International Journal of Business and Management; Vol. 10, No. 7; 2015
ISSN 1833-3850 E-ISSN 1833-8119
Published by Canadian Center of Science and Education

Succession Decision in Vietnamese Family Companies

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Received: April 1, 2015 Accepted: April 28, 2015 Online Published: June 20, 2015

doi:10.5539/ijbm.v10n7p208 URL: http://dx.doi.org/10.5539/ijbm.v10n7p208

Abstract

This study examines the relationship between the choices of family or outside CEO with company performance. The sample of this study covered 65 Vietnamese family companies in 17 industries. The findings indicate, as anticipated, that family CEO enhanced company performance greater than outside CEO. Within the family company, CEO-successor enhanced the firm value lower than the CEO-founder. Contacts with the business environment, education, experience and sufficient business capital may provide young CEOs with values added to better manage family companies than founders.

Keywords: succession, CEO, family member, outsider, Vietnam

1. Introduction

Succession is no more something of a novelty in the developed countries. Whereas, in Vietnam, most enterprises are still very young. The Vietnamese economy has undergone a nearly 25 years' process of renovation; this is also a period that equals the length of service of a Vietnamese entrepreneur. It is therefore easily understandable why the issue of succession among leadership generations has recently been much referred to in recent time. Family businesses constitute the most popular form, as one can put it, making up over two thirds of the firms who employ over half of the global workforce. Family companies actually play an important role in business activities. Nevertheless, studies have shown that family companies have a low rate of existence (Ket De Vries, 1993; Morris, Williams, & Nel, 1996). One of the determinants that result in this low rate is the difficulty in the succession the family generations. How the process of succession of the family generations influences the company performance? In the world, there have been numerous studies on the choice of succeeding leaders as the family members or outsiders (Burkart, Panunzi, & Shleifer, 2002; Lee, Lim, & Lim, 2003).

In the context of Vietnam, from the first generation, when the Business Law was formed in 1990 till the second generation, namely entrepreneurs of the WTO integration period in 2005-2006, unlike the entrepreneurs of the first and second generations descended chiefly from poverty and hardship to set themselves up in business empty-handed, the entrepreneurs nowadays are those who were born in the lap of luxury and are assuming very great responsibilities associated with thousands of billion Vietnamese dong. This is a really challenge to companies and founders in handing down their legacy to the potential successors. Some companies train their sons or grandsons to be their successors. Nevertheless, failure still occurs when the successors do not have the sufficient competence and experience to meet the business targets against the difficult background of the business environment today. To ensure their existence, family companies therefore should have the skills and a professional management model from a CEO not belonging to a family based on attainments rather than the criteria such as blood-relationship or kinship.

This study is intended to examination whether the choice of successor outside the family will better influence the performance of Vietnamese family companies or not? The findings obtained may be used as references in the course of handing down legacy and strengthening management performance in Vietnamese family companies.

2. Theoretical Framework

2.1 Theories of Choice of Successor from Family Insiders or Outsiders

Supporters of family succession (Family CEO) stressed that Family CEOs had a better knowledge of companies and their social associations (Chung, Lubatkin, Rogers, & Owers, 1987). Accordingly, the family candidate would ensure the smooth succession process and maintain the stability, as they got used to and would impulse the development of the existing business strategy of the company (Carlson, 1961). Family succession also promoted loyalty and reputation thereby resulting in better performance (Davis, Schoorman & Donaldson, 1997).

It was also pointed out by experts that companies owned and managed by families achieved better performance than those managed by experts (Monsen & Associates, 1968; Daily & Dollinger, 1992; Ang & Associates, 2000). Family members often held the key positions in family companies. Owner-managed businesses had return on equity (ROE) 75% higher than that of businesses managed by outsider CEOs (Monsen & Associates, 1968). A study in the United States by Anderson and Reeb (2003) proved that family businesses had Tobin'Q ratio and ROA higher when the family members were CEOs.

Villalonga and Amit (2006) conducted a study on the performance of family managed and non-family managed businesses in the United States. The findings showed that family ownership would only create values when the founders were CEOs or Chair-people with outsider CEOs. Experts also found out that family companies who intended to hand down the business to their future generations had better performance than the rest. The study further indicated that Family CEOs played an important part in managing families companies, and family members played the role of managers (Miller & Breton-Miller, 2006). Daily and Dollinger (1992) remarked that outsider CEO managed companies were of larger sizes and carried out more adventurous business strategies. On the contrary, family owned companies were of similar sizes and very rarely carry out adventurous business strategies yet their performance was higher.

Jayaraman, Khorana, and Nelling (2000), based on their analysis of financial indicators believed that size and time of operation affected and reduced the performance of Family CEOs. The study by John and Associates (2010) showed that Family CEO managed companies did not increase business performance. However, when the successor was descended from the founder family, the company value was enhanced again. This can be explained that since the founder CEOs were not skillful managers and / or the founder CEOs dispersed their assets in order to cut taxes.

Conversely, other experimental studies demonstrated that outsider CEO managed companies operated much better than the founders. Lauterbach and Vaninsky (1999) differentiated between the companies managed by a representative of the owner and the outsider CEO managed companies. This analysis showed that owner managed companies had much worse business performance. Family companies therefore should change their model of management, strengthen power devolvement, attract talents, and prepare for the process of succession (Sharma, Chrisman, & Chua, 1997). A study in Taiwan by Lin and Hu (2007) suggested that family companies had limited money flows and could not control the money flows which required the professional skills from outsider CEOs.

Outsider CEOs of families were usually selected as a solution for solving the company's difficulties (Helmich & Brown, 1972). When facing request for major, comprehensive changes, outsider managers shall be a more priority choice, since they are not bound by the former structures and the traditional values of the company. Kosnik (1987) emphasized that an outsider successor was the most effective remedy to ensure the comprehensive change in the management model of the company. Hambrick and Mason (1984) argued that when the company operated poorly and needed a "new causative agent of change", more likely the successor would be outside the family members. Overview of the studies above indicated that no absolute agreement was reached on the choice of successor from outsiders or the family members.

2.2 Succession Features in Vietnamese Family Companies

In management, Vietnamese family companies demonstrate three basic features: Firstly, with respect to capital, money of the company is from the owners. In other countries, a company is regarded as a family company when the owner holds approximately 15-20% of capital. Secondly, with respect to size, that is the type of small and medium-sized enterprise. When talking about size, one usually thinks about productivity or performance. Small and medium-sized enterprises generate more jobs for society than major companies, and this is what professional observations show. Nevertheless, they can keep as small as that forever, that's why in the conjunction between small-sized enterprises and the increase in employment there appear new enterprises. It's thanks to the emergence of new companies that there is the increase in employment which was previously abstract. With respect to flexibility, small and medium-sized enterprises are capable of revolving with economic situations quicker than major enterprises. However, compared with major enterprises, they are worse in many aspects. Major enterprises greatly benefit from their size of production, on a large scale and at cheap price. Thirdly, with respect to management and control, in Vietnamese family companies, the owners (founders) manage for convenience's sake, basing on the talent they are endowed and from their experiences. Among these three features, the mode of management is the most difficult one when talking about legacy succession.

Factual observations of the legacy succession process in some Vietnamese family companies in recent times have indicated that this process can be effected in one of the two ways: (share) capital transfer or power succession. Capital transfer: This kind of transfer is simple. Making testament is a way for the children to hold the parents' capital in the business. The other way is the parents make a contract to transfer their capital to the children in accordance with the company's charter. In family companies, owners usually invest almost all their money, if insufficient, they would mobilize from their kinship, relatives. I.e. the company limited form. When the company flourishes, the owner often divide the shares among the efficient associates. By then, in the company's capital, there is the part of outsiders, yet this accounts for not a high proportion. Power succession: It is this kind that is really legacy succession. In this regard, there is a suggestion that a certain roadmap should be designed, with lessons on change management, at the same ripe time, so as to avoid conflicts and fill the gaps between generations.

In Vietnam, family company is a very popular form. Among the Top 500 largest businesses of Vietnam, over one third follows the "nepotism" model. As from 1986 to date, Vietnamese family companies have made remarkable contributions to the development of the country, have made gigantic changes in business, and quite a few among them have become big businesses/trade names in the economy of Vietnam, such as Phu Nhuan Gold, Silver and Precious Stone, Kinh Do Confectionery, Minh Long I Ceramics and Porcelains, Saigon Paper, Dai Dong Tien Plastics, etc. However, according to the results of a survey conducted by the Saigon Economic Times, Vietnamese family companies have had so many difficulties in existing and developing of the second, and especially the third, generation. The succession in the form of "from generation to generation" actually started from the second generation. And even the succession between these two generations also caused a family company to begin to have conflicts in interests and signs of decline. The strongest point of a family company is the "co-operation" relations among the key members. Nevertheless, it is in that very strongest point there exists a weak point, which is essential and decisive for the development of the family company. When implementing the succession between generations, successors have to share their ownership in the spirit of "partner" relationship. They have to decide together on the way of managing and controlling, for example, common assets. At this moment, issues concerning business management arise. A majority of family companies will suffer a defeat in solving this administration issue. In the context of Vietnam, this study hypothesizes that succession to CEO inside the family has considerable impact on improving business performance than employing CEO outside. The study supposition is:

Hypothesis: *The company's business performance is under the positive influence of the choice of CEO being a family member.*

3. Methodology

This study was conducted by developing the hypotheses and reevaluating by quantitative method. The survey was carried out between July 2011 and March 2012 with the set of samples of 65 Vietnamese family companies, including 41 listed mass companies and 24 unlisted companies. The data for this study was collected from the secondary sources: corporate consolidated financial statements, data available at Ho Chi Minh City Stock Exchange (HSX) and Hanoi Stock Exchange (HNX), Vietstock Information Gate, State Securities Commission of Vietnam (SSC), Vietnamese Securities Magazine of SSC. Table 1 summarizes the basic figures about the set of samples.

Table 1. Findings of companies under survey

Variable	Frequency	%	Variable	Frequency	%
Kind of Successor			*Number of years in operation:*		
Founder (generation F1)	46	70.8	6 - 10 years	5	7.7
Successor (generation F2)	19	29.2	10 - 15 years	17	26.2
Total	65	100%	15 - 20 years	16	24.6
CEO Classification			>20 years	27	41.5
CEO Insider	59	90.8	*Total*	65	100%
CEO Outsider	6	9.2			
Total	65	100%			
Geographical Location:			*Industries*		
Hanoi	11	16.9	Agriculture & Forestry	7	10.7

Ho Chi Minh City	19	29.2	Textile & Garment	8	12.3
Danang	6	9.2	Aquaculture & Breeding	7	10.7
Haiphong	6	9.2	Hospitality	6	9.2
Ninh Binh	8	12.3	Manufacturing	9	13.8
Binh Duong	5	7.6	Food & Beverage	4	6.3
Can Tho	3	4.6	Construction & Real Estate	8	12.3
Other Provinces, Cities	7	11.0	Finance & Banking & Insurance	5	7.8
			Other	11	16.9
Total	65	100%	*Total*	65	100%

Source: Summary of Survey Results.

Table 1 shows that over 70% of leaders of family companies belong to the first generation/founder (F1) group, and this group has made remarkable contributions to Vietnam's economic growth. Whereas, the second generation/successors (F2) accounts for a lower proportion, i.e. approx. 30%. The majority of Vietnamese family companies today are being run by founders, however, this succession tendency is ever growing. A large number of Vietnamese family companies have handed down part or all their rights to control and leadership to subsequent generations to ensure that the process of family power succession will still exist in the later generations. Table 1 also indicates that most Vietnamese family companies are still being managed by CEO family members (90.8%). Meanwhile, there are only 6 family companies having CEO outsiders to manage, including two foreigners.

This research model was based on the model by Anderson and Reeb (2003) and Haniffa and Hudaib (2006), in order to examine the impact of the choice of CEO family members or outsiders on the company's performance.

$$PERF = b_0 + b_1CEO_{it} + b_2DEBT_{it} + b_3FAGE_{it} + b_4FSIZE_{it} + b_5CP_{it} + b_6IP_{it} + b_7TS_{it} + b_8OTH_{it}$$

where:

PERF = Business performance measured by Tobin's Q index equal to (Market value of share capital + total liability) / (Book value of total assets)

CEO = type of CEO. Variable CEO measured by dummy variable (0, 1). In case of CEO family members, it takes the value of 1, otherwise, it is 0.

DEBT = Debt. Debt is the book value of the long-term debt against total assets. In family companies, the first generation has a tendency to use to the maximum owner's equity against the capital borrowed from outside (Sonfield & Lussier, 2004). Chen, Chen, and Cheng (2008) pointed out that family companies faced a great deal of difficulty in mobilizing capital from the outside (borrowing at interest from the bank or through stock exchange).

AGE = Operating time defined by the number of years from company incorporation. Business operating time is an important and decisive factor of growth and the possibility of winding up. When operating time prolongs, managers will accumulate and acquire more knowledge and skills in management (Evans, 1987). Studies pointed out that new companies, of some certain size, would grow quicker than senior companies (Dunne & Hughes, 1994). Senior companies became rigid by the routine procedures, passive and conservative business processes thereby achieving low performance (Boeker, 1997).

SIZE = Size measured by logarithm of the book value of total assets. The size of the company won't be expanded if the managers, out of their fear for loss of control power, are not willing to employ sources from the outside (Church, 1993). Small-sized family firms would encounter many difficulties in the process of training and developing managers as successors, as well as in accepting advices from outside experts on planning the succession process. Otherwise, major companies may probably have numerous qualified and experienced on the spot to guaranty the succession (Harveston, Davis, & Lyden, 1997).

CP = consumer product

IP = industrial product

TS = Trade & service

OTH = Other business line

Such business lines as consumer goods, industrial products, trade & service, construction, projects of infrastructure, technology, hotel and real estate will have value of 1, and the rest is 0. Haniffa and Hudaib (2006), in a study conducted in Europe, observed that in some industries, family companies operated more effectively than in others.

4. Research Results

Data was used according to a panel data table and the correlation coefficient between variables was analyzed. Since the difference in the correlation coefficient between variables was not too large, and the VIF multicollinearity test outcome was 1.33, the issue of multicollinearity did not affect the model results (Table 2).

Table 2. Pearson correlation inspection

Variables	Q	CEO	DEBT	SIZE	AGE	CP	IP	TS	OTH
Q	1								
CEO	0.25***	1							
DEBT	-0.09**	-0.02	1						
SIZE	-0.21***	-0.07**	0.47***	1					
AGE	-0.04**	-0.05	0.11***	0.17***	1				
CP	-0.09	0.10***	-0.07**	-0.21***	-0.05	1			
IP	0.05**	0.03	-0.08**	-0.17***	0.02	-0.35***	1		
TS	-0.23***	-0.07**	0.06	0.01	0.05	-0.19***	-0.26***	1	
OTH	0.14***	-0.02	0.02	0.17***	0.10***	-0.17***	-0.24***	-0.13***	1

Note. Multicollinearity test VIF=1.33;

*Significant at p < .01; **Significant at p < .05; ***Significant at p < .10.

Table 2 shows that CEO has positive correlation with Tobin's Q variable (statistically significant at the rate of 1%). This indicates that CEO family members have positive impact on the company performance. Meanwhile, there exists a negative relationship between Tobin's Q and size, operating time, commercial service and other industries.

Next, panel data was regressively analyzed in two ways: random effect and fixed effect. In order to find out which regression analysis was most suitable between these two methods, the author employed Hausman test (Hausman, 1978). Table 3 displays regression results. The Chi2 rate of Hausman test indicates that the fixed effect was the most suitable model in this study.

Table 3. Results by two regression methods

Variables	Random effect		Fixed effect	
	Coefficients	p value	Coefficients	p value
Constant	0.628**	0.001	0.879**	0.001
Family CEO (H1)	0.009**	0.001	0.110**	0.001
DEBT	- 0.103	0.839	0.005	0.839
SIZE	-0.212**	0.001	-0.219**	0.001
AGE	-0.053**	0.001	-0.182**	0.001
CP	0.372**	0.002	0.041**	0.002
IP	0.293**	0.001	0.083**	0.001
TS	0.051**	0.003	0.051**	0.003
OTH	-0.097**	0.001	0.131**	0.001
R2	14.21		12.87	
Adj. R2	13.00		12.35	
Hausman test Chi2 = 5.52**				

*Significant at p < .01; **Significant at p < .05; ***Significant at p < .10.

According to table 3, variable CEO has a positive relationship with business performance (Tobin's Q variable) of the company. This result can be accounted for as due to the majority of CEO family members spend most of their time working at the companies controlled by their families, these CEOs have more profound knowledge of the organizational and personnel structures, particularly the corporate cultural values than CEO outsiders. Such

CEOs may arrive at optimal decisions and usually make succession plans. This finding supported the previous studies (Anderson & Reeb, 2003). Hence, hypothesis H1 was accepted in this study.

Company size variable has a positive impact on Tobin's Q variable at the rate of 0.219 and is statistically significant at the rate of 10%. This rate indicates that when size increases by 1 unit, effect will increase by 0.219 unit. This can be accounted for as that large-sized family companies may produce more profit then small-sized ones, hence such companies will have more resources and opportunities in training and fostering leaders-successors and in making more systematic succession plans, as well as employ great resources to seek for advices from outside experts to make it possible for the process of making succession plans (Trow, 1961).

Operating time variable has a negative impact on Tobin's Q variable at the rate of 0.182 and is statistically significant at the rate of 10%. This finding indicates that when family companies thrive over time, their business performance goes down. Senior companies normally achieve their business performance ratio lower than that of small companies (Dunne & Hughes, 1994). The possible reasons are that in the course of time company management principles grow rigid according to the habit of strictly observing leader's (founder's) decisions, there is no innovation in the business process thus this keeps the performance going down (Boeker, 1997).

Most industries have positive impact on Tobin's Q variable. In other words, almost all different industries make remarkable contributions to improving the performance of family companies.

In short, this study confirms that family CEOs improve the company performance higher than outside CEOs. CEO successors have also been proved to improve the company performance more as CEO founders. Contacts with the business environment, education, experience and sufficient business capital may provide young CEOs with values added to better manage family companies than founders. Irrespective of limits, the focus of this study is on family companies only. In the future, the research model may be extended to embrace the companies not fall under the management of family companies, from that to draw more typical conclusions.

5. Implications and Suggestions

Study findings shows that the choice of CEO successors being family members has the positive impact on the business performance of Vietnamese family companies. Administering a business cannot avoid conflicts and administering an Eastern family business is more likely to cause conflicts. That's why power succession in Vietnamese family companies should follow a roadmap which is consistent with the modes of change administration, at a proper and ripe time. To begin with a legacy succession process, obviously the first generation of leaders had to think about investment in the next generation right from the very early days, since children when growing up would not automatically have the intention to become a member of their parents' companies. In many cases, the young successors even did not care for or did not want to engage in the undertaking in the future.

Children's knowledge about their parents' businesses must be trained and plans of development must be reckoned very early. That means parents ought to have plans for the development of generations after them. In addition to the school's training in knowledge, skills, altitudes like other children, families have to spend time training and exert influence on subsequent generations in at least four aspects:

- Enhancing awareness to help families succeed: Success of family companies should be very early recognized by children. Subsequent generations may live better, have more passion and be happier if learning that they are part of their family companies' future.
- Arousing love for the family business: Having a passion for the business the families are pursuing is usually the main reason for subsequent generations to be engaged in. That is also why young generations wish to work outside so as to acquire further profession and experience first. Having a solid knowledge about the undertaking which the family is pursuing is the factor to create success, loyalty and passion in subsequent undertaking.
- Creating challenges for development: If subsequent generations can work right from the time they are still very young, they will early be aware of the value of money they make. Choice of profession at higher education and choice of working for another company after graduation will become clearer in the roadmap of returning to family company succession at the proper time.
- Creating a sense of earning money: A reasonably interesting thing is that attitudes towards money differ greatly between the two consecutive generations. It is unnecessary that if a generation has a passion for earning money then so will be the next one. Therefore, if a generation wishes to have a succession in earning money in their own way, they must train this sense for the next generation.

The study pointed out the necessity to give priority to choice of succession among family members; however, there should be the harmony of interests between family career and that of associates, employees of the company. Although everyone knows that this is the career of a family, the way of running the whole system does not reveal too distinctively the "nepotic" characteristic, let's open wide many windows, provide much space for the talents who are working within the framework of manufacturing - business so that they can demonstrate their capacities and initiatives and benefit the company. There should also be stress placed on "seeking talents" by looking for administrators more talented than family members without worrying about being ruled over by expenses as the success brought about by the talented administrator for the company is much greater. Legacy successors ought to create a balance between families & associates in organizations, provide them with a lot of necessary information, including unfavourable information in business. It is associates who will help propose ways to handle and tackle in an objective manner, thus further bringing into play families' strength.

6. Concluding Remarks

This study indicates that the choice of CEO successors being family members has the positive impact on performance (Tobin's Q) of Vietnamese family companies. In the future, studies with longer periods of time will produce more objective results in exploring the relationship between choice of successors and business performance.

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