Indonesian Family Business vs. Non-Family Business Enterprises: Which has Better Performance?

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Abstract

There are numbers of family business listed in Indonesia Stock Exchange but there are not much of researches that can show how well they perform in generating profit. This research elaborates the performance of family businesses that are listed in Indonesia Stock Exchange from 2006 to 2010. This is important because during that period there is a global recession in 2008 and this occurrence provide information on how well the company sustain their business. This also shows how the family company manages to gain profit.This research uses return on equity, return on assets, net profit margin, and basic earning power as proxy profitability. Each ratio indicates the performance of the company from several different points of views. However, it is also important to consider the company's ability in generating profit from their activity. Hence, it is important also to consider the activity ratio from several perspectives such as total assets turnover, inventory turnover, and fix assets turnover. The results indicate that in Indonesia non family companies perform and sustain better than family companies.

Keywords: *Indonesian Family Business, Profitability Ratio, Activity Ratio*

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1. Introduction

Global recession on 2008 has directly and indirectly affected every industry in all over the world including Indonesia. The direct impacts that Indonesia encompassed in every industry were the depreciation of Rupiah value towards US Dollar and the rise of inflation on goods and services (www.setneg.go.id). While the indirect effect to Indonesia industry was the fall in the number of exports due to the decrease in demand in several countries such as United States of America and in the European countries (www.bi.go.id). In Indonesia, most of the companies are owned by family or individual. The global recession has also influenced them in terms of selling and buying due to the fall in demand and the depreciation of Rupiah value. The exporters were cutting their production due to the decrease number of orders, while the importers have to struggle for the rise of material or product cost which they had to buy (Akhmadi et. al, 2011).

However, several researchers in several countries found that family business has the ability to sustain crisis and perform better than non family business. While in Indonesia, there are hardly any published scientific research that describes the performance between family and non-family business. In India, Sindhuja (2009) made a research and found that not all performance indicators in favor of family managed business, most of the others were in favor of non family managed business. Different results presented by Allouche, Amann, Jaussaud, and Kurashina (2008) in Japan. They found that in overall family business has better performance than non family business. Westhead and Cowling (1997), on the other hand, present different finding from their research in United Kingdom. They found that there were no significant performance differences between family businesses and non family businesses. Rettab and Azzam (2011) found their result quite interesting in Dubai. Their research was based on the industry that the family business operates. They found that family business was better than non family business in trading and in construction industry, but weaker in manufacturing and service industry. The Indonesia's well known business magazine, SWA, made a deep interview with ten top management which also the owner of family companies. The interview is conducted to explore the strength and weaknesses of family companies, such as:

Table 1.: Strength and Weaknesses of Family Companies

STRENGTH	%	WEAKNESSES	%
1. Strong (long term) vision	80	1. Potential conflict	66.7
2. There are family values as a guidance and to unite	80	2. Lack of planning	44.4
3. The strong feeling of belonging among the family members	70	3. Lack of management system	44.4
4. Easy to communicate and can be done informally	70	4. Only rely on the family figures	11.1
5. Easy to control	60	5. Hesitation in the family	11.1
6. Easily in early detection of family members capability	50	6. Personal emotions involved in job decision	11.1
7. Lean and agile bureaucracy	30	7. Hard to control family members	11.1
8. Understand every family members' interest	10	8. Centralist tendency	11.1

Source: SWA Magazine, March 2011 Edition

Based on that, this research intended to find the comparison of performance of family companies with non family companies in Indonesia especially their performance before and after the global crisis.

2. Literature Review

Many researches on family business describe the definition of family business as a research guideline. They argued that defining family business will determine the result of the analysis (Westhead and Cowling, 1998). This research uses family business defined in Sindhuja (2009) research, such as:

- The company is managed by members from a single dominant family group.
- There is a single dominant family group owns more than 50% of the shares of the company.
- The members of the family in the company perceived the company as a family business.
- There is a successor from the family member in the company or managed by the family's successor.

- The management is consists of main family members.
- The executives of the company held by family members.

Other research describe family firm if it is controlled by its founders, or by the founders' families and their heirs (Burkart, Panunzi, and Shleifer, 2003). Donnelley (2004) added that an organization is called family company if there are at least (must have) two generations in the family are involved and have decision power in influencing company's policy. This research uses the definition to determine the samples of this research.

Since this research aimed to explain the differences in performance between family business and non family business, defining the company's performance is also crucial in this research. Previous research uses many different types of performance measurement to determine the differences between family and non family business. Each type of performance measurement denotes different perception. Westhead and Cowling (1997) uses sales, net profit, profitability, productivity, exports, and employment to associate with company's performance.

Different proxy presented by Rettab and Azzam (2011) by using exports, paid-up capital, and number of employees to measure performance. While Allouche *et al.*(2008) uses return on assets, return on equity, return on invested capital, total debts to total capital ratio, long-term debt to total capital ratio, current ratios, and quick ratio. Sindhuja (2009) uses more variables to measure performance, such as Tobin's Q ratio, compound annual growth rate of the total assets, return on assets, return on net worth, return on capital employed, profit margin, sales turnover, earning per share, market capitalization, net operating profit after tax, debt to equity ratio, and net worth.

Among several performance ratio used by previous researchers, Du Pont analysis is considered as the most suited analysis to analyze company's financial performance (Listiadi, 2007). By using Du Pont analysis, it can explain how the companies can perform and how do they differ between one and another. Return on assets explains how a company generates profit from the amount of assets they invested. Smith (2008) uses return on assets (ROA) as the only indicator to measure profitability found that in Australia and Belgium, in most industry, there are no significant differences between family and non family businesses. However, using only ROA to represent profitability is not enough. In order to describe how the company able to generate profit for the equity holder, return on equity (ROE) should be used. ROE can also be used to understand the amount of equity and liability to generate profit when it is compared to ROA. When the value of ROA is more than half the value of ROE, this indicates that the company uses liability more than equity to generate profit (Helfert, 2001).

Basic earning power (BEP) is a ratio to indicate the ability of a company to pay the amount of interest imposed from the number of debt borrowed. This ratio is useful for the creditor to estimate the ability of the company to pay the interest. It also indicates the ability of a company to generate profit for the investors before it is imposed by tax and interest. This ratio is useful to compare companies from different industries, because different industries might have different tax rates or interest rates. Net profit margin (NPM) on the other hand is useful in comparing companies in the same industry. NPM indicate the level of expenses that the companies generate in creating their profit. This indicates their effectiveness in productivity in reducing costs (Sindhuja, 2009; Helfert, 2001).Total assets turnover (TATO) indicate the effectiveness of a company in generating sales from the assets used. Previous researchers use TATO to explain further on how the companies generate profit. Such researchers are Sindhuja (2009) which found that non family managed businesses has better TATO than family managed business, and Westhead and

Cowling (1997) found no significant difference in TATO between family companies and non family companies. Fixed assets turnover (FATO) on the other hand is not a commonly used ratio to describe the activity performance. Hence, it indicates the ability of a company in utilizing the machines, plants, land, and other fixed assets to generate profit. If the value of FATO is not much different with TATO, then the company is too costly in generating profit (Helfert, 2001; Brigham, and Houston, 2007).

3. Hypothesis Development

Based on the previous research method of determining performance, this research develops several hypotheses to answer the topic of this research. Since there is several ways to proxy performance, this research decided to use profitability ratios and operating ratios to measure performance. Profitability ratios and operating ratios are related to each other and can describe the source of profit that the company generates. Profitability ratios that most suit to describe company's performance and commonly used by investors to measure performance are return on equity (ROE), return on assets (ROA), basic earning power (BEP), and net profit margin (NPM). This ratios will the determine the profitability performance of the company as it is used by previous research partly in Sindhuja (2009), Allouche *et al.*(2008), and Westhead and Cowling (1997). Therefore the first hypothesis is:

H_1 : Family business is more profitable than non family business

Operating ratios help to describe how the company performs in generating profit. Such as total assets turnover describes how the company utilize their assets to generate sales, while fixed assets turnover describes the effectiveness of the company in operating its production to generate profit (Brigham and Houston, 2007).

H_2 : Family business is more effective in operating the company than non family business

The economic condition can directly affect company's performance. The economic crisis in 2008 has decrease the growth of Gross Domestic Product in several sectors of industry. This can be seen from the Indonesia Central Statistic Bureau (BPS) year 2008 and 2009 that most of the industry does not grow as the good as the previous years (www.bps.go.id).

H_3 : The family business's profitability sustain better two years before and two years after 2008 than non family business

H_4 : The family business's operation sustain better two years before and two years after 2008 than non family business

4. Research Methodology

The samples are the family companies listed in Indonesia Stock Exchange and have financial report from 2006 to 2010. The criterion of the family companies is as mentioned in the literature review, while the non family companies are selected according to the family companies' type of industry and the most profitable company in the industry. The reason is to have a comparison between the best family companies and non family companies in the industry. The method use to calculate the differences between family and non family companies' performance is T test. T test is the best way to calculate the difference between two groups when the two groups have the same number of samples (Lind, Marchal, and Wathen, 2008).

5. Results

Based on the criterion of the family company, this research has selected twenty two family companies and another twenty two non family companies from nine different industries. The T test made to the performance ratio found that ROA between family and non family companies are negatively significant. From the mean comparison, the mean of family companies ROA (5.1) are lower than non family companies ROA (10.2). On the other hand, the difference between family companies ROE and non family ROE are found to be negatively significant at 10% confidence. Family companies' mean of ROE (11.1) are indicated to be lower than non family companies' mean of ROE (17). In contrast, NPM of family companies is found to have no significant difference in mean with non family companies (sig. >10%) even though the mean comparison indicates non family companies' mean of NPM (8.7) are greater than family companies' mean of NPM (8.1). While the mean of BEP between family companies and non family companies are found to be negatively significant. The mean of BEP in non family companies (15.4) are much higher than family companies' (10.3). Based on that result it can be concluded that in general profitability of non family business is better than family companies'. Therefore the first hypothesis that stated "Family business is more profitable than non family business" is rejected.

Table 2. T test Results of Profitability Ratio

		Mean	t	Sig. (2-tailed)
Pair 1	ROA fam	5.0730	-4.145	0.000
	ROA non	10.1814		
Pair 2	ROE fam	11.0675	-1.915	0.058
	ROE non	16.9545		
Pair 3	NPM fam	8.1127	-0.371	0.711
	NPM non	8.7051		
Pair 4	BEP fam	10.3399	-2.915	0.004
	BEP non	15.4408		

Source: Processed Data

The activity ratios also found to have the similar results as the profitability ratios. The mean of TATO between family and non family companies are found to be negatively significant (sig.< 5%). Family companies' mean of TATO (0.9) is much lower than non family companies' mean of TATO (3.7). The same results are shown in FATO that the mean difference between family and non family companies are negatively significant (sig.< 5%).

Table 3. T test Results of Activity Ratio

		Mean	T	Sig. (2-tailed)
Pair 5	TATO fam	0.9309	-2.915	0.033
	TATO non	3.6842		
Pair 6	FATO fam	3.9563	-3.233	0.002
	FATO non	11.2195		

Source: Processed Data

These results also indicate that the second hypothesis that stated "Family business is more effective in operating the company than non family business" is rejected and null hypothesis is accepted. The results of non family companies' profitability ratios that outperformed family companies' profitability ratios might be caused by the activity ratios that also indicate that non family companies perform better than family companies. However, all the t values are negative which indicate that family companies' performance statistically has negative relationship with non family companies. The family companies' profitability performance before 2008, in 2006 and 2007, indicate that in overall is lower than non family companies' profitability performance. This can be seen from the profitability ratio where the mean of ROA between family and non family companies is negatively significant (sig.< 5%).mThe mean value of ROA of family companies (5.1) is lower than non family companies (9.0). Different results indicated in ROE mean, based on the t test there are no significant difference in mean between family companies and non family companies (sig.> 10%) even though the mean value of non family companies (18.2) is greater than family companies (9.6).

The similar results indicated in NPM mean (sig.> 10%) where there are no significant difference in mean of NPM between family companies and non family companies. The value of NPM mean of family companies (9.9) lower than non family companies (10.8) even though they are insignificant in difference. However, the mean of BEP between family and non family companies are negatively significant (sig.< 5%). The mean values of BEP of non family companies (14.9) are much higher than family companies (7.7).

Table 4. T test Results of Profitability Ratio Before 2008

		Mean	T	Sig. (2-tailed)
Pair 1	ROA fam	5.0655	-2.297	0.027
	ROA non	8.9248		
Pair 2	ROE fam	9.6268	-1.535	0.132
	ROE non	18.2305		
Pair 3	NPM fam	9.8514	-0.560	0.578
	NPM non	10.8407		
Pair 4	BEP fam	7.7223	-3.177	0.003
	BEP non	14.9393		

Source: Processed Data

Different results found in companies' profitability performance after 2008, in 2009 and 2010, which most of the profitability ratios indicate that there are no significant difference between family companies and non family companies especially in NPM, BEP, ROE, and TATO (sig.> 10%). While the differences of ROA mean and FATO mean between family companies and non family companies is found negatively significant (sig.< 5%). The values of mean of non family companies are higher than family companies.

The ROA mean value of non family companies is 9.3 higher than family companies mean value which is only 5.9. While the FATO mean value of non family companies is 9.9 much higher than family companies which only 4.6.

Table 5. T test Results of Profitability Ratio After 2008

		Mean	T	Sig. (2-tailed)
Pair 1	ROA fam	5.8982	-1.932	0.060
	ROA non	9.3116		
Pair 2	ROE fam	13.8286	-0.786	0.436
	ROE non	17.0686		
Pair 3	NPM fam	7.7798	-0.126	0.900
	NPM non	8.1605		
Pair 4	BEP fam	14.3214	-0.423	0.674
	BEP non	15.6461		

Source: Processed Data

Based on the results of the companies' profitability performance before and after 2008, in overall results it can be concluded that it rejects the third hypothesis which stated that "The family business's profitability sustain better two years before and two years after 2008 than non family business ". Based on the mean values of the profitability ratio between 2006 and 2010 it is found that most of the values fall in 2007 to 2008 except ROA and BEP of non family companies which increases in its value in 2007 to 2008. The opposite effects occurred in 2008 to 2009 where most of the profitability means values are increasing except ROA and BEP of non family companies.

The activity ratios also indicate similar results with the profitability ratios. FATO ratio in 2006-2007 periods and 2009-2010 periods found to have negative significant difference in means value. While TATO ratio of family and non family companies found to have insignificant difference in the mean value in the period two years before and after 2008 (sig.> 10%).

Table 6. T test Results of TATO Before and After 2008

		Mean	T	Sig. (2-tailed)
Before 2008	TATO fam	0.8684	-1.498	0.141
	TATO non	3.9989		
After 2008	TATO fam	0.9811	-1.259	0.215
	TATO non	2.6095		

Source: Processed Data

FATO ratios of non family companies in 2006 to 2007 period is 11.5 much higher than family companies which only generate 3.5 in mean value. In addition, the similar effect occurs in 2009 to 2010 where the non family companies generate 9.9 FATO mean value higher than 4.6 generated by family companies.

Table 7. T test Results of FATO Before and After 2008

		Mean	T	Sig. (2-tailed)
Before 2008	FATO fam	3.4634	-2.203	0.033
	FATO non	11.4641		
After 2008	FATO fam	4.5945	-1.916	0.062
	FATO non	9.8684		

Source: Processed Data

In overall the activity performance of the family and non family companies are quite different. From the mean values of TATO and FATO throughout the years, the family companies found to fall in 2007 and rise in 2008 to 2010. While non family companies indicate that the mean value of TATO and FATO increases in 2006 to 2008 and decreases in 2008 to 2009, then increases again in 2009 to 2010.

Based on the result of the activity ratios, it can be concluded that the forth hypothesis is rejected and the statement “The family business’s operation sustain better two years before and two years after 2008 than non family business” is not quite true. Therefore, in overall non family companies perform better than family companies.

6. Conclusion and Recommendation

In summary, non family companies outperformed family companies both in making profit and in operations in Indonesia. This research results support part of the Sindhuja (2009) findings and contradicts with Allouche, Amann, Jaussaud, and Kurashina (2008), Westhead and Cowling (1997), and Rettab and Azzam (2011) findings. One of the strong reasons is TATO and FATO of non family companies is much better than family companies. This implies that the effectiveness in utilizing the company’s assets to generate profit is much better in non family companies than in family companies.

Moreover, the differences between TATO and FATO of non family companies are much wider than family companies. This implies that the use of fixed assets by non family companies is less than the family companies. This indicates that family company is not as efficient as the non family companies are.

In general non family companies sustain better than family business. However, only in activity ratios that family companies that indicate an increase in 2008 to 2010 period even though the fourth hypothesis is rejected. It is recommended that in future research that in comparing between family and non family companies, not only should be based on the type of industry but also the size between the companies should be the same. This might reduce the biases in comparing family with non family companies.

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