobin's Q performance measure. However, a similar relationship is not significant when corporate performance is measured by ROA. This might be explained by DeAngelo and DeAngelo (2000), who argued that when most of firm shares are owned by family, it motivates them to pursuit their own interests rather than the interest of the firm, at the expense of minority shareholders, and thus the poor performance of these firms.

Conclusion

The main motivation of this study was to understand the impact of family involvement in one of the most important developing countries in the Middle East, Jordan. Knowledge of family firms and corporate performance has mostly been derived from a large volume of research conducted in developed countries, with very little coming from developing countries. Therefore, it is important to know how appointed family members at top position such as CEO work in different companies, especially those controlled by the hands of families. Therefore, the main objective of the study was to examine the relationship between family CEO and financial performance of family firms in Jordan as one example of developing countries. The study found that family CEO both in term of Tobin's Q and ROA has a negative relationship with the performance of family firms. In addition, we found some evidence for a relationship between performance and CEO duality in family firms. The results support the view that CEO duality is important for family firm performance. Our results also show that ownership concentration has a negative correlation with corporate performance as measured by Tobin's Q and ROA. Main limitation of this paper is that the sample period ends in 2015. Al-Htaybat et al. (2011), investigated listed Jordanian companies to explore the current status of corporate online reporting. They reported that approximately 36% of Jordanian listed companies were without accessible and active websites. For this reason, this study used data for the period 2009 to 2015, while future research could include later periods.

Acknowledgement

The authors are grateful to the Middle East University, Amman, Jordan for the financial support granted to cover the publication fee of this research article.

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