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Does family firm have better performance? empirical research in indonesia smes

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Abstract

Small and Medium Enterprises (SMEs) have an essential and strategic role in national economic development. SMEs are proven to be resistant to the financial crisis and absorb part of the workforce in Indonesia. This study examines whether SMEs family firm and diversification have better performance. The research sample was 114 SMEs owners in the Special Region of Yogyakarta. The results of the study prove that SMEs family firm and SMEs that diversify have better performance. The results of this study are expected to provide advice to SMEs owners that family businesses can be expanded through diversification to increase business value.

Keywords: Family ownership; diversification; SMEs performance

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INTRODUCTION

Small and Medium Enterprises (SMEs) have an essential position, especially in economic growth throughout Indonesia. Most companies in Indonesia are micro and small enterprises. SMEs play a role in driving the pace of economic growth after the monetary crisis that occurred in the period 1997 to 1998 when large companies experienced difficulties in developing their businesses. Only the SMEs sector remains strong and contributes revenues significantly to it and to the State of Indonesia, Suci (2017).

Based on the type of the owner, SMEs ownership mostly has similarity if compare to the large companies. It can be categorized into two types, namely family and non-family firm. Family ownership can be described by either purely family ownership or a combination between family and corporation. While non-family ownership usually described by single ownership or corporate ownership. The different types of SMEs ownership will impact on the differentiation of strategy, risk management, decision making and performance achievement, Sunarjanto, Roida, & Christiana, (2013).

This study will examine the relationship between family ownership, diversification, and SME performance. This study examines family ownership because the majority of SMEs are owned and managed by families. Family firm especially SMEs, the roles of which can be seen both directly and indirectly. Direct involvement can be seen by the participation of family members in business planning, while indirect involvement can be seen by the proportion of ownership in the capital participation, Tjantoko (2014).

The importance of family involvement is not the only reason to survive, expand market share and increase competitiveness, SMEs can diversify their business to realize it (Baptista, Karaöz, & Leitão, 2012). Business diversification is an effort to expand the business by increasing the number of segments either by adding business units or expanding business units or increasing the market share that has been owned and developing a variety of products (Sumendap, Tommy, & Maramis, 2018). In terms of business dynamics, entrepreneurs in small industries usually diversify their business in terms of raw materials and production output. Business diversification in SMEs can be divided into two types, the stable diversification which do the same diversification like the previous business and the unstable diversification, Hamid & Susilo, (2011). In the family business, second-generation successors tend to expand family businesses through diversification to increase business value, Weng & Chi, (2019).

Many research has attempted to link the performance of SMEs with other variables such as information technology, Chang, Yen, Ng, & Chang, (2012); Budiarto, Prabowo, & Herawan, (2017), accounting Ismail & King, (2014), Ediraras, (2011); human resource competency, Dubihlela & Rundora, (2014); Ardiana, Brahmayanti, & Subaedi, (2010); Entrepreneurial orientation and business networking capabilities, Keh, Nguyen, & Ng, (2007; Lukiastuti, (2012); Enterpreneur Keh et al., (2007); Naranjo-Valencia, Calderón-Hernández, Jiménez-Jiménez, & Sanz-Valle, (2018); Sari, (2014). Although research on the performance of SMEs has been extensively studied, this research is still interesting because: First, the successfull of family businesses, especially in SMEs, can be measured through strategic policies, one of them is diversification Weng & Chi, (2019). Second, work commitments from family members are higher than non-families in contributing ~~to~~ the economic's growth, Gozali, (2014). Third, when compared to other countries, the performance of SMEs in Indonesia is still low (Tahi Hamonangan Tambunan, (2011). Fourth, most of Indonesian SMEs run their business traditionally with low productivity levels T. Hamonangan Tambunan (2011); McKague et al., (2011).

Literature review

SMEs

Small and Medium Enterprises (SMEs) in Indonesia have different meanings. According to Indonesian Law Number 20/2008 about Small and Medium Enterprises, the definition of SMEs is a productive businesses owned by individuals or business entities that have met the requirements of small businesses. The requirements for SMEs are having less than 50 million net assets, less than 300 million turnover for micro businesses and less than 500 million for small businesses. The Central Bureau of Statistics provides the definition of SMEs based on the number of workers in each category. For small businesses are a kind of business entities that have 5 to 19 employees, while medium companies are business entities that have 20 to 99 employees.

Family ownership

Companies that are purely owned by the public only exist in several major countries, in developing countries including Indonesia, most companies are owned by their family. A family company is a company consisting of 2 or more family members who oversee the company's finances (De Pontet, Aronoff, Mendoza, & Ward, 2012). It said to be a family firms if the family dominates the equity or management and control (Kraus, Pohjola, & Koponen, 2012). The reason is the family is one of the crucial factors in business because of the social capital. Another factor that drives the success of a family business is the support of an information network built by family members. Many SMEs, especially owned by families, put their family members to the top management position, while employees who are not family members put in the bottom level of management. It has an aim to ensure the business continuity (Gozali, 2014).

Diversification

Business diversification is a form of business development by expanding the number of segments both business and geographical. Companies can also do diversification by increasing their existing market share or developing various products (Sumendap et al., 2018). The diversification strategy used by company is likely can increase the complexity of the problem, especially in the structure of ownership and control of the organization. The complexity of these problems causes businesses that have a lot of diversifications face a higher risk of failure. However, many companies continue to diversify because they already have large capital with higher income levels which predicted before (Lucyanda & Wardhani, 2017).

SMEs performance

Organizational performance is an accumulation of the performance of all members in the organization and is a means for companies in the process towards corporate goals. There are 4 leading causes of low production of small and medium enterprises in Indonesia: 1) Nearly 60% of small businesses still use traditional technology; 2) Market share tends to decrease due to the lack of capital, weak technology and managerial; 3) Most small businesses are unable to meet administrative requirements to obtain assistance from the Bank; 4) The level of dependence on government facilities still huge. SMEs that succeed in overcoming the above problems are likely to have an excellent or positive performance, but those who do not realize will experience negative performance. Positive performance means the company can achieve its objectives, while negative performance suggests that the company cannot meet its objectives (Ardiana et al., 2010; Purnomo & Lestari, 2010).

Hypothesis development

Family companies have control of company activities and can increase company value. Families who have large enough shares can do an interest that aims to reduce conflicts that occur so that it can increase the companies value (Anderson & Reeb, 2003). Family members resources can also reduce labor from outside the organization. Family ownership will encourage managers of family businesses to work better because the success of the strategies will contribute significantly to the success of the organization (Kim & Gao, 2013).

A family company has self-actualization, so the organization's manager will run his business correctly because he feels like the owner. In the family firms, the manager will have a variety of relevant information that will be announced to all parties to prevent asimetry information between the owner and the manager as a family member. Family ownership will reduce moral hazard actions from managers who act deviate from the initial interests of the company. A concentrated family ownership will reduce fraud's tendencies committed by the manager so that the owner being helpful by its condition. Because of the family ownership, all corporate strategies can be controlled to minimize strategy errors/failures that have a negative impact on the company's performance (Anita, Kirmizi, & Savitri, 2018). Based on previous research findings, the following hypothesis is proposed:

H_1: SMEs family firms have better performance than non-family firms

SMEs can survive long in the environmental uncertainty by diversifying products, geographical markets or knowledge (Delbufalo, Poggesi, & Borra, 2016). Empirical evidence states that companies with a tremendous level of idle financial condition tend to choose diversified technology resources (Alliance, Acquisition) in response to poor innovative performance (Carnes, Xu, Sirmon, & Karadag, 2019; Choi, Lee, & Bae, 2019). Family firms may have significant effects on general strategic decisions and diversified choices in particular such as product and geographical diversification (Muñoz-Bullón & Sanchez-Bueno, 2011).

The diversification strategy allows SMEs to exploit the company's ability to expand the company's core industry product lines, generate benefits from the business scope and create existing market opportunities (Pangboonyanon & Kalasin, 2018). Diversified companies have lower average capital costs than stand-alone companies (Hann, Ogneva, & Ozbas, 2013). Besides, diversified companies perform better (Shen, Au, & Yi, 2018). The hypotheses to be tested are as follows:

H_2: Diversified SMEs have better performance than non-diversified

METHOD

The population of this study is all active SMEs owner in the city of Yogyakarta in 2018. The sampling technique used is purposive sampling which are selected according to predetermined criteria. The criteria are:

Respondents (samples) are the SMEs owners/managers;

According to Indonesian's Law No. 20 of 2008, the number of employees are less than 10 for micro, less than 30 for small businesses and less than 300 to medium-sized firms.

There are 125 questionnaires were distributed, with 91.2% return rate. There are 114 returned questionnaires which could be used as research analysis.

Table 1. Description of Respondents

		Sleman	Kulon Progo	Gunung Kidul	Bantul	Yogyakarta	Total
Size	Micro	20	27	22	22	13	84
	Small		2	2	3	1	8
	Medium			1		1	2
Ownership	Non-family	9	3	3	17	7	39
	Family firms	11	26	22	8	8	75
Diversification	Diversified	8	24	6	12	7	57
	Not-diversified	12	5	19	13	8	57
Type of business	Retail	2	8	21	12	8	51
	Services		2	3		2	7
	Kraft	1	4		11	1	17
	Food	17	15	1	2	4	39
Age of business	<3 years	2	8	2	3	5	20
	4-10 years	17	13	10	12	6	58
	11-20 years	1	5	6	9	2	23
	>21 years		3	7	1	2	13
Number of employees	<10	20	24	25	23	12	104
	11-30		4	3	2		9
	31-99		1				1
Owners Education	Elementary school	1	1	5	4		11
	Junior High shool	4	4	3	3	1	15
	Senior High school	14	17	11	11	6	59
	Bachelor	1	7	6	7	8	29

Variable measurement

The variables used in this study are the SMEs performance as measured by 6 question indicated: the way of business, profitability, success, growth, business development and market share (Radzi, Nor, & Ali, 2017). Respondents will answer six items of questions and measured by a Likert scale, with 1 (strongly disagree) to 5 (strongly agree). Family ownership is measured using categories, 1 for non-family firms and 2 for family firms (Chu, 2009). Diversification is measured using categories to indicate whether a company is diversified or not diversified. Type 1 is diversified firms and 2 for not diversified firms (Muñoz-Bullón & Sanchez-Bueno, 2011).

Table 2. Measurement of variables

Variables	Definition	Measurement
SMEs ownership	Family companies run from one generation to the next (Morck & Yeung, 2004;Cahyani & Sanjaya, 2017)	Non-family firms Family firms (Chu, 2009)
Diversification	Business diversification is a form of business development by expanding the number of segments in business or developing various types of products (Sumendap et al., 2018)	Diversified Not-diversified (Muñoz-Bullón & Sanchez-Bueno, 2011)
SMEs performance	Performance is the result of work that can be achieved by a person or group of people in the organization and is a determining tool for achieving organizational goals (Ardiana et al., 2010)	The way of business Profitability Success Growth Business development Market share (Radzi et al., 2017)

The test of instrument

Testing instruments in this study using validity and reliability tests. A valid questionnaire if the question in the survey can express something that will be measured by the questionnaire. Test the validity of using the Pearson correlation while the reliability test uses the Cronbach alpha (Ghozali, 2018).

Table 3. SMEs performance validity testing

No	Instrument	*Pearson correlation*
1.	I am happy with the way my business is operated	0.691**
2.	I am satisfied with the growth of net income of the business	0.756**
3.	I consider my business as successful	0.747**
4.	I consider my business as growing	0.771**
5.	My business will continue to expand in the future	0.729**
6.	The company's market share is growing from year to year	0.792**

** significant < 1%

Reliability is a tool for measuring a questionnaire which is an indicator of a variable. A questionnaire is said to be reliable if a person's answer to a statement is consistent or stable over time. (Ghozali, 2018). The results of the reliability test of the SMEs performance have a Cronbach Alpha value of 0.787.

Hypothesis testing and discussion

The aim of testing both of hypotheses is to examines SMEs performance differences based on family ownership and diversification strategies.

Table 4. Independent-sample t-test of family ownership

No	Instrumen t	Mean		*Lavene's test for equality of variances*	*P Value*
		Non-family firm	Family firm		
1	I am happy with the way my business is operated	0.423	0.431	0.015*	0.554
2	I am satisfied with the growth of net income of the business	0.385	0.428	0.435	0.000**
3	I consider my business as successful	0.359	0.413	0.457	0.001*
4	I consider my business as growing	0.390	0.424	0.956	0.012*
5	My business will continue to expand in the future	0.428	0.433	0.038*	0.681
6	The company's market share is growing from year to year	0.387	0.424	0.184	0.020*

* significant < 5% ,** significant < 1%

Based on table 4, it can be explained that family firms have a better performance than non-family firms. The most significant difference in instrument number 2 with an average value of 0.385 for non-family firms and 0.428 for family firms. The results of this study support previous research that family ownership has a strong motivation in conducting corporate supervision. Besides, the family workforce contributes more, and relatively little family capital compared to non-family companies that are comparable in improving company performance (Anita et al., 2018; Barbera & Moores, 2013)

Table 5. Independent-sample t-test of diversification

No	Instrumen t	Mean		***Lavene's test for equality of variances***	***P Value***
		Diversified	Not diversivied		
1	I am happy with the way my business is operated	0.440	0.416	0.779	0.042*
2	I am satisfied with the growth of net income of the business	0.428	0.398	0.147	0.006*
3	I consider my business as successful	0.421	0.368	0.001*	0.000**
4	I consider my business as growing	0.433	0.391	0.720	0.001*
5	My business will continue to expand in the future	0.449	0.414	0.577	0.003*
6	The company's market share is growing from year to year	0.430	0.393	0.055	0.014*

* significant < 5% ,** significant < 1%

Based on table 5, it can be explained that there are differences in performance based on diversification. Diversified companies have better performance than companies that are not diversified. In question number 3 about the success of a business in the future, the mean value of a diversified company is 0.421 higher than a non-diversified company. The results of this study state that family businesses can be expanded through diversification to increase business values, Weng & Chi, (2019).

CONCLUSION

Based on the results of data analysis conducted, it can be concluded that SMEs family firms and diversified SMEs have better performance. This study has several limitations; first, this study does not divide whether SMEs family firms are managed alone or run by others. The self-managed family business can be done by transferring embedded values as a family culture, but differences in managerial mindset between the first generation and the next generation can be prolonged conflicts within the family, Simanjuntak, (2011). Second, this study does not consider succession based on generations. Given the second generation is more aggressive in pursuing diversification strategies to reduce uncertainty in the economic environment, Weng & Chi, (2019). Third, this study does not test the type of diversification whether it is still one line or different from the primary business. Companies that run a business diversification strategy with multi-segments have lower excess value than companies that only have one business line so that they have not provided optimal results on company performance, Kurniasari & Tahun, (2013).

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