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Family Enterprises and Minority Shareholders: Benefits and Risks in Corporate Governance

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ABSTRACT

This essay mainly studies the benefits of minority shareholders in family businesses. Through the Secondary research method to investigate the relevant data of countries worldwide, it is found that family businesses dominate the global business and make significant contributions to employment and GDP growth. Moreover, family enterprises attach importance to brand inheritance and the long-term development of the company. Their good brand image and endurance in difficulties have increased the overall revenue of the company, thus benefiting minority shareholders to a certain extent. Nevertheless, this essay points out that there is a unique "agency issue" in family enterprises and demonstrates that this issue will damage the interests of minority shareholders through the case of Samsung. Furthermore, this essay finds that family infighting is more likely to occur in older family businesses, which brings a new research dimension to family business governance.

KEYWORDS

Family Business; Minority Shareholders; Principle-Principle Problem; Family Ownership; Infighting; Family Business Governance

1. INTRODUCTION

The structure of family ownership is complex. In many scenarios, family ownership is described as a situation where the family not only holds a majority share in the company but is also actively involved in the company's operations (D'Este & Carabelli, 2022; Mallin, 2019). While family businesses bring certain advantages that positively impact the company's growth, the potential risks should not be ignored. In recent years, scholars have had different perspectives on the benefits that family businesses can bring to stakeholders. Therefore, this essay will focus on the benefits of minority shareholders in family businesses. Firstly, analyzing the current status of family businesses in various countries worldwide. Secondly, by combining real-life examples, the essay will discuss the benefits of minority shareholders from four aspects: family's emphasis on brand inheritance, family's behavior when facing difficulties, agency problems of the family business, and the conflicts within the family. Finally, make a summary.

2. CURRENT STATUS OF FAMILY OWNERSHIP

According to McKinsey and Company (2024), family businesses provide 60% of jobs in countries worldwide and contribute more than 70% of global GDP. Europe is one of the regions with the largest share of family businesses in the world, with 57% of family businesses over 100 years old (Ernst & Young Global, 2023; Tharawat Magazine, 2023). In addition, family-owned Businesses' workforce participation rates are very high in the European region; family-owned Businesses' workforce participation rates refer to the percentage of employees employed by family-owned businesses as a percentage of the total workforce in a country or region (Tharawat Magazine, 2023). For example, Mexico accounts for 90%, Spain 86%, and Italy 70% (Tharawat Magazine, 2023). Obviously, the proportion of Family enterprises in Europe is more concentrated than that in other countries, which means that the development of Family ownership may be related to the development of the country and its history. There is a certain correlation between culture and other factors.

In addition, in these countries, family businesses contribute a significant portion to their respective national GDP. For instance, Spain accounts for 70%, Italy 68%, and Canada 60% (Tharawat Magazine, 2023). This indicates that family-owned businesses not only occupy a central position in the employment market of various countries but also serve as important drivers of GDP growth.

Currently, family ownership encompasses a variety of industries. It covers about 11 industries, especially Consumer Discretionary, which accounts for 18%; Industrials, for 16%; and Consumer staples, for 13% (Tharawat Magazine, 2023). For example, French luxury goods group Louis Vuitton Moet Hennessy (LVMH), Swiss luxury goods group Richemont, South Korean technology company Samsung Group, and American retail company Walmart Group are typical representatives of family businesses in different industries (Ernst & Young, 2023; Lieskoski, 2020; Pastore, 2018).

Based on the dominant position of family businesses in global business patterns, scholars have begun to discuss whether families with large shares are influencing the overall business direction of the company and making decisions that benefit all stakeholders (D'Este & Carabelli, 2022). So, the minority shareholders, who are the important stakeholders of the firm, their rights will be directly affected by the behavior or decisions of the family members.

3. BENEFITS TO MINORITY SHAREHOLDERS IN FAMILY OWNERSHIP

3.1. The Impact of Brand Heritage on Minority Shareholders

Most family businesses attach great importance to brand heritage (Blombäck & Brunninge, 2013). For example, European family-owned businesses often aim to create an attractive brand culture and project a good family image to gain the support of the market (Pastore, 2018). Motoc's (2013) research further confirms that the image and reputation of family businesses directly affect financial performance. This is because consumers perceive products from family businesses with a strong brand image as more reliable, thereby increasing their desire to make purchases (Binz et al., 2013).

For example, LVMH is controlled by the Bernard Arnault family, which holds 48% of the group's shares and 63.5% of its voting rights, and several family members hold executive positions (LVMH, 2023; Market Screener, 2024). In recent years, LVMH has strengthened its corporate culture of "luxury," "royalty," and "elegance" in the minds of consumers through the acquisition of brands such as Loro Piana and Christian Dior (Harrow, 2023). In addition, LVMH is committed to implementing sustainable development strategies, such as developing sustainable leather to reduce carbon emissions, which has helped the company earn a good reputation (LVMH, 2023). By the end of 2023, LVMH's revenue had increased by 9% compared to 2022, and its share price rose 7.9% for the year to 733.60 euros (LVMH, 2023). By acquiring luxury companies with unique brand cultures and adopting a sustainable development strategy, Bernard Arnault has made LVMH's culture more diversified and attractive. Meanwhile, adopting a sustainable development strategy also meets market demand, helps the company earn more profits, and boosts its stock price. Therefore, as a minority shareholder, they can also benefit to some extent, especially the financial benefits.

However, the benefits of minority shareholders are also influenced by other factors. For example, another well-known luxury group, Kering, has always been committed to doing CSR and sustainable development practices. They have developed a biodiversity strategy to ensure that their activities are carried out on the basis of animal welfare and the protection of ecological resources (Kering, 2019). Unfortunately, Kering's revenue in 2023 was 1.78% lower than in 2022 (Kering, 2023). This event was attributed to the family members' lack of professional ability, leading to strategic mistakes, which decreased the company's revenue and damaged the interests of minority shareholders (KERING, 2024). In other words, the strong management ability of family members is an important prerequisite for the benefit of minority shareholders.

3.2. Impact of Family Members' Long-Term Vision on Minority Shareholders

Family businesses and non-family businesses have significant differences in defining success standards (Pastore, 2018). Non-family businesses prioritize short-term profits and dividends, while family businesses place greater value on the legacy of the company (Kappes & Schmid, 2013; Pastore, 2018). Therefore, during difficult times, family businesses often exhibit more endurance compared to non-family businesses (Birdthistle & Hales, 2023).

For example, a survey report on global businesses during the COVID-19 period revealed that both family-owned and non-family businesses needed to swiftly take action to adapt to significant market changes (Mastering A Comeback, 2021). In such circumstances, family businesses with a long-term development philosophy gained significant advantages (Minichilli et al., 2015). Most family businesses choose a transformation strategy rather than the downsizing approach employed by non-family businesses. Family members aspire for the company to serve not only as a profit-generating tool but also to benefit society (Mastering A Comeback, 2021). According to Mastering A Comeback (2021), during the COVID-19 period, family-owned business income is 15% higher than non-family business income. In other words, the reason why family businesses were able to withstand immense pressure and avoid layoffs during the COVID-19 period may be to gain support from employees and society. Only in this way can the company overcome various obstacles, survive in the long term, and be passed down through generations. Therefore, family businesses are better positioned to protect the interests of the company compared to non-family businesses during difficult times, which is an important factor in benefiting minority shareholders. Minority shareholders do not need to worry about major shareholders abandoning the company or other damaging actions in pursuit of short-term profits.

However, not all family businesses can achieve this when facing challenges. The research has certain limitations (Mastering A Comeback, 2021). The majority of the surveyed companies were from the United Arab Emirates, and the culture of the country has influenced the values of its family-owned business members to some extent, making them more willing to contribute to society (Naoum et al., 2015). In other words, the differences in external factors of country, culture, and legal policy may make family-owned businesses take different measures when facing difficulties. Therefore, the degree of benefit of minority shareholders in family-owned businesses under different external factors needs to be further studied.

3.3. Challenges Faced by Minority Shareholders in Family-Owned Businesses

3.3.1. The Impact of Principle-Principal problem on Minority Shareholders in Family business

In fact, some scholars have proposed that family business can reduce agency problems to some extent and bring benefits to minority shareholders. When a family owns a large share of a company and is actively involved in its operations, they play a real "stewardship role" (Anderson & Reeb, 2003; Sacristán-Navarro et al., 2015). This is because family members share the same interests and are more inclined to make strategic decisions that benefit all stakeholders, including minority shareholders (Laffranchini & Braun, 2014).

However, there are scholars who hold different views. Barker and Chiu (2014) and Morck and Yeung (2003) argued that although family firms do not involve agency issues in the traditional sense, they still face unique "principal-principal problems." This is because families, in order to protect their wealth, sometimes hoard resources at the expense of the company's overall interests (Laffranchini & Braun, 2014). For instance, some large family firms may utilize their information advantage to pursue their interests (Huang et al., 2023). In this case, it can be inferred that family members prioritize their own interests rather than minority shareholders.

Additionally, the lack of government regulation in emerging economies also exacerbates the Principal-principal problem (D'Este & Carabelli, 2022; Huang et al., 2023). For instance, in Korea, chaebols hold significant influence and power (Lieskoski, 2020). Samsung Group Chairman Lee Kun-hee employed controversial methods to sell shares in order to secure broader development opportunities for his son and ensure a smooth financial inheritance (Lieskoski, 2020).

Lee Kun-hee sold Samsung Data Systems (SDS) shares to his son and three other family members at the price of only 7,150 won per share, while the market price of the stock was 550,000 won (Lieskoski, 2020). Clearly, this significantly increased the wealth of the Samsung family, but minority shareholders of SDS suffered huge economic losses. Despite their egregious behavior, the Lee family only faced public criticism rather than serious sanctions because of the South Korean government's inadequate regulatory system (Lieskoski, 2020).

Therefore, in order to protect the interests of minority shareholders under family ownership structures, some measures need to be taken. Firstly, the market system should be strengthened by reinforcing listing regulations and introducing corporate governance standards (Barker & Chiu, 2014). Secondly, regulatory authorities should enhance requirements for corporate information disclosure to ensure market transparency (Barker & Chiu, 2014). Furthermore, the listing rules are adopted to enable minority shareholders to participate informally in decision-making and prevent controlling shareholders from using majority voting rights to suppress minority shareholders' interests (Barker & Chiu, 2014). By implementing these measures, it is possible to maximize the avoidance of improper actions taken by family members for personal privacy, thereby safeguarding the interests of minority shareholders.

3.3.2. The Impact of Internal Family Conflicts on Minority Shareholders in Family business

Family businesses could experience family conflicts, which can impact the company's profitability and cause losses to minority shareholders (Lozano et al., 2016). For instance, when it comes to issues such as "successor candidates," "share inheritance," and "property division," family members will resort to various ways, sometimes even unethical ones, to secure higher positions and occupy more family property (Pastore, 2018). This chaotic situation has a negative impact on the company's reputation and development.

For example, in 1982, GUCCI successfully went public, and the GUCCI family remained involved in the company's operations (Pastore, 2018). Until 1989, when Maurizio Gucci became the CEO, he made a major decision mistake, resulting in a steep decline in GUCCI's performance (Pastore, 2018). As a result, different factions of the GUCCI family began to seize control of the company through fraud, embezzlement, and murder (Admin, 2023; Pastore, 2018). This family struggle diverted the attention of the company's management, preventing them from making the right decisions for the company's operations (Admin, 2023; Pastore, 2018). Ultimately, the company's finances and reputation suffered significant damage, harming all stakeholders involved (Admin, 2023; Pastore, 2018).

In fact, according to Lozano et al. (2016), family member conflicts are more likely to occur in older family-owned businesses. This is because the departure or death of the founder leaves the family with a stabilizing force, which leads to competing interests among family members (Lozano et al., 2016). However, for young family firms, when the company is just starting out, there are no succession and property division issues, so internal family conflicts are less likely to occur (Lozano et al., 2016).

In other words, family disputes increase the risk of damage to the interests of minority shareholders. While not all family businesses experience internal conflicts, when they do occur, these risks can not only result in decreased returns for minority shareholders but even lead to the downfall of the company. Therefore, family businesses may be able to establish effective internal family governance mechanisms to reduce the likelihood of severe conflict issues, thus protecting the legitimate rights and interests of minority shareholders (Barker & Chiu, 2014).

In summary, family ownership is more detrimental to minority shareholders. Some well-known family businesses have a good brand culture and family image, so they have generated rich profits and benefited minority shareholders. But it should be based on the good management ability of the family members. Moreover, while some family members will prioritize the long-term growth of the business and strive to balance the interests of multiple stakeholders during difficult times, this does not mean that all family businesses will make similar choices when faced with different political, environmental, and cultural factors. When it comes to safeguarding their own wealth, the majority of family-owned businesses tend to prioritize personal interests. Especially when it comes to "share inheritance" or "property division," some families may fight for more rights via fraud, murder, and other ways.

However, these behaviors will seriously damage the company's reputation and overall revenue, thus greatly damaging the interests of minority shareholders. Although internal conflicts predominantly occur in young family firms, as time passes, the number of old family-owned businesses will increase, leading to a more frequent occurrence of such situations. Therefore, only by strengthening supervision and formulating strict internal and external corporate governance guidelines can family members be prevented from making opaque decisions and using improper ways, thus protecting minority shareholders' rights and interests to a certain extent.

4. CONCLUSION

This essay begins with a survey of current global data on family businesses and family ownership and finds that family businesses are prevalent worldwide and contribute significant value to global GDP, especially in places like Europe. Secondly, this essay discovers that family ownership may benefit minority shareholders to a certain extent, but there are many limiting factors. For example, since family enterprises are controlled by a family, they often attach great importance to corporate reputation and influence and are more resilient in the face of industry-wide or global crises compared to non-family enterprises. This will prompt minority shareholders to obtain stable returns. Next, the essay mainly discusses the topic of "agency issue" that has been hotly debated by scholars. However, the final conclusion is that they do not involve agency issues but form their own model of agency problem, also known as the principal-principal problem. Under the external conditions of an imperfect system, economic structure, and country, the interests of minority shareholders are further swallowed by the family, which is fully reflected in Samsung Group in South Korea. Finally, this paper discusses the situation of infighting within family businesses and finds that infighting may eventually cause great harm to the entire group, including the family and minority shareholders. However, other scholars point out that the scenario of family infighting depends on specific drivers. For example, young family businesses do not tend to have infighting.

In conclusion, although some scholars have shown that family enterprises can bring advantages to minority shareholders, from a practical and comprehensive perspective, the final result may often cause varying degrees of harm to minority shareholders. This is often due to an imperfect system and the founder or family members using their own powerful rights and social status for favouritism and malpractice. Therefore, by strengthening market supervision and establishing internal and external rules and regulations, the interests of minority shareholders can be protected to a certain extent.

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