

Family-Sponsored Ventures

The Entrepreneurial Advantage Of Nations:
First Annual Global Entrepreneurship Symposium

United Nations Headquarters
April 29, 2003

Joseph H. Astrachan, Ph.D
Shaker A. Zahra, Ph.D
Pramodita Sharma, Ph.D

Family-Sponsored Ventures

Joseph H. Astrachan, Ph.D., Kennesaw State University
Shaker A. Zahra, Ph.D., Babson College
Pramodita Sharma, Ph.D., Wilfrid Laurier University, Canada

In 1999 the Global Entrepreneurship Monitor (GEM) program was initiated by Babson College and London Business School with sponsorship from the Kauffman Foundation to:

- Measure differences in the level of entrepreneurial activity between countries.
- Probe for a systematic relationship between entrepreneurship and national economic growth.
- Uncover factors that lead to higher level so of entrepreneurship.
- **Suggest policies that may enhance the national level of entrepreneurial activity.**

Data were assembled for each participating country from four basic sources: 1) surveys of over a hundred thousand adults; 2) in-depth interviews with almost a thousand national experts on entrepreneurship; 3) standardized questionnaires completed by the national experts, and 4) a wide selection of standardized national data from such sources as the World Bank, International Monetary Fund, United Nations and the like. The 37 countries participating in 2002 provides a truly global assessment of these issues.

The Kauffman Foundation and the Business Council for the United Nations recently convened the first international policy discussion related to these issues at The Entrepreneurial Advantage of Nations: The First Annual Global Entrepreneurship Symposium. Held at the U.N. Headquarters, the symposium featured various experts who explored the social, financial, educational and demographic underpinnings related to the creation and support of national entrepreneurial activity.

The enclosed report provide an analysis of one of the four special topics addressed at the symposium: patterns of female entrepreneurship, sources of financial support, high-potential entrepreneurship, and the prevalence of family-sponsored new ventures. These reports provide new and more precise information on these issues, which should enhance the effectiveness of relevant government policies.

Introduction

Family-sponsored business ventures – those owned and managed by families or groups of relatives -- dominate the economic landscape of the world, simultaneously fostering economic growth and social stability. Because so many of these ventures are new and growing businesses, examining the role of family sponsorship is important in understanding entrepreneurial processes.

With the support of the George and Robin Raymond Family Business Institute, researchers with the Global Entrepreneurship Monitor project conducted a pretest in 10 of the GEM 2002 countries. Businesses operating in countries with varying developmental levels -- Australia, Brazil, Hungary, Israel, New Zealand, Singapore, Spain, Sweden, the United Kingdom and the United States -- were surveyed so as to allow the examination of findings across a diverse sample.

The GEM Family-Sponsored Ventures research was intended to:

- ◆ Estimate the number of new firms that are controlled by families.
- ◆ Study the characteristics of new family firms.
- ◆ Estimate the level of family financial sponsorship of new firms.
- ◆ Determine future research issues.

In this report, findings from the GEM Family-Sponsored Ventures research are examined alongside results of other studies to develop a multifaceted perspective on how family sponsorship contributes to entrepreneurship and what policies may be advisable to support the success of family-sponsored ventures.

Families and business: A winning mix

Family businesses possess a unique and winning combination of social, human, and financial capital that equips them to foster the economic and social health of nations. Family firms' unique structures, governance, and cultures enable them to take the risks necessary to create new business and pursue growth, thereby generating employment for relatives and non-relatives alike. Research provides a strong indication that these trends are likely to continue.

Though some family firms experience serious problems in managing the transition from the founder to other family members, many survive for generations -- creating a stable source of economic, technological, and social progress and a stable base of long-term capital needed for new venture development. As these firms exist primarily on a local level, they also provide for community investment and overall social stability and welfare.

GEM data show that 25 million new family firms were created in 2002. Findings also show just how involved families are in the entrepreneurial process. Table 1 illustrates that 63 percent of ventures now in the planning stages will be launched with family funding, while 85 percent of all established ventures start with some level of family backing. (See also *The Important Role of Family Firms in Financing Entrepreneurship*.)

**Table 1. Distribution of Businesses With Family Venture Backing:
10 GEM 2002 Countries**

	Start-ups	New firms	Established firms
Number of cases	1,425	1,594	3,743
Family-sponsored ventures	63%	76%	85%

In this study, it is assumed that family businesses are those in which a family holds more than 50 percent and those in which a single majority owner shares ownership with his or her family.

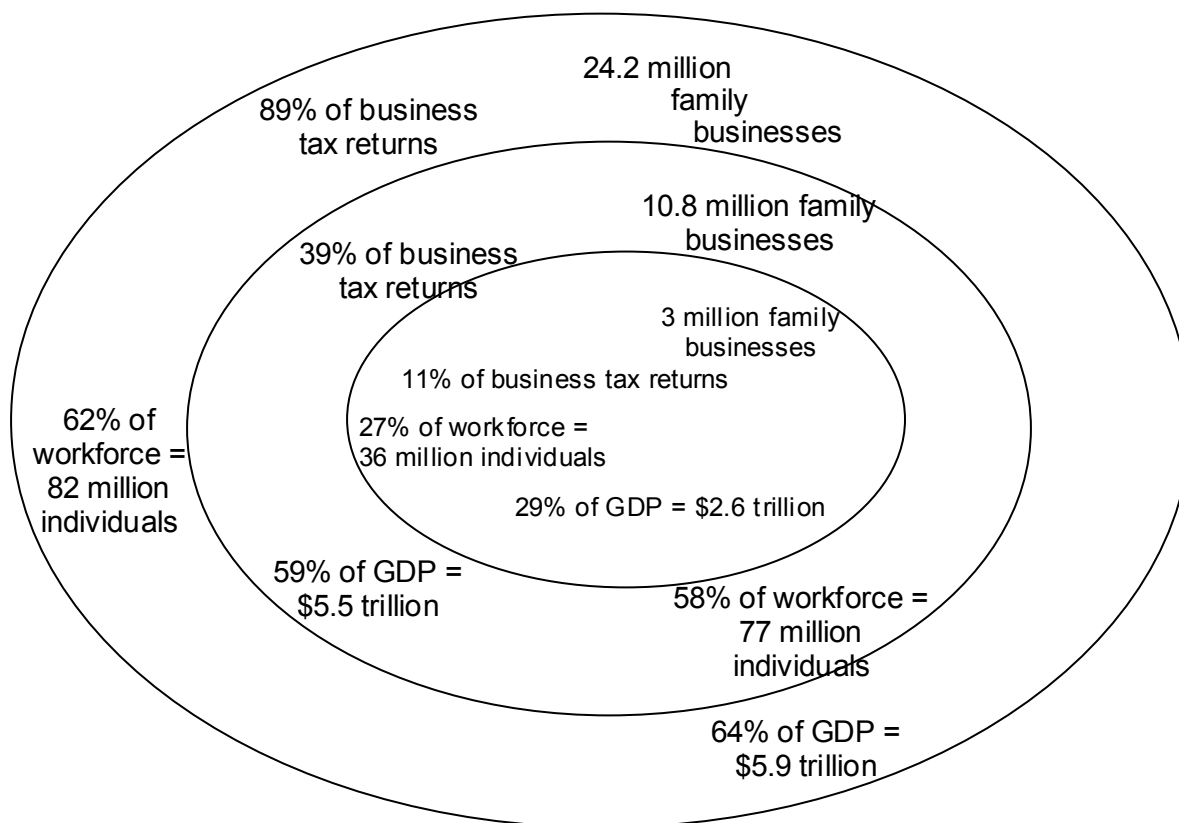
Further defining the family-sponsored venture: The epicenter of the world economy

In addition to the GEM definition of a family-sponsored venture, other researchers have developed definitions to describe several levels of family engagement and their contributions to the larger economy.

In the United States, as many as 90 percent of all existing companies – some 24 million – may be considered family owned or controlledⁱⁱ (Astrachan and Shanker, 2002). These family businesses certainly constitute the overwhelming majority of micro-enterprises.

Astrachan and Shanker propose three definitions of “family business.” Their broadest definition, represented in the outermost ring of Figure 1, includes businesses where the family controls the firm’s strategic direction and participates in running the firm. Their middle definition applies to firms where the founder or founder’s descendant runs the firm and intends to keep the family in control. The narrowest, more conservative definition includes only family firms in which multiple generations participate in the business, where more than one member of the owner’s family has management responsibility, and where multiple generations of family owners and employees hold controlling ownership.

Figure 1. Family Business' Contribution to the U.S. Economy ("Bull's Eye")



In further verifying the vital role of families in entrepreneurship, GEM data largely confirm other research. For example, the 1997 American Family Business Surveyⁱⁱⁱ found that more than 9 million families own businesses in the United States, with one out of every 10 households owning at least one business^{iv} (Heck and Stafford, 2001). Research conducted in Asia, Europe, and South America has revealed a similar prevalence of family firms.

Worldwide, a similar pattern exists. Through a cascade of ownership structures, family firms control the vast majority of national economies in multiple regions of the globe. These firms may be connected through cross-ownership as well as personal and professional ties, providing community and local stability while also facilitating cross-border collaboration.

The distribution of family ownership, however, varies substantially by country. In Table 2, GEM data show that families on average own 75 percent of businesses – ranging from 85 percent in Brazil to 51 percent in Sweden.

Brazil	Hungary	United Kingdom	New Zealand	Israel	Australia	United States	Singapore	Spain	Sweden	Country Average
85%	79%	77%	75%	73%	74%	74%	64%	55%	51%	75%

Characteristics of the Family-Sponsored Venture

New family-sponsored ventures share a number of characteristics. Several are highlighted below:

Substantial income generation

The 1997 American Family Business Survey revealed that family firms generate \$10.4 trillion, or more than half of the business revenue in the United States.

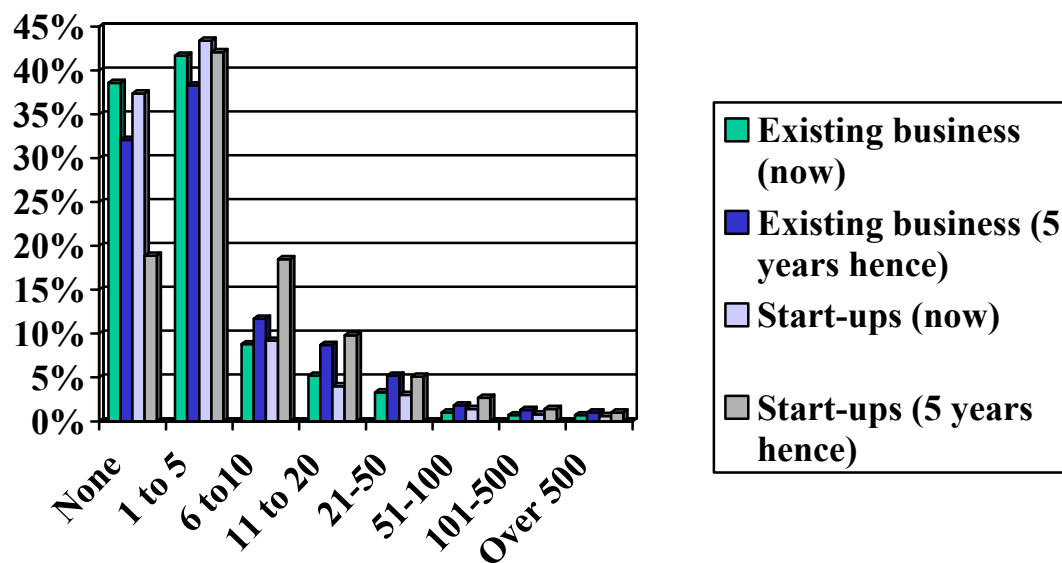
Astrachan and Shanker find that, when using the most expansive definition of family business, and perhaps the one most appropriate for policy formulation, family businesses account for 64 percent of U.S. Gross Domestic Product, or \$5.9 trillion. Even when using the narrowest definition, however, family businesses are still found to generate significant sums: \$2.6 trillion, 29 percent of the GDP.

Steady growth

Family businesses show remarkable tenacity. According to the 2002 American Family Business Survey^v (Astrachan, et al. 2002), these firms continue to grow even in poor economic environments. Thirty percent of the firms in this study report revenue growth exceeding 11 percent over a recent three-year period, compared with only 21 percent of firms reporting similar growth as of 1997.

The GEM data offer additional insight into family-business growth, suggesting that family businesses worldwide are growing in moderate increments – a strategy more likely to produce global stability. GEM also finds that family-sponsored ventures exhibit modest plans to increase employment in existing and start-up enterprises.

Chart 1. Existing Businesses and New Start-ups: Jobs Now and in Five Years



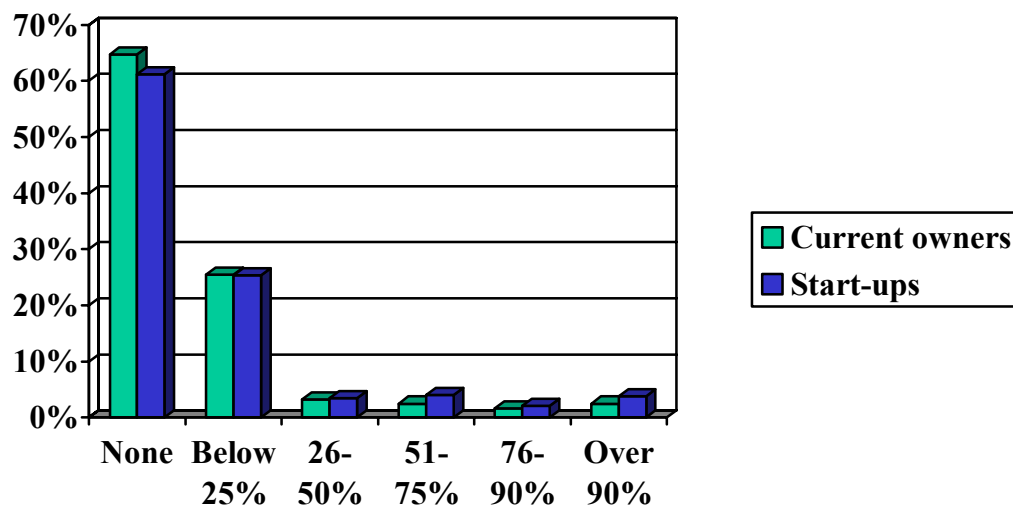
Domestic focus

Interestingly, family-business growth is achieved by focusing on domestic markets. This supports the proposition that family businesses are locally focused, economically stabilizing entities. Similarly, two-thirds of the respondents to the American Family Business Survey report no international sales.

Similar focus on domestic markets is revealed through GEM data: Almost 65 percent of family business owners report their entire sales to be domestic, and more than 60 percent of new start-ups are geared toward domestic sales.

The strong focus on domestic sales may be tied to the costs of pursuing and fulfilling international sales, requiring economies of scale seen only in larger businesses. Businesses also may face a difficulty in moving their operations to other countries. Whatever the reasons for minimal emphasis on exports, it's seems clear that communities benefit when family businesses are focused locally for the long term.

Chart 2. Revenues From Non-Domestic Markets



Necessity, opportunity and employment growth

Some entrepreneurs launch their ventures because they have no better options for work. Other entrepreneurs see opportunities and capitalize on them.

More than 30 percent of the businesses in the GEM study began as “necessity” ventures, often providing stable income for the founder and his or her family, and sometimes growing as the need demands.

Some 65 percent of firms in the GEM study began as “opportunity” ventures, suggesting that family-business entrepreneurs are so closely tied to their communities and markets that they are ideally positioned to identify and develop new opportunities. Should opportunities prove substantial, such businesses will become growing employers.

The potential expansion of many micro-family enterprises into employers is an important facet of this trend. As seen in Chart 1, more than 80 percent of the responding firms were micro-enterprises that employed five or fewer people. While most of these

firms expect to see revenue growth within the next five years, more than 70 percent nevertheless perceive that keeping employment at five or fewer and resisting downsizing show evidence of stability. The GEM data illustrate that family firms provide and will continue to provide a stable, if not a growing, source of employment. Because net job creation is an essential strategic goal for developing and developed countries alike, the continuing creation of family firms is good news. More people are likely to find jobs in family firms, and many of them will be highly skilled.

Continuity and efficiency

The GEM data further indicate that family companies play important roles in providing economic stability. A look at industries in which family firms are concentrated is telling. For example, 14 percent of family businesses work in manufacturing, a sector noted for needing long-term capital commitments, while 39 percent work in the labor-intensive sector of retail, hotels, and restaurants. Not only do families appear well-equipped to take the long view when using financial capital, but they also can make lengthy commitments when building brand identity needed in labor-intensive businesses such as the hospitality industry.

Table 3. Industries Represented by Established Family-Backed Ventures

Agriculture, forestry, fishing	4%
Mining, construction	5%
Manufacturing	14%
Transport, communication, utilities	6%
Wholesale, motor vehicle sale, service	6%
Retail, hotels, restaurants	39%
Financial, insurance, real estate	5%
Business services	10%
Health, education, social services	5%
Consumer services	8%

Family-sponsored enterprises also exhibit a strong desire to stay in business. The 2002 American Family Business Survey indicates that almost nine out of 10 family-business leaders believe the same family or families will control their businesses five years from now. And a recent study of 192 family firms in Finland, for example, found that the average firm had existed for 57 years and had seven members of the family actively involved in different facets of the business (Koiranen, 2002). As with other countries, some firms have existed for more than 100 years under the control of the same owner family.

This finding is important because family firms represent an efficient economic organizational form where the cost of operations is often reduced. For example, only in family companies where owner and manager are the same are the goals of shareholders, board members, and managers aligned. The stable ownership of family businesses also supports patient investments in developing new technologies and exploring complicated strategic options. Further, learning new skills and building capabilities

require considerable and continued investments. It is perhaps only in multi-generational family companies that a business has a common and committed multi-generational investor group.

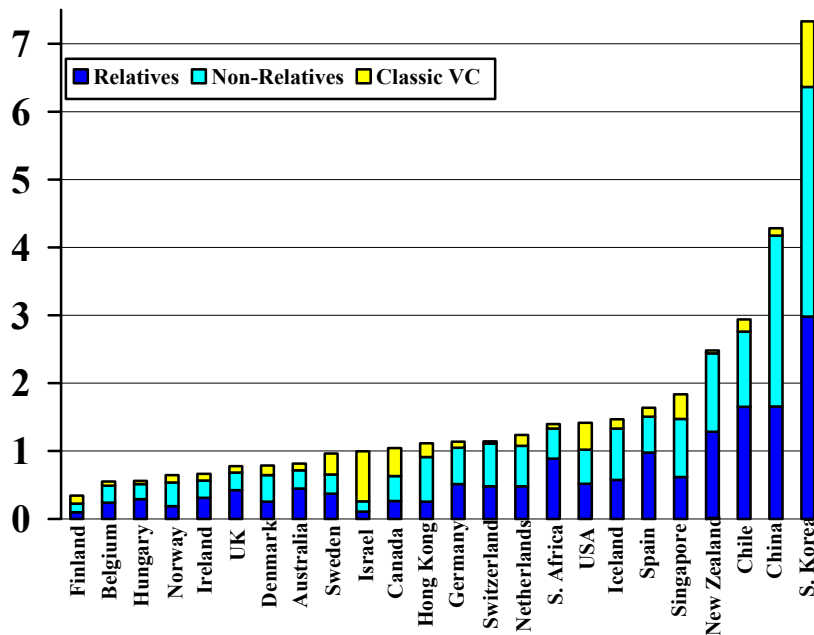
The Important Role of Family Firms in Financing Entrepreneurship

One of the most notable findings of the GEM research is the incredibly large role families play in establishing new ventures – and, by extension, influencing the growth and viability of national economies.

Data from the 2002 GEM study , show that family-business investments as a percent of all informal investments ranged from nearly 30 percent to more than 80 percent. Countries where family business financing constitutes the largest share of informal investment include Mexico, India, Brazil, South Africa, Spain, and Australia. Further, Chart 3 shows that funds provided by relatives range from 0.5 percent to nearly 3 percent of GDP. Funding new ventures through money raised from relatives is very important in countries such as South Korea, China, Chile, Spain, the United States, Australia, the United Kingdom, Ireland, and New Zealand.

Additional research has found that cultural, political, and legal issues affect family-based new-venture investment. Further studies need to be conducted to determine whether making an environment more favorable to family investment can support economic growth, job creation, and socioeconomic stability.

Chart 3. Domestic Informal and Classic Venture Capital Investments as a Percent of GDP



Classic venture capital comprises investments in seed, early, start-up, and expansion-stage companies.

The 2002 GEM study shows that family investor prevalence rates are highest in Mexico, Iceland, Thailand, the U.S., South Africa, New Zealand, South Korea and Chile. The opposite is true of Japan, Russia, Brazil and Israel, again illustrating the role of political and legal systems in investment activities.

Chart 4. Family-Business Investments as a Percent of All Informal Investments

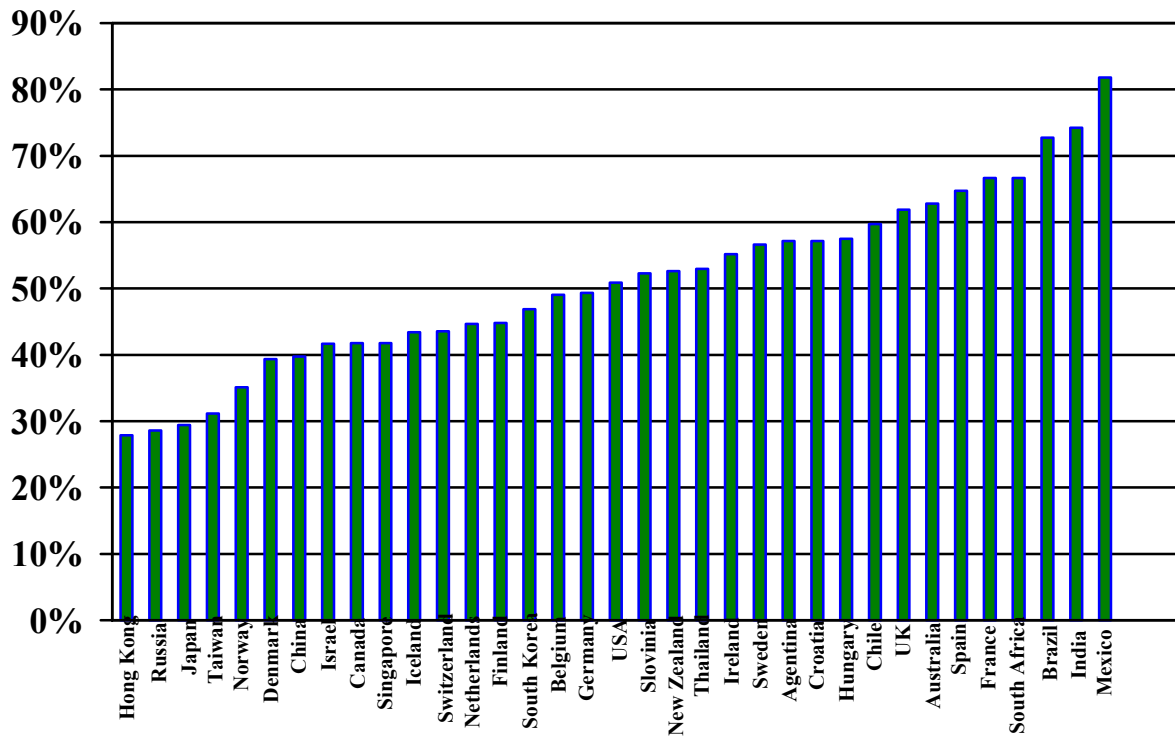


Table 5. Prevalence of Informal Investment by Country

	Informal Investment					Classic Venture Capital	Classic Venture Capital & Informal Investment				
	Prevalence of Informal Investors 18 years & older	Average Annual Informal Investment per investor (1998-2002)	Total Informal for country by adults 20 years & older US\$ million	Total Informal Investment per capita US\$	Total Informal Investment per GDP Percent		Classic VC Invested domestically in 2001	Informal & Classic VC Combined	Informal as a percent of Combined	Average Total per Person 20 years and older	Average Total per GDP
	Percent	US\$	US\$ million	US\$	Percent		\$US million	US\$ million	Percent	US \$	Percent
Argentina	1.9	2,308	1,143,783	44	0.42						
Australia	1.7	10,201	2,555,126	173	0.72	353,919	2,909,045	87.8%	197	0.82%	
Belgium	1.4	9,482	1,110,213	137	0.49	140,240	1,250,453	88.8%	154	0.55%	
Brazil	1.1	754	499,351	4	0.10						
Canada	3.1	5,858	4,421,571	179	0.63	2,863,619	7,285,190	60.7%	295	1.04%	
Chile	3.8	4,561	1,833,704	174	2.76	119,373	1,953,077	93.9%	185	4.63%	
China	5.0	1,068	48,371,573	53	4.17	149,905	48,521,478	99.7%	53	4.19%	
Croatia	1.3					4,028					
Denmark	3.4	7,340	1,041,242	248	0.65	226,548	1,267,791	82.1%	302	0.79%	
Finland	2.7	2,434	269,950	66	0.23	143,631	413,580	65.3%	102	0.35%	
France	1.6					1,004,218					
Germany	3.7	7,803	19,309,583	286	1.05	1,676,338	20,985,921	92.0%	310	1.14%	
Hong Kong	3.2	8,123	1,471,474	256	0.91	332,521	1,803,995	81.6%	314	1.11%	
Hungary	2.2	1,352	240,438	30	0.51	23,507	263,945	91.1%	33	0.56%	
Iceland	7.4	6,569	99,727	484	1.33	10,422	110,149	90.5%	535	1.47%	
India	2.6	311	5,221,008	8	1.10						
Ireland	3.0	7,025	575,742	211	0.57	100,923	676,665	85.1%	248	0.67%	
Israel	1.5	4,587	286,599	70	0.26	811,188	1,097,787	26.1%	269	0.99%	
Italy	1.6					780,999					
Japan	1.0					1,460,347					
Mexico	5.9	991	3,671,771	58	0.59						
Netherlands	1.7	19,630	4,094,475	326	1.08	613,846	4,708,321	87.0%	375	1.24%	
New Zealand	4.3	9,654	1,207,930	419	2.44	20,482	1,228,412	98.3%	426	2.48%	
Norway	4.8	5,337	884,578	256	0.54	170,209	1,054,787	83.9%	305	0.64%	
Poland	1.3					54,044					
Portugal						50,155					
Russia	2.2	871	1,304,258	12	0.42						
Singapore	3.5	10,650	1,299,353	371	1.47	318,496	1,299,353	100.0%	371	1.47%	
Slovenia	2.2					3,500					
S. Africa	3.5	1,596	1,489,777	55	1.33	77,373	1,567,149	95.1%	58	1.40%	
S. Korea	4.9	15,445	26,903,090	752	6.36	4,094,731	30,997,821	86.8%	867	7.33%	
Spain	2.6	10,101	8,764,280	267	1.51	757,397	9,521,678	92.0%	290	1.64%	
Sweden	2.9	6,891	1,373,469	197	0.66	642,064	2,015,532	68.1%	289	0.96%	
Switzerland	4.2	11,265	2,736,685	470	1.11	82,241	2,818,926	97.1%	484	1.14%	
Taiwan	3.2	25,996	14,749,195	837	5.22						
Thailand	5.3	37	86,219	2	0.08						
U.K.	1.6	13,057	9,742,788	210	0.68	1,307,555	11,050,343	88.2%	238	0.78%	
USA	4.6	10,715	103,985,109	497	1.02	40,618,800	144,603,909	71.9%	691	1.417%	
All Nations	2.9	7,941	270,744,061	110	0.95	59,012,617	299,405,307	81.5%	207	1.38%	
	Only nations with at least 40 informal investors reporting amount invested 1998-2002. 3,795 informal investors reporting in 31 nations.						Combined classic VC & informal totals and averages Include only nations with data for both classic and informal.				

What motivates entrepreneurs?

Other factors are important to business formations that derive from family and family experience. For example, even though prior exhibits show that family investment is readily available across the many countries, start-up prevalence rates differ. While almost 60 percent of the respondents from the United States were involved in independent start-ups, only one in five respondents from Spain were involved in similar activities. A quick examination shows that three factors appear related to start-up activities:

- ◆ being acquainted with another entrepreneur,
- ◆ belief that one possesses the skills and knowledge needed for business creation, and
- ◆ the lack of a fear of failure.

Table 4. Independent Start-up Explanatory Variables

	% of respondents involved in independent start-ups	% of respondents who know someone personally who started a business in the past two years	% of respondents who believe they have the knowledge, skills and experience required to start a new business	% of respondents who believe that fear of failure would prevent them from starting a business
U.S.	59	64	90	13
Singapore	47	54	78	27
New Zealand	35	57	90	19
Brazil	34	55	83	32
Hungary	28	59	89	13
UK	26	47	88	20
Israel	23	57	83	37
Sweden	23	65	84	14
Australia	23	48	83	22
Spain	21	63	88	30
TOTAL	34%	55%	87%	21%

While all respondents had family ties, a majority reported closely knowing entrepreneurs who had started a business in the last two years. Exposure to the highs and lows of owning and running a family business enabled them to feel comfortable with the idea of starting their own venture. Kenyon-Rouvinez reports similar findings in a study of serial entrepreneurial families. A large majority of the respondents (90 percent for the U.S. and 78 percent for Singapore, for example) reported feeling secure in their own skills and experiences to start new ventures, and experiencing a low fear of failure (range: 13 percent U.S. and 37 percent Israel). It seems that a cultural heritage, both country and familial, as well as personal experience with entrepreneurial success can greatly enhance entrepreneurial actualization.

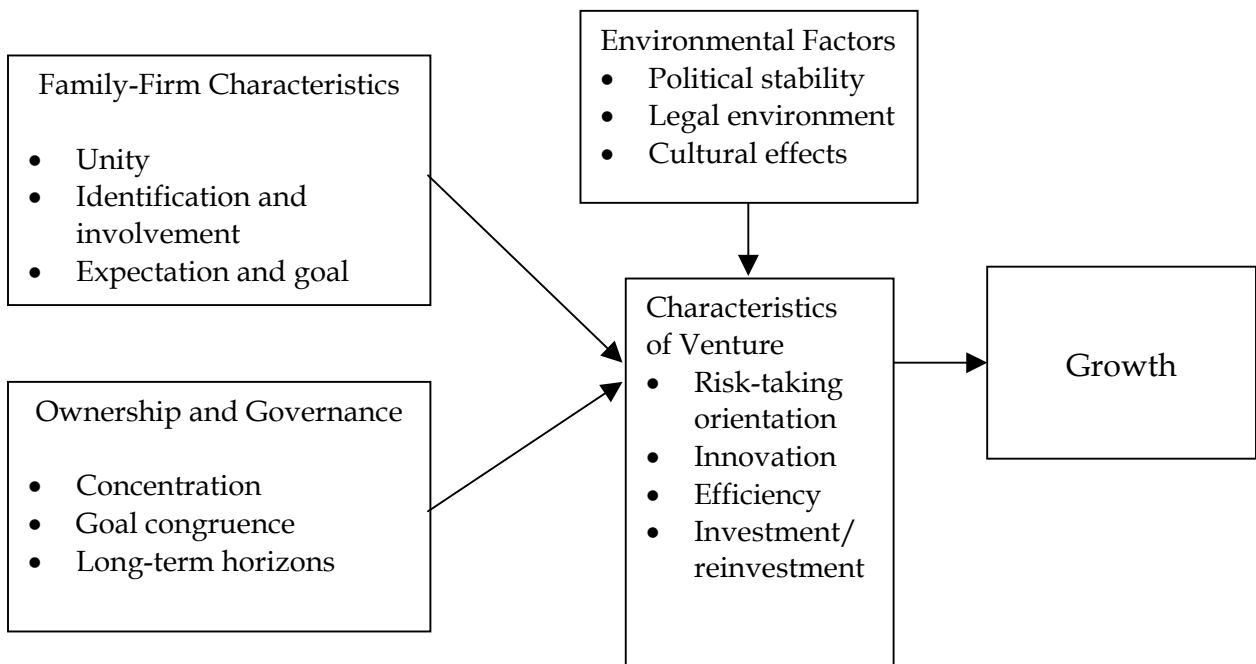
Family businesses also can be seen as forces for positive social change. For example, GEM data suggest that women-led businesses are quite prevalent among family-backed ventures, representing 48 percent of the sample. Future research should explore other ways in which family businesses lead social as well as economic change -- advocating for environmental issues, workplace and employment issues, philanthropy, and community investment, for example.

Clearly, then, family-sponsored ventures dominate the economies in most nations by generating significant employment and revenues, continuing to grow despite adverse economic conditions, and staying small and focused on local economies. These characteristics paint a picture of businesses that take a long view, cement community stability and prosperity, drive positive social change, and are well-positioned to identify and capitalize on new market, product, and service opportunities.

Secrets of sustained growth in family-sponsored firms

Several factors combine to explain family firms' ability to achieve and sustain growth. As Figure 2 shows, the nature and ownership of the family firms combine to influence their ability to take risks by creating and entering new businesses.

Figure 2. A Proposed Model of Sustainable Family-Business Growth



◆ Family firm characteristics.

The founder's direct involvement in the company's operations is an important attribute for strategic and symbolic reasons. Founder involvement ensures consistency of vision, which creates a long-term view of the company, industry and competition. A long view encourages patient investment. Forty-eight percent of the respondents in the GEM study had made personal investments in a business started by a close family member. Such investments bond family owners to their businesses and enhance the congruence of their goals.

The founder's presence also inspires the active interest of other family members and provides them with cognitive maps that aid in identifying opportunities and raising the comfort level needed to start a venture. Founders also bring in employees from outside the family and train them to understand the values and culture that prevail within the company. Understanding cultural variables is important for creating commitment and ensuring goal congruence among different management groups. In developing countries, employment and acculturation is an important means of upgrading the skills of talented newcomers and preparing them for leadership positions.

Family involvement also creates a sense of unity and common purpose, driving family members to make sacrifices to protect the family and the business. They likely look for more economical ways to run the business, understanding that business success means greater family wealth. Over time, starting and running an independent business becomes a way of life for individuals from entrepreneurial families.

◆ **Ownership and governance.**

The family ownership structure provides supports organizational efficiency. Owners are managers; because their interests are aligned with the needs of their companies, they tend to take a long view. Further, ownership is heavily concentrated, making it possible to implement important strategic changes more rapidly.

Governance variables influence family-firm growth in another powerful, subtler way -- in a reduced need for formal and contract-based governance. In non-family companies, managerial opportunism can be constrained through contracts, strong governance and oversight, all of which increase expenses.

Obstacles to change and growth

Despite the vitality of family businesses and their importance for national growth and development, several factors appear to inhibit their success and survival. Impediments to growth vary significantly across countries, reflecting cultural, political, historical, and ideological factors. The following are among the most serious impediments for growth:

- Existing legal frameworks might inhibit family capitalization of businesses and, in later generations, the smooth transfer of ownership. These may prevent future generations of family-firm owners from maintaining the stable employment levels and other social and personal benefits they have been providing. Even in some advanced countries, inheritance laws complicate the transfer of assets.
- Evaluating and valuing property rights remains a major obstacle. Intangible assets, which are crucial to the success of many family firms, are often ignored by traditional accounting systems, especially in developing countries. This might make it difficult for younger family firms to obtain necessary resources to grow.
- Political instability and high political costs of business formation. Entrepreneurship thrives in stable political environments and where governments lower the financial and political barriers to entry.

As research clearly indicates the prevalence and important role of family firms in creating social and economic stability in nations around the world, we encourage each

nation to set up a task force to determine the legal frameworks that would enhance the growth of family firms in their specific context.

Conclusion

Family businesses are renewable yet precious resources that grow and benefit nations when tended, shrink but survive tenaciously when neglected, and stabilize the natural erosion of economies set in place by business and political realities. They are important to national welfare and likely international prosperity.

In summary, as GEM principal investigator William Bygrave has stated, "The new family firms in the 10-country GEM sample number 12 to 25 million, accounting for one-third to two-thirds of all start-up and new firms in these countries. Without family-supported efforts, it seems evident that the scope of entrepreneurial activity would be substantially reduced."

References

- i Reynolds, P.D., W. D. Bygrave, and L.W. Cox, 2002 Global Entrepreneurship Monitor: the Ewing Marion Kauffman Foundation.
- ii Astrachan, J.H., and M.C. Shanker. 2002 Family Businesses' Contribution to the U.S. Economy: A Closer Look.
- iii The Arthur Andersen/MassMutual American Family Business Survey '97 was conducted by the Arthur Andersen Center for Family Business and the Massachusetts Mutual Life Insurance Company with the assistance of Loyola University Chicago Family Business Center and the Family Enterprise Center at Kennesaw State University.
- iv Heck, R.K.Z. & Stafford, K. (2001). The vital institution of family business: Economic benefits hidden in plain sight. In G.K. McCann & N. Upton (Eds.). *Destroying Myths and Creating Value in Family Business*. pp. 9-17. Deland, FL: Stetson University Press.
- v Astrachan, J.H., I.E. Allen, and S. Spinelli. 2002. *MassMutual/Raymond Institute American Family Business Survey*. Springfield, MA: MassMutual Financial Group.