Chapter 13

Understanding Family Firm Profitability Heterogeneity: Differences Within Family Managed Firms and the Interaction Effect of Innovative Effort

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ABSTRACT

Understanding family firm heterogeneity has become a topic of critical importance among academics and practitioners in the family business research field. This chapter aims to provide new insights into this theme by examining the differences in profitability within the pool of family firms. Furthermore, this chapter introduces an exceptional strategic element, namely innovative effort, to analyse when and to what extent the deployed innovative effort influences the family involvement in management-firm profitability relationship. Using a panel dataset on 3,164 observations of Spanish private manufacturing firms over the 2000–2015 period, the findings reveal significant differences in the profitability of family firms depending on the degree of family involvement in the firm’s management. The findings also show that innovative effort reinforces the positive effect that family involvement in management exerts on firm profitability.

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INTRODUCTION

Firm profitability is essential to sustain the financial health of firms, regions and nations (Wolff & Pett, 2006). The study of profitability within family firms has been acknowledged as an issue of utmost importance (De Massis, Kotlar, Mazzola, Minola, & Sciascia, 2018; Kotlar, Fang, De Massis, & Frattini, 2014; Sciascia, Mazzola, & Kellermanns, 2014), insofar as family firms are ubiquitous and dominant forms of organizations in many countries of the world (La Porta, Lopez-De-Silanes, & Shleifer, 1999; Villalonga & Amit, 2006) and due to the critical nature of profitability to guarantee firm perpetuation and sustainability (Gottardo & Moisello, 2015). Nevertheless, there is little evidence in the existing literature on the study of profitability within the pool of family firms, despite the recognition of family firm heterogeneity and the acknowledgment of higher variability in profitability goals among family firms than between family and non-family firms (Chrisman & Patel, 2012; Chua, Chrisman, Steier, & Rau, 2012; Rau, Sabine, Schneider-Siebke, & Gunther, 2019).

Family firm heterogeneity can be expressed through goals (Chrisman, Chua, Pearson, & Barnett, 2012), governance structures (Carney, 2005), resources (Habbershon, Williams, & MacMillan, 2003), and founder values (García-Álvarez & López-Sintas, 2001). However, it has been argued that is the family involvement in the firm what really makes unique a family firm (Berrone, Cruz, & Gómez-Mejía, 2012; Chua, Chrisman, & Sharma, 1999), and more precisely, the family involvement in the firm management (Gallucci, Santulli, & Calabrò, 2015; Martínez-Alonso, Martínez-Romero, & Rojo-Ramírez, 2019). Specifically, a main source of family firm heterogeneity is in the degree to which family members occupy top management positions, as high or low levels of family involvement may determine the features of the management team (Diéguez-Soto & Martínez-Romero, 2019; Hambrick & Mason, 1984). Indeed, family involvement in management is generally recognized as a fundamental conditioning of firm profitability (Martínez-Romero, Martínez-Alonso, Casado-Belmonte, & Diéguez-Soto, 2019), since it enables family members to engage in decision-making processes and therefore, exert a significant influence on organizational outcomes (Hambrick & Mason, 1984). Therefore, more research is needed in analysing how family involvement in management, as a potential source of family firm heterogeneity, influences firm profitability within the pool of family firms.

Moreover, to further delve into family firm heterogeneity, this chapter introduces a moderating factor (Chrisman et al., 2012; Chua et al., 2012), which may help to unravel mixed findings from previous research on the family management-firm profitability relationship. In this respect, an important gap persists in the comprehension of how strategic decision making may moderate the relationship between family involvement in management and firm profitability within the pool of family firms. Thus, this study introduces innovative effort as an exceptional strategic element that might influence the impact of family involvement in management on firm profitability. Innovative effort is understood as the manner in which a business encourages investments in research and development (R&D) to get innovation outcomes. The authors’ contention is that innovative effort might reinforce the distinctive influence that family involvement in management exerts on firm profitability.

Based on the aforementioned and using the resource-based view (RBV) as the theoretical approach, this chapter seeks to shed light on this theme addressing the following research questions. How does the level of family involvement in management influence the achievement of firm profitability in family firms? Does innovative effort moderate the expected impact of family involvement in management on firm profitability? To answer these questions, the authors performed an empirical analysis with different econometric models that cover the hypotheses, utilizing a panel data sample of 3,164 observations of...