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21

*The Key to Success of
Family Businesses:
an empirical analysis
based upon survey results*

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Summary

1. This paper examines “innovativeness”, “managerial structure”, “corporate philosophy (managerial philosophy)”, and “managerial succession” as factors likely to have an impact upon family businesses (FBs) on the basis of a questionnaire survey conducted in October 2007 by the Mizuho Research Institute Ltd. (MHRI). Each of these factors is tested by statistical analysis to find out which factors possess significant correlations with performance (the change in number of employees).
2. Summarizing the analytical results, we found a clear correlation between the variable regarding corporate philosophy and the performance of FBs. More specifically, performance was significantly lower among companies “which do not engage in efforts to instill corporate philosophy”. This indicates the importance of efforts to share common values in the corporate philosophy – regardless of what they may be – within the company in day-to-day operations. Furthermore, we also found that performance was significantly higher among companies which had “altered their corporate philosophy in the past”. Putting aside the question of whether a company had altered the essential core value of its corporate philosophy, the results suggest that the addition of values to keep in touch with the times and the modernization of the language used to express the philosophy lead to a better understanding of the company both within and outside of the company and ultimately raise its performance.
3. Secondly, in terms of managerial succession, we found that post-succession conditions have a greater impact upon performance than pre-succession conditions. More specifically, we found that the shorter the time span since succession of top management, the lower the company’s performance, suggesting that it takes a certain period of time for adjustment until a company is able to return to its normal course of business under the successor. Furthermore, the results also indicate that in cases

- of FBs with second or third-generation CEOs, in other words relatively new FBs without long-established histories, the strong interference by the preceding CEO in managerial matters after succession has a negative impact upon performance.
4. Thirdly, particularly in cases of FBs with long-established histories, we found that growth potential tends to be higher among companies possessing a positive attitude toward the development of new products/services (in other words, innovative companies). The findings shed light upon the fact that many established companies advocate a “tradition of continuous innovation” and that a large number of established companies have expanded their business through unrelenting efforts toward innovation.
 5. Lastly, turning to variables regarding managerial structure (such as the composition of board members, the intra-company decision-making process, the existence of a person acting as a *de facto* aide to the CEO (hereinafter referred to as the “CEO’s aide”) and the state of internal systems/rules), we could not find a significant correlation with growth potential in many of these variables. Having said so, the importance of a CEO’s aide tended to be higher among small and medium-sized FBs.

1. Introduction

There are approximately 2.6 million corporate enterprises in Japan, of which more than 95% or about 2.4 million companies are “*douzoku-gaisya*” (family concerns) in which a small number of family members hold the majority of stocks (according to FY2006 tax statistics of Japan’s National Tax Agency). While the term *douzoku-gaisya* is a term used in tax law matters, companies in which members of the founding family possess a controlling interest or controlling shares are referred to generally as family businesses (hereinafter referred to as “FBs”).

Among these FBs, there are many companies which date more than 100 years since establishment. Despite the absence of accurate statistics, Japan is said to be home to ten thousands of FBs with long-established histories (hereinafter referred to as either “established company/companies” or “established FBs”) according to credit research companies. Japan is exceptional in the large number of established companies. What are the factors differentiating established companies from relatively young companies? Put differently, what are the managerial characteristics of FBs which are achieving continuous growth?

These questions prompted us at MHRI to conduct a questionnaire survey of the member firms of MHRI’s Forum–M membership organization in October 2007 (“*Questionnaire Survey on the Continuous Development of Companies*”, hereafter referred to as the “*MHRI Survey*”). In the *MHRI Survey*, we posed questions on the following five factors which are likely to have an impact upon the performance of FBs: “innovativeness”, “check-and-balance functions toward top management”, “managerial control structure”, “corporate philosophy (managerial philosophy)”, and “managerial succession”.

The five factors were selected for the following reasons. Firstly, “innovativeness” was selected as a factor on the basis of the hypothesis that there is a certain relationship between innovativeness and the longevity of a corporation, stemming from observations that many established companies are run under a corporate philosophy of “continuous innovation”.

Secondly, it would be important to incorporate some sort of “check-and-balance function” in the decision-making process in the case of FBs which are generally subject to weaker external checks such as those by general stockholders in comparison to listed companies. In the *MHRI Survey*, we asked questions on the number of non-family board members and the existence of external board members and external auditors from the perspective of structures to serve as checks and balances.

Thirdly, we focused upon “managerial control structure” from the

perspective of “organizational development as a company” which is necessary along with the development of a company. In the case of small and medium-sized FBs with a limited number of employees and range of business, top management (note 1) would be able to keep a watchful eye upon the entire company. Conversely, a company may grow beyond the control of top management in the event it becomes larger than a certain size. For a company to grow beyond this stage, it would be necessary to upgrade its system of managerial control through the clarification of its internal rules in written form and the introduction of managerial accounting to grasp various facets of corporate activity in the form of quantified information.

Fourthly, “corporate philosophy” serves as a kind of mechanism of corporate governance which regulates all members of the company, and is generally perceived to be important for the continuous development of business. However, the recent frequency of corporate scandals among Japan’s FBs prompts us to question that a more important task might be to share common values in the corporate philosophy within the company. Thus, in the *MHRI Survey*, we asked questions on what concrete measures were taken to instill their corporate philosophy.

Lastly, the importance of “managerial succession” in FBs is beyond doubt. In contrast to non-FBs where top management positions are selected through rigorous competition within the company, top management of FBs are succeeded from among limited members of the founding family. The key to success of this process is to carry out well-planned preliminary preparations for the successor to acquire sufficient managerial capabilities and to set up an intra-company system to provide adequate support for the new CEO upon succession. Furthermore, the smooth succession of personal assets such as company stocks and commercial land is also important in the case of FBs.

The results of the *MHRI Survey* revealed the existence of a certain relationship between several factors and the performance of FBs (note 2). Although the details of the findings are compiled in Horiuchi and Noda (2008), the analysis therein is a mere cross

analysis between the factors and corporate performance and stops short of clarifying which factors possess high correlations with performance.

This paper explores what factors possess significant correlations with performance after managerial succession by a probit analysis with various variables regarding “innovativeness”, “managerial structure” (“check-and-balance function” and “managerial control structure”), “corporate philosophy”, and “managerial succession”.

The method of analysis in this paper may be differentiated from preceding works in terms of the three following characteristics. Firstly, this paper incorporates variables regarding corporate philosophy. The majority of existing research on corporate philosophy is either case studies of specific companies or cross analyses of survey results. Very few studies explore relationships such as those between corporate philosophy and performance using statistical methods.

Secondly, this paper compares established companies with relatively young companies. In a large number of existing works on established companies, the survey subjects are limited to established companies, at least in the case of Japan (note 3). Not many step further to compare relatively young companies with established companies to find out and analyze the characteristics of established companies. In this paper, we classified the FBs which provided responses to the *MHRI Survey* into “second and third generation FBs” and “fourth generation or older FBs (deemed as “established FBs”)” in terms of the generation of the top senior management or CEO and carried out observations on how the factors affecting performance differ between the two groups.

The third characteristic of this paper is its comparison of companies classified by corporate size. As mentioned earlier, in the event a company grows larger than a certain size, it would become necessary to upgrade the managerial control structure since the CEO of FBs would not be able to keep an eye over the entire company. We thus explored the differences – mainly in terms of managerial control structure – by comparing the respondent

companies classified into the following three groups according to the number of employees: “less than 100”, “100 – less than 200” and “200 –”.

In the preceding section, we have set forth the overall framework and significance of this paper. Lastly, touching briefly upon the format of this paper, we shall provide an overview of the responses, mainly in the form of the items picked up in the form of variables in empirical analysis in Section 2. In Section 3, we shall provide an explanation of the results of analysis subsequent to an explanation of the variables used in statistical analysis and a presentation of a hypothesis. Section 4 sets forth our concluding comments.

2. The factors related to the growth of FBs revealed in the *MHRI Survey*

In this Section, we shall provide an overview of the results of the *MHRI Survey*. The *MHRI Survey* was conducted in October 2007 toward its member firms. The respondents were selected from among unquoted companies satisfying certain criteria such as the number of employees (more than 30 employees) and credit-ratings (a mark of at least 50 by the Teikoku Databank, a Japanese credit research company). We sent questionnaires to 6,000 companies and received effective responses from 1,702 companies (ratio of effective responses: 28.4%).

(1) The fundamental attributes of the responding companies

a. The founding family’s participation in management

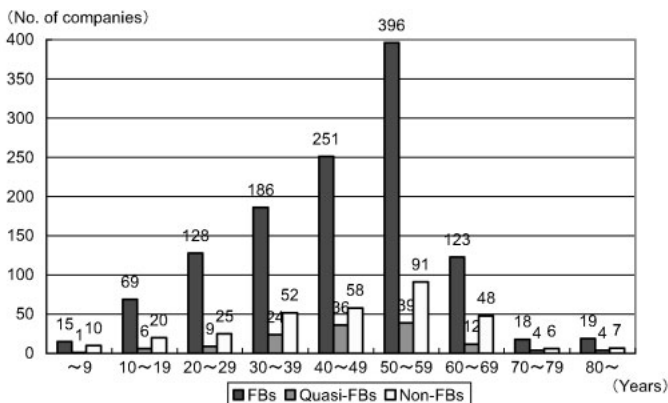
While the main target of the *MHRI Survey* is FBs controlled by founding families, questionnaires were also sent to many companies other than FBs. Classified in terms of management participation, 1,205 (70.8%) of the respondents were “FBs” in which the founding

family possesses representative rights, 135 (7.9%) were “quasi-FBs” in which members of the founding family participate in management as directors without representation, and 317 (18.6%) were non-FBs in which the founding family does not participate in management.

b. Company history

The *MHRI Survey* did not include any direct questions on company history. By classifying the respondents on the basis of Teikoku Databank’s data regarding the “date of incorporation”, we found that a large number of respondents were concentrated within the band of 50–59 years. **Chart 1** indicates that the number of respondents grows less as one moves away from this band. The foregoing reveals that the core segment of the *MHRI Survey* are companies possessing considerably long histories.

Chart 1: Number of companies responding to the *MHRI Survey* (by the number of years elapsed since establishment)



Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

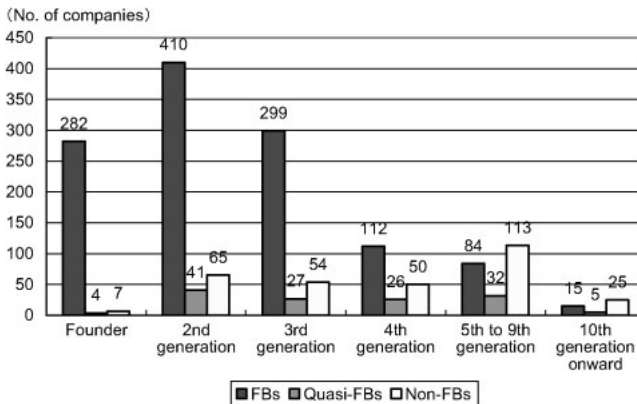
c. The generation of the CEO

Next, by counting the number of generations since the founder, we found that most FBs fell within the founding generation to the

third generation and that most non-FBs fell into the fifth to ninth generation (**Chart 2**).

Such difference between FBs and non-FBs stems most likely from the difference in the CEO’s years in office. In the case of non-FBs, the tenure of the CEO is subject to certain limitations in most cases because CEOs are usually selected through promotions up the corporate hierarchy. In contrast, the tenure of CEOs is usually not defined in the case of FBs. In the event the CEO is contemplating succession by one’s child, it would be necessary for the incumbent CEO to remain in management until the child has acquired sufficient managerial capabilities. On average, the number of years in office is presumably longer among FBs.

Chart 2: Number of companies responding to the *MHRI Survey* (by the generation of the CEO)



Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

(2) Innovativeness

The term “established company” or “time-honored company” may conjure images of a company with a dogged loyalty to tradition succeeded through generations. However, preceding works indicate that there are actually more established companies which have

engaged in the development of new products/services to match the current times, while honoring traditional values including technology, know-how, and corporate cultures which were nurtured through the years (note 4).

In a question on the stance toward development of new products/services, we found that the majority of the respondents of the *MHRI Survey* – which possess on average a corporate history of 45 years – take a “balanced” stance toward development. 74.9% of all FBs said that they “develop new products/services in accordance to the change of times while preserving existing products/services”. On the other hand, 8.9% of FBs fell into the “conservative” category, citing “the importance of preserving existing products/services and a relatively subdued attitude toward the development of new products/services” and 13.9% of FBs fell into the “innovative” category, saying that they “have taken a positive stance toward the development of new products/services to match the times without much heed for preserving existing products/services”.

The observations above regarding a company’s stance toward development in terms of corporate performance (change in number of employees) revealed that there was a larger percentage (note 5) of responding FBs with strong performance (note 6) among the group taking an “innovative” and “balanced” stance toward development than the group taking a “conservative” stance. The findings suggest that a flexible and positive product development stance in touch with environmental shifts is stimulating growth and continuation of businesses among FBs.

(3) Managerial structure

While FBs enjoy the advantage of prompt decision-making under the CEO’s leadership and the ability to take large business risks, they also possess weaknesses such as the lack of external checks especially by general stockholders. Accordingly, check-and-balance functions toward top managerial positions from both within and outside the company are extremely important in the case of FBs.

Even though the CEO would be able to keep a watchful eye over

the entire company in the case of small and medium-sized FBs, this would not be possible in the event a company grows larger than a certain size. At this stage, an organizational overhaul – or an improvement of the managerial control structure – would be necessary.

Although the direction of control would flow in the opposite direction in the case of “check-and-balance functions toward top management” (from bottom or outside to top of the company) and in the case of “managerial control” (from top to bottom of the company), this paper will consider both as issues within the scope of “managerial structure” in the tally of responses to the *MHRI Survey*.

In the *MHRI Survey*, we questioned the member companies on the following four factors regarding “managerial structure”: (1) the founding family’s degree of control (the composition of board of directors), (2) the FB CEO’s leadership skills (the state of consensual decision-making at the board of directors or other decision-making body), (3) human resources to assist the FB CEO (the “CEO’s aide”), and (4) other systems/internal rules for management control (for example, managerial accounting, intra-company rules, external directors/auditors).

a. The composition of board of directors

In most FBs, a large part of the stocks (voting rights) and board positions (such as directors) are held by the founding family. To find out the degree of control by the founding family, we asked questions on the composition of the board of directors and found that members of the founding family dominated the board of directors in only 12.9% of FBs. 33.5% said that “the majority of directors are members of the founding family” and 45.2% said that “up to one-half of the directors are members of the founding family.”

b. The state of consensual decision-making

In response to our question regarding the decision-making body, the majority of FBs said that they hold regular meetings for consensual decision-making. Only 14.6% said that “regular meetings

for consensual decision-making are not held and most decisions are made by the CEO” As for the conduct of the meeting, 19.5% said that the decision-making process was conducted upon discussion under the leadership of the CEO (top management) and 53.2% said that “ultimate decision-making was conducted under the CEO’s initiative despite the placement of emphasis upon discussions among members”. Together, the respondents in these groups made up more than 70% of responding FBs. Only a few FBs said that the CEO does not take initiative (companies responding to the effect that “emphasis is placed upon discussions among members and the CEO does not rush to make a decision until a consensus can be discerned” (11.4%).

A look at the relationship between the conduct of decision-making meetings and performance indicates a lower percentage of strong performance among responding FBs in which the CEO does not take initiative (note 7). This suggests that emphasis upon consensus-formation at the expense of prompt decision-making does not serve as a positive factor for the performance of FBs.

c. The “CEO’s aide”

In many FBs, there are person(s) who assume staff roles or serve as reliable advisors to the CEO (hereinafter referred to as the “CEO’s aide”). Their existence may not be underestimated in the case of FBs where authorities and responsibilities are concentrated upon the CEO. For example, the Small and Medium Enterprise Agency of Japan came up with an analysis in 2003 that SMEs with person(s) assuming roles as aides possess high growth potential.

In response to our question whether there are such persons among executives and regular employees other than founding family members, more than 80% of the FBs said that there are such persons (“among executives” (68.0%), “among employees” (13.0%)).

Furthermore, we found a higher percentage of FBs performing well among the group with CEO’s aides in comparison to those without (note 8). This suggests the importance of the role played by

the “No. 2” serving as an aide to the FB CEO.

d. Other systems and internal rules for managerial control

In addition to the foregoing, the *MHRI Survey* asked questions on the following five items regarding systems and internal rules for managerial control: (1) managerial accounting, (2) rules on personnel affairs such as wages and promotions, (3) rules on administrative authorities, (4) external director/auditors, and (5) internal whistle–blowing systems (note 9).

The results reveal that managerial accounting, rules on personnel affairs, and rules on administrative authorities were established in most FBs. On the other hand, the survey revealed rather unremarkable results regarding the establishment of external directors/auditors and internal whistle–blowing systems (**Chart 3**).

**Chart 3: Systems and internal rules for managerial control
(FBs with CEOs of the second or older generations)**

	“Established by or prior to the preceding CEO”	“Established by the incumbent CEO”	“Do not have such systems/rules”
Managerial accounting	47.7	45.2	5.5
Rules on personnel affairs such as wages and promotions	49.2	44.5	4.9
Rules on administrative authorities	36.0	40.2	22.0
External directors/auditors	25.7	19.4	52.3
Internal whistle-blowing systems	7.1	13.8	76.9

Note: The figures refer to the percentage of responding companies (%).
Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

Looking at the relationship between the establishment of such systems/rules and performance, we found a common trait with respect to all five systems/rules. The group of FBs in which such systems/rules were “established by the incumbent CEO” had a higher percentage of companies achieving strong performance than the group which “do not have such systems/rules” or which had “established by or prior to the preceding CEO” (note 10). These results

suggest the possibility that the competitiveness of FBs is raised through the development of these systems/rules for management control.

(4) Corporate philosophy

Corporate philosophy is an embodiment of a company's ideology and *raison d'être* and is perceived to possess significant importance as a kind of mechanism of corporate governance which regulates all members of the company. However, the recent frequency of corporate scandals among Japan's FBs prompts us to question that a more important task might be to share common values in the corporate philosophy within the company. Therefore, we questioned the respondents regarding the substance and alterations (if any) of the corporate philosophy and measures taken to instill the corporate philosophy within the company.

a. The substance of the corporate philosophy

In the *MHRI Survey*, we asked the respondents to list up to three concepts which are valued in particular as their corporate philosophy (including company creed, company motto or codes of action), the largest number of companies (approximately two-thirds of FBs) cited "the achievement of customer satisfaction" (**Chart 4**). Furthermore, we found a tendency for newer generations to place emphasis upon business stability (selecting items such as "eternity of one's own company", and "focus upon core business"). In contrast, many founders placed emphasis upon growth (items such as "expansion and growth of business").

Chart 4: Ideals emphasized in corporate philosophy (FBs, by generation of CEO)

	Total < N=1198 >	Founder < N=280 >	Second generation < N=407 >	Third generation < N=299 >	Fourth generation onward < N=209 >
Achievement of customer satisfaction	68.4	69.3	69.8	66.2	67.5
Provision of high quality goods and services	44.5	42.5	47.2	46.8	38.3
Happiness of employees	43.4	42.5	45.0	42.8	43.1
Contribution to society	29.2	26.4	30.7	27.4	32.5
Eternity of one's own company	21.0	17.1	20.4	22.7	25.4
Focus upon core business	20.4	14.3	21.1	23.4	23.0
Expansion and growth of business	15.4	25.0	11.5	13.7	12.0
Good relations with business counterparts	14.3	15.7	14.0	11.0	16.7
Technological innovation	7.9	8.6	8.1	8.0	6.7
Supply at fair prices	6.5	7.1	6.4	6.4	6.2
Globalization of business	3.0	4.6	2.5	3.0	1.9
Supply at low prices	2.3	2.5	2.0	2.3	2.4
Stockholders' interests	1.5	1.8	0.7	1.7	2.4
Others	0.9	1.1	0.5	0.7	1.9
None in particular	0.6	0.0	0.7	0.7	1.0

Notes: 1. The figures refer to the percentage of responding companies (%). Up to three responses allowed.

2. N = no. of responding companies

Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

b. Alteration of corporate philosophy

To our query whether the corporate philosophy had been altered in the past, the majority (52.6%) responded that “the corporate philosophy has never been altered since establishment”. Even so, note that 45.4% of the FBs said that “they had altered the corporate philosophy”. In particular, 36.1% provided responses to the effect that the corporate philosophy had been altered during the current generation.

The results that nearly half of FBs had altered their corporate philosophy were rather unexpected, given the strong impression in general that corporate philosophy is (or should be) succeeded through the generations. Having said so, “alterations of corporate philosophy” covers a wide range of changes of varying degree from (1) alterations which replace the former corporate philosophy with

an entirely different new philosophy, (2) the addition of new elements to match the times to the existing corporate philosophy, (3) the “translation” of antiquated language to more contemporary expressions, and (4) the conversion of abstract corporate philosophy to more concrete terms which are easier to understand (including, for example, the drafting of specific codes of action). The responses that “they had altered the corporate philosophy” most likely includes all of the foregoing degrees of alterations.

Turning to performance, we found that performance was relatively higher among the group which had altered their corporate philosophy in the past than the group which had never made alterations to their philosophy (note 11). We presume that by altering their corporate philosophy (such as translations into contemporary expressions or conversions into specific codes of action), FBs were able to achieve a deeper understanding of its corporate philosophy within the company.

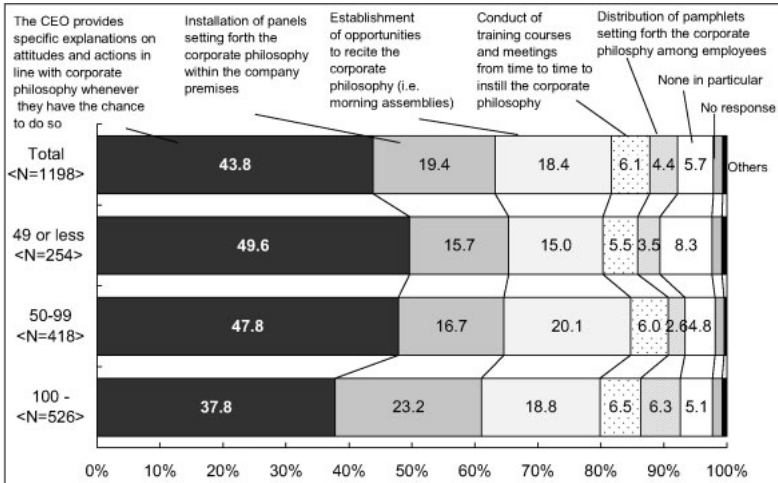
c. Measures to instill the corporate philosophy within the company

As mentioned above, the mere existence of a corporate philosophy is insufficient. A more important task might be to share common values in the corporate philosophy within the company. We thus asked what measures were taken in order to instill the corporate philosophy within the company and found that the largest number of FBs said that “the CEO provides specific explanations on attitudes and actions in line with corporate philosophy whenever they have the chance to do so” (**Chart 5**). This indicates that top management of FBs place emphasis upon speaking directly with its employees rather than perfunctory methods such as the installation of panels setting forth the corporate philosophy within the company premises or the recitation of the corporate philosophy during morning assemblies/meetings.

In terms of the size of companies, we found that the larger the company, the lower the percentage of companies saying that top management speaks directly with employees and the higher the

percentage of responses citing the installation of panels and recitation at morning assemblies, due perhaps to the difficulty to maintain close communications between top management and employees when a company grows larger.

Chart 5: Measures to instill the corporate philosophy within the company (FBs, by number of companies)



Note: N = no. of responding companies
 Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

(5) Managerial succession

Lastly, we shall provide explanations on the results of responses concerning managerial succession. The *MHRI Survey* posed questions in two phases; namely “managerial succession from the preceding CEO to the incumbent CEO” and “managerial succession from the incumbent CEO to the successor”. Here, we shall touch upon the former which is related to the empirical analysis in the subsequent section (note 12).

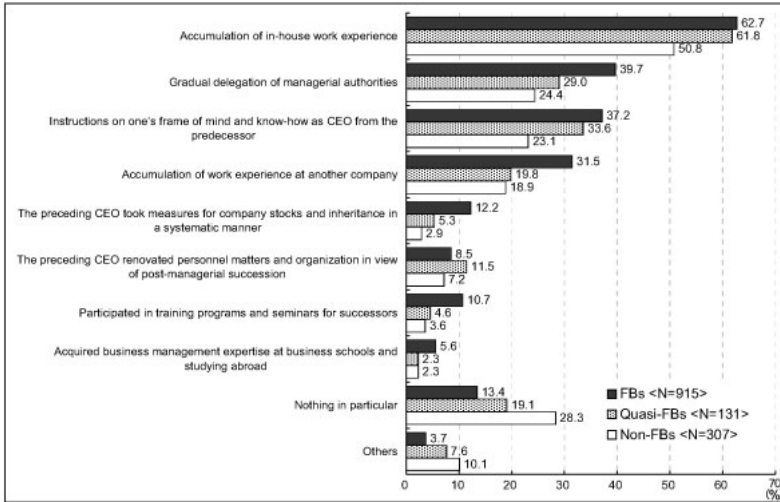
a. The relationship between the preceding CEO and the incumbent

The results of our survey regarding the relationship of the incumbent CEO with the preceding CEO revealed that nearly two-thirds (65.0%) of incumbent CEOs were “children” of the preceding CEO in FBs. When including “sons-in-law/adoptees” (7.1%), “brothers” (6.2%), “spouses” (1.2%), and “other family members” (9.2%), nearly 90% of FB CEOs (88.7%) are the kin of the preceding CEO. The rest of the responses are comprised of “management/employee other than family members” (6.7%) and “others/no responses” (4.3%).

b. Preparations for managerial succession from the preceding CEO

We then posed questions on what were the most important matter(s) in the preparations for managerial succession from the preceding CEO to the incumbent. An overwhelming majority (62.7%) of FBs cited the “accumulation of in-house work experience” (**Chart 6**). We also found a relatively large number of responses by FBs regarding a “gradual delegation of managerial authorities” (39.7%) and “instructions on one’s frame of mind and know-how as CEO from the predecessor” (37.2%). On the other hand, 13.4% of FBs said that “no particular measures were taken” in contrast to 28.3% of non-FBs which chose the same response. The foregoing provides a glimpse that FBs’ take more time and efforts for preparations for managerial succession than non-FBs whose CEOs are selected through in-house promotions.

Chart 6: Preparations for managerial succession from the preceding CEO (the second generation onward)



Notes: 1. The figures refer to the percentage of responding companies (%). Up to three responses allowed.

2. N = no. of responding companies

Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

c. Involvement of preceding CEO after managerial succession

Although the involvement of the preceding CEO in management is not a unique phenomenon to FBs, there are many cases in which the predecessor provides instructions or advice toward the successor and even continues to hold *de facto* leadership in extreme cases even after the transfer of representation rights to the succeeding CEO. If the successor lacks experience or if there are no capable advisors (the “CEO’s aide”) to the successor, the successor would benefit from the predecessor’s advice provided from time to time as necessary. However, as indicated by the Small and Medium Enterprise Agency (2004), excessive advice by the predecessor may serve as a detriment to the successor’s leadership and the formation of trust between the successor and in-house staff.

In response to our question on the involvement of the predecessor after succession, 24.2% of FBs said that “the

predecessor did not participate at all in decision-making and refrained from providing virtually any instruction/advice”. In other words, the predecessor had been involved in some way in three-fourths of FBs. That said, in many of these cases, the involvement was limited to frequencies and contents only on an “as necessary” basis. To be more precise, the responses to the effect that “the incumbent sought the predecessor’s instruction/advice as necessary” (34.3%) and “the predecessor provided instruction/advice every now and then” (25.0%) combined made up approximately 60% of all responses. Note that the percentage of responses that “the predecessor continued to hold substantive decision-making rights” (8.6%) and “the incumbent sought the predecessor’s instruction/advice on a daily basis” (6.4%) remained on a single-digit level.

In relation to performance, we found that performance was relatively higher among the group which said that “the predecessor did not participate at all in decision-making and refrained from providing virtually any instruction/advice” in comparison to companies choosing other responses – in particular those which cited a high degree of involvement by the predecessor (note 13). As mentioned before, even though the necessity for the predecessor’s advice would differ depending upon the successor’s experience and the surrounding staff, the most desirable role of the predecessor after withdrawal from top management positions would be an “advisor in times of trouble” who provides minimum necessary advice when the successor is (or appears to be) troubled and refrains from unnecessary involvement.

3. Empirical analysis: identifying the factors correlated with performance after managerial succession

As we observed in the previous section, the *MHRI Survey* indicated that the following factors are likely to have an impact upon the performance of FBs: “innovativeness”, “managerial structure”, “corporate philosophy (managerial philosophy)”, and “managerial succession”. In this section, we shall identify which factors have a strong correlation with corporate performance and conversely which factors do not possess definite correlations through probit analysis incorporating the above factors as independent variables.

In this paper, the sample will be limited to companies in the *MHRI Survey* of which are headed by CEOs of the second generation onward counting from the founder. This is because we have included the factor regarding managerial succession as an independent variable. Furthermore, as stated in Section 1, we grouped the respondents into “second and third generation FBs” and “fourth generation or older FBs” in terms of the generation of the top senior management or CEO in order to discern differences between established FBs and other FBs. Likewise, we also grouped the respondents into the following three categories according to the number of employees to shed light upon the differences in terms of corporate size: “less than 100”, “100 – less than 200” and “200 –”.

Let us proceed with an explanation of the variables and to present and analyze the results (for the definitions of the variables and sample statistics, refer to Annexes 1 and 2 at the end of this paper).

(1) The dependent variable

In preceding works, the change in number of employees is frequently used as an indicator to gauge the performance of SMEs. Even though indicators on profit would seem to be a more appropriate measure, the percentage change in number of employees is used instead because there are wide annual

fluctuations in figures on profits and the possibility of accounting manipulation of profits and costs in the case of SMEs.

Thus, this paper will also use indicators on the number of employees as the dependent variable. The dependent variable is set by creating dummy variables as follows to the question, “how has the number of employees changed since managerial succession to the present”: “1” for companies which said that employee growth was following an “upward trend (a sharp upward trend + a mild upward trend)”, “0” for companies which said that employee growth was following a “flat or downward trend (a flat trend + a mild downward trend + a sharp downward trend)”. As a result of probit analysis, readings which show a statistically significant positive correlation between each of the independent variables and the dependent variable indicate that “companies with a larger value attributed to the independent variable may have a higher probability of strong growth performance after managerial succession” (for the value of variables, refer to Appendix Table 1: Definition of variables).

(2) The independent variables

a. Innovativeness

As indicators to gauge the degree of innovativeness, a dummy variable were set as follows: “1” for “innovative” or “balanced” companies and “0” for “conservative” companies (refer to Section 2. (2)). The hypothetical sign condition with respect to this variable is positive.

In **Chart 7**, we compared the mean value of the variables among companies with strong performance after managerial succession (companies with the number of employees following an upward trend) and the mean value of the variables among companies with weak performance after managerial succession (companies with the number of employees following a flat or downward trend) and tested whether the variance is statistically significant by using the *t*-test. Looking at the variable on innovativeness, we found that innovativeness was significantly higher among companies with

stronger growth potential.

b. Managerial structure

With respect to managerial structure, we set variables for seven out of the eight items in the *MHRI Survey* explained under Section 2 (the composition of board of directors, the state of consensual decision-making, the “CEO’s aide”, managerial accounting, rules on personnel affairs, rules on administrative authorities, external directors/auditors, and internal whistle-blowing systems), excluding the rules on personnel affairs (note 14) due to its strong correlation with other variables.

(a) The composition of board of directors

While there are various possible patterns regarding the composition of management of FBs, the merits and demerits of a board of directors comprised solely of members of the founding family would be as follows. Although the loss of diversity in opinions may serve as a detriment, the possibility that it may speed up the decision-making process and lead to efficient management may not be ruled out altogether.

In this paper, companies which responded that “all directors are members of the founding family” in the *MHRI Survey* are given a variable of “1” and all other companies were given a variable of “0”. It is difficult to determine whether the sign condition is positive or negative in the case of this variable. *T*-tests revealed that the percentage of companies in which “all directors are members of the founding family” was significantly higher among companies with high growth potential (**Chart 7**).

(b) The state of consensual decision-making

Section 2 indicated the possibility that companies in which the CEO does not exercise leadership in consensual decision-making at board of directors meetings (and other such meetings) may be inferior in terms of growth potential. In view of these findings, companies which responded that “emphasis is placed upon

discussions among members and the CEO does not rush to make a decision until a consensus can be discerned” (companies in which the CEO does not exercise leadership in a positive manner) are given a variable of “1” and all other companies were given a variable of “0”. The hypothetical sign condition with respect to this variable is negative. However, *t*-tests revealed that there were no significant differentials in the mean values of these variables between companies with high growth potential and those with low growth potential (**Chart 7**).

(c) The “CEO’s aide”

Given the possibility that the existence of the “CEO’s aide” to assist the CEO in decision-making and conduct of business affects the performance of FBs, we attributed a variable of “1” to companies which responded that “there is a person acting as the ‘CEO’s aide’” and “0” to companies which said that “there are no persons acting as the ‘CEO’s aide’”. The hypothetical sign condition with respect to this variable is positive. The results of *t*-tests were also consistent with our hypothesis (**Chart 7**).

(d) Managerial accounting, rules on administrative authorities, external directors/auditors, internal whistle-blowing systems

As we said in Section 2, a trait common to all these four systems is that companies which had upgraded these systems under the current CEO had higher growth potential according to the *MHRI Survey*. In other words, the results indicate the possibility that the competitiveness of FBs is raised through the improvement of managerial control.

Thus, we attributed the following variables to the four systems/rules: “1” for companies in which the systems/rules were “established by the current CEO” and “0” for companies which “have not established” or “established by or prior to the preceding CEO”. In view of Section 2, the hypothetical sign conditions for all four variables are presumed to be positive. The results of *t*-tests

confirmed, as expected, the existence of a significant differential with respect to the following three factors: (1) managerial accounting, (2) rules on administrative authorities, and (3) external directors/auditors. However, even though the sign condition was positive, we could not confirm a significant differential as expected with respect to the internal whistle-blowing system (**Chart 7**).

c. Corporate philosophy

On corporate philosophy, we created two variables; one regarding whether a company is taking efforts to instill the corporate philosophy within the company and one on whether a company had altered its corporate philosophy in the past.

(a) Efforts to instill corporate philosophy

The majority of companies which provided responses to the *MHRI Survey* possess corporate philosophies (**Chart 4**). Regardless of what such corporate philosophy might be, as we pointed out in Section 2, it would seem more important to raise the awareness on the corporate philosophy within the company so as to avoid the corporate philosophy from degenerating into a hollow phrase. We therefore attributed a variable of “1” to companies which said that they are “not engaged in any particular efforts to instill the corporate philosophy” and “0” to companies which said that they are “engaged in efforts of some sort”. The hypothetical sign of the coefficient is negative. The results of *t*-tests were consistent with our hypothesis, indicating that the lower the growth potential of a company, the higher the likelihood that it is not engaged in efforts to instill its corporate philosophy (**Chart 7**).

(b) Alteration of corporate philosophy

As mentioned in Section 2, we found that the majority of companies had “altered their corporate philosophy”, including the “translation” of the original language of the corporate philosophy set forth by the founder to more contemporary expressions and its conversion to more concrete terms which are easier to understand.

Furthermore, the findings also suggest the possibility that companies which had altered their corporate philosophy exhibit relatively higher performance. Here, we attributed the following variable: “1” for companies which said in the *MHRI Survey* that they “have altered their corporate philosophy in the past” and “0” for companies which said that they “have never made alterations to their corporate philosophy”. The presumed sign of the coefficient is positive. Again, the results of *t*-tests were also consistent.

d. Managerial succession

Turning to managerial succession, we shall use the following four variables as variables with the potential to affect performance after succession.

(a) Pattern of succession

There are frequent indications in preceding works (note 15) on managerial succession that post-succession performance of companies succeeded by family members such as children (“intra-family succession”) tends to fall below the performance of “non-family succession” where management is succeeded by employees and persons from outside the company.

We created a dummy variable to serve as an independent variable as follows: “1” for companies which said in the *MHRI Survey* that they had and conducted “intra-family succession” from the preceding to the incumbent CEO and “0” for companies which had conducted “extra-family succession”. If we were to take into account the conclusions in many of the preceding works, the sign conditions of the coefficient for this variable would presumably be negative. However, the results of *t*-tests were contrary to assumptions, revealing that intra-family successions were significantly higher among companies with higher growth potential (**Chart 7**).

(b) Preparations for succession

Preparations and plans on a long-term perspective are considered important for smooth managerial succession. Several

preceding works (note 16) have shown that efforts to take a certain amount of time for preparations have a positive impact upon post-succession performance.

Here, we created a variable as follows: “1” for companies which said in the *MHRI Survey* that they had done “nothing special to prepare for succession” and “0” for all other companies (companies which had made preparations of some sort). Although the sign condition of the coefficient for this variable would naturally be negative, *t*-tests did not reveal significant differentials between companies with high growth potential after succession and companies with low post-succession growth potential (**Chart 7**).

(c) Involvement by the preceding CEO after succession

Managerial succession does not end at the point in time of the CEO’s succession. Rather, its success depends upon the smoothness of business operations after succession. Various factors such as the personality and managerial capabilities of the succeeding CEO, ongoing creditworthiness in the eyes of business counterparts, and relations with in-house parties (board members and employees) are perceivable as factors which affect management after succession by the succeeding CEO. In this paper, we set forth a variable on “involvement by the preceding CEO” by the degree of involvement: “4” for “extremely strong”, “3” for “slightly strong”, “2” for “slightly weak” and “1” for “extremely weak”. As indicated by the results of the *MHRI Survey* described in Section 2, the sign condition of the coefficient with respect to this variable is presumed to be negative. The results of *t*-tests show that the preceding CEO’s managerial involvement is significantly stronger among companies with low growth potential, which is consistent with our hypothesis (**Chart 7**).

(d) Number of years elapsed since managerial succession

It is generally believed that in managerial succession, a certain amount of time for adjustment is necessary for a company to return to its normal course of business after succession. The results of preceding works more or less support this hypothesis (note 17).

In this paper, we shall also include the number of years elapsed since managerial succession in the independent variables. With respect to the five options to the question, “how many years have elapsed since managerial succession from the preceding to the incumbent CEO?” (“less than 5 years”, “5 years – less than 10 years”, “10 years – less than 20 years”, “20 years – less than 30 years” and “30 years –”), we set dummy variables with “1” for companies which fall within the purview and “0” for companies which do not fall within the purview for all five options (note 18), with the dummy variable for “5 years – less than 10 years” as the base category. Assuming that there is an adjustment period of several years after managerial succession, the results of estimations are expected to be negative for the coefficient for “less than 5 years”. Even though the way in which the variables are created is different from the foregoing, *t*-tests reveal that the number of years elapsed is significantly longer for companies with high growth potential. This is consistent with the foregoing hypothesis (Chart 7).

e. Control variables

In addition to the independent variables listed above, we created dummy variables regarding industrial sector, geographic region, company size and company history to control corporate attributes. As for industrial sector, we categorized the respondents to the *MHRI Survey* into four categories including “manufacturers”, “wholesale, retail and restaurants”, “services” and “others” and created dummy variables (industrial sector dummy) with “1” for companies which fall within the industrial sector and “0” for companies which do not. Given the disproportionate concentration of the respondents of the *MHRI Survey* to metropolitan Tokyo and the prefectures of Kanagawa, Saitama and Chiba, we created a dummy variable (the metropolitan area dummy), with “1” for companies in the metropolitan area and “0” for all other companies. Regarding company size, we used the values derived by logarithmic conversion of the number of employees of the relevant company according to latest research results by the Teikoku Databank. Lastly, with respect

to company history, we used the generation of the CEO as an alternative indicator, given the large number of companies for which data on the founding year are not available in the *MHRI Survey*.

Chart 7: The variables on post-succession performance and the difference with mean values (FBs)

Variables		Companies which said that employee growth was following an "upward trend"	Companies which said that employee growth was following a "flat or downward trend"	Difference with mean values
		(a)	(b)	(a)-(b)
Innovativeness	Stance toward new product/service development	0.93	0.87	0.06 ***
Managerial structure	The composition of board of directors	0.16	0.11	0.06 ***
	The state of consensual decision-making	0.12	0.14	-0.03
	The "CEO's aide"	0.85	0.80	0.05 **
	Managerial accounting	0.46	0.22	0.24 ***
	Rules on administrative authorities	0.43	0.22	0.21 ***
	External directors/auditors	0.17	0.10	0.08 ***
Corporate philosophy	Internal whistle-blowing systems	0.13	0.11	0.03
	Efforts to instill corporate philosophy	0.03	0.09	-0.06 ***
Managerial succession	Alteration of corporate philosophy	0.53	0.38	0.15 ***
	Pattern of succession	0.93	0.88	0.05 ***
	Preparations for succession	0.08	0.07	0.01
	Involvement by the preceding CEO after succession	1.89	2.09	-0.20 ***
Others	No. of years elapsed since managerial succession (1)	2.91	2.30	0.61 ***
	Generation of CEO	1.74	2.12	-0.38 ***
	Size of company (logarithmic conversion of no. of employees)	2.01	2.01	-0.00
No. of observations		402	409	

Notes: 1. The values of the variable are as follows: 1 for "less than 5 years", 2 for "5 years – less than 10 years", 3 for "10 years – less than 20 years", 4 for "20 years – less than 30 years", and 5 for "30 years –".
2. The ***, ** and * are the results of *t*-tests, indicating levels of significance at 1%, 5% and 10% respectively.

Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

(3) Results of estimates ①: comparison of FBs and non-FBs

Even though this paper focuses upon FBs, we shall first compare the results of estimates between FBs and non-FBs (**Chart 8**). From a bird's eye perspective, we were able to obtain results consistent with our initial assumption with approximately one-half of the independent variables with respect to FBs (details will be provided later), when expanding the level of significance to 10%. In contrast, only two of the independent variables were deemed to have

statistical significance with respect to non-FBs.

Looking closer at each of the variables, note that there are wide differences with respect to the variable on corporate philosophy. In the case of FBs, the estimates yielded results showing a significant correlation as expected between performance and “measures to instill corporate philosophy (were not taken)” or “alteration of corporate philosophy (had been conducted in the past)”. In contrast, significant results were not obtained for non-FBs. This suggests that corporate philosophy is not as important for non-FBs as in the case of FBs.

Secondly, as expected, the correlation between performance and the “number of years elapsed since managerial succession (is short)” was significantly negative for FBs. Even though the sign condition was negative in the case of non-FBs, the results did not satisfy the level of significance. Since CEOs of non-FBs are, as a general rule, selected from among persons possessing qualifications for top management positions through rigorous in-house competition, the “adjustment period” necessary from the assumption of office to actual performance may be short.

Thirdly, the results revealed that the correlation between performance and the “involvement of the preceding CEO after managerial succession (is strong)” is significantly negative in both FBs and non-FBs. The results indicate the possibility that the previous CEO’s exercise of strong influence upon management in positions such as counsel or advisor has a negative effect upon performance.

Chart 8: Probit estimates (FBs and non-FBs)

	Variables	Hypothetical sign condition of coefficient	Total of responding companies	FBs	Quasi-FBs	Non-FBs
Innovativeness	Stance toward new product/service development	+	0.190	0.322 *	0.615	0.003
Managerial structure	The composition of board of directors (1)	+ or -		0.287 *		
	The state of consensual decision-making	-	-0.042	-0.060	-0.194	-0.046
	The "CEO's aide" (1)	+		0.213	-0.167	
	Managerial accounting	+	0.349 ***	0.383 ***	-0.823 *	0.898 ***
	Rules on administrative authorities	+	0.206 **	0.163	1.164 **	-0.047
	External directors/ auditors	+	-0.008	0.083	0.045	-0.487
Corporate philosophy	Internal whistle-blowing systems	+	0.076	-0.090	0.513	0.365
	Efforts to instill corporate philosophy	-	-0.561 ***	-0.606 **	-0.904	-0.585
Managerial succession	Alteration of corporate philosophy	+	0.189 **	0.292 ***	0.279	-0.148
	Pattern of succession	-	-0.111	0.012	-0.031	-0.320
	Preparations for succession	-	0.025	0.160	-0.049	-0.228
	Involvement by the preceding CEO after succession	-	-0.133 ***	-0.125 *	0.028	-0.267 **
	No. of years elapsed since managerial succession	-	-0.256 **	-0.284 *	-0.134	-0.354
	Less than 5 years	Base category				
	5 years - less than 10 years		+	-0.168	-0.139	0.417
10 years - less than 20 years	+		0.228	0.192	0.810	1.077
20 years - less than 30 years	+		0.150	0.213		-0.374
30 years -	+					
No. of observations			1116	723	100	244
Prob > chi2			0.000 ***	0.000 ***	0.160	0.000 ***
Pseudo R2			0.104	0.130	0.204	0.170

- Notes: 1. Items which were not included in the questionnaires toward non-FBs.
 2. Descriptions on the dummy variables regarding industrial sector, the metropolitan area, company size and company history have been omitted.
 3. The ***, ** and * are the results of *t*-tests, indicating levels of significance at 1%, 5% and 10% respectively.

Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

(4) Results of estimates ②: details regarding FBs

In the section below, we shall take a closer look at the results of estimates regarding FBs through each of the independent variables. In doing so, we shall also take into consideration the generation of the CEO and size of companies (**Charts 9 and 10**).

a. Innovativeness

The results of estimates regarding “positive stance toward new (product/service) development to keep in touch with changing times”, used as a proxy variable to show the degree of innovativeness, revealed a significantly positive (albeit a 10%-level) correlation for FBs overall.

Let us look closer in terms of the generation of the CEO. In the case of FBs headed by second or third generation CEOs, the sign is

positive despite the absence of any significance. In contrast, in the case of fourth generation or older FBs (so-called “established FBs”) the results were significantly positive at the 5%-level, confirming a correlation between innovativeness and growth potential. While we mentioned before that many established companies advocate a “tradition of continuous innovation”, the findings shed light upon the fact that a large number of established companies have expanded their business through unrelenting efforts toward innovation.

b. Managerial structure

Overall, we could not obtain significant results as expected with respect to the variables regarding managerial structure. We shall look at each of the variables below.

(a) The composition of board of directors

It was confirmed that growth potential tends to be higher among FBs whose boards of directors are dominated by members of the founding family (despite a significance level of 10%). In particular, the correlation was significantly positive at the 5%-level among established FBs. A plausible reason for the findings is that the existence of time-honored management philosophies (such as corporate philosophy and managerial guidelines) and concerted efforts toward business promotion by family members who share such common values are leading to the maintenance of high growth in the case of established companies.

(b) The state of consensual decision-making

Despite the hypothesis that growth potential would lag among companies headed by CEOs who do not exercise leadership in meetings such as the board of directors, we could not obtain supporting results either in terms of FBs as a whole or in terms of the generation of the CEO or company size.

(c) The “CEO’s aide”

We could not obtain significant results to support our hypothesis

that growth potential tends to be higher among companies with persons serving as the CEO's aide. The sole exception was a significant positive correlation among FBs with employees less than 100 persons at the 10%-level. The results suggest that persons assisting the CEO play a relatively more important role in smaller FBs.

(d) Managerial accounting, rules on administrative authorities, external directors/auditors, internal whistle-blowing systems

We found that growth potential of FBs was significantly higher among companies adopting managerial accounting under the current CEO. As initially expected, the findings indicate the possibility that a company's growth potential may be lifted through the adoption of managerial accounting. Nevertheless, in terms of generations of CEOs and company size, we did not find a significant correlation with respect to established FBs and FBs with at least 100 employees. This may stem from the fact that many of the companies with these attributes have already adopted managerial accounting by or prior to the preceding CEO and hence the small sample of companies which adopted the system under the current CEO.

As for the rules on administrative authorities, external directors/auditors, and internal whistle-blowing systems, we could not obtain significant results.

c. Corporate philosophy

The results revealed that the variable regarding corporate philosophy had the strongest correlation with growth potential after managerial succession.

(a) Efforts to instill corporate philosophy

As expected, we found that growth potential tends to be lower among FBs which do not engage in efforts to instill corporate philosophy. The results underscore the importance of daily efforts to instill the corporate philosophy within the company, regardless of

what values or philosophy a company might choose to embrace.

(b) Alteration of corporate philosophy

The results confirmed that FBs which have altered their corporate philosophy in the past tend to possess higher growth potential (however, there is no significant correlation from the fourth generation onward). Setting aside the question of whether or not alterations are made to the core essence of the corporate philosophy, it is quite likely that additions of new aspects to keep in touch with the times or “translations” of the original language of the corporate philosophy to more contemporary expressions, lead to a better understanding of the company both within and outside of the company and ultimately raise its performance.

b. Managerial succession

The results regarding managerial succession vary widely among the independent variables.

(a) Pattern of succession

The results did not confirm a difference in performance due to patterns of succession. As far as the analysis in this paper is concerned, the results do not support the hypothesis that “there is a higher possibility of a successor with inferior capabilities being selected in the case of family successions”.

(b) Preparations for succession

All in all, the estimates did not yield statistically meaningful results and did not support the hypothesis that “post–succession performance tends to be lower among companies which have not prepared for managerial succession”. Even though there is no simple interpretation of these results, some of the plausible reasons may be that companies with a solid managerial system are not affected by the lack of preparations or that preparations do not possess substantial impact since the difficulties facing CEOs only become evident after succession.

(c) Involvement by the preceding CEO after succession

In terms of overall FBs, the results were as expected; a significantly negative correlation (albeit a significance level of 10%), suggesting the possibility that the preceding CEO's continuation of strong involvement in management even after retirement serves as a negative impact upon corporate performance.

In terms of the generation of CEOs, the result was significantly negative at the 1%-level with respect to second and third generation FBs, indicating a strong negative correlation between the preceding CEO's involvement and growth potential. On the contrary, the result regarding established FBs was significantly positive at the 5%-level. Despite the difficulty of interpreting this result, one possible reason is that established FBs possess a wealth of anecdotes and morals stemming from their long history which are succeeded from the preceding CEO to the successor in a gradual process, which can be utilized in business management.

(d) Number of years elapsed since managerial succession

In terms of overall FBs, the results confirmed that growth potential tends to be lower among companies with a relatively short time span (number of years) since managerial succession (albeit a significance level of 10%). The findings suggest the possibility that performance stagnates during the "adjustment phase" lasting for several years after managerial succession until management under the succeeding CEO returns to its normal course of business.

The results for FBs categorized in terms of corporate size revealed a significantly negative correlation only in companies with "100 – less than 200 employees". While the interpretation of these results is extremely difficult, the absence of a negative correlation between the number of years elapsed since managerial succession and growth potential may stem from factors such as the following: (1) CEOs of small FBs may keep a watchful eye over the entire company, and (2) conversely, larger FBs may be equipped with a structure for management as an organization even though they may be family-owned.

Chart 9: Probit estimates (FBs: comparisons by the generation of the CEO)

Variables		Hypothetical sign condition of coefficient	Total of responding companies	2nd or 3rd generation	4th generation onward
Innovativeness	Stance toward new product/service development	+	0.322 *	0.132	1.366 **
Managerial structure	The composition of board of directors (1)	+ or -	0.287 *	0.209	0.881 **
	The state of consensual decision-making	-	-0.060	-0.148	0.049
	The "CEO's aide" (1)	+	0.213	0.223	0.158
	Managerial accounting	+	0.383 ***	0.391 ***	0.334
	Rules on administrative authorities	+	0.163	0.056	0.580 **
	External directors/auditors	+	0.083	0.158	-0.085
	Internal whistle-blowing systems	+	-0.090	-0.254	0.054
Corporate philosophy	Efforts to instill corporate philosophy	-	-0.606 **	-0.560 **	-1.315 *
	Alteration of corporate philosophy	+	0.292 ***	0.350 ***	0.074
Managerial succession	Pattern of succession	-	0.012	-0.415	0.320
	Preparations for succession	-	0.160	0.134	0.053
	Involvement by the preceding CEO after succession	-	-0.125 *	-0.231 ***	0.329 **
	No. of years elapsed since managerial succession	-	-0.284 *	-0.199	-0.458
	Less than 5 years				
	5 years - less than 10 years	Base category			
10 years - less than 20 years	+	-0.139	-0.077	-0.061	
20 years - less than 30 years	+	0.192	0.370 *	0.213	
30 years -	+	0.213	0.289	0.197	
No. of observations			723	545	178
Prob > chi2			0.000 ***	0.000 ***	0.003 ***
Pseudo R2			0.130	0.124	0.193

Notes: 1. Descriptions on the dummy variables regarding industrial sector, the metropolitan area, company size and company history have been omitted.

2. The ***, ** and * are the results of *t*-tests, indicating levels of significance at 1%, 5% and 10% respectively.

Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

Chart 10: Probit estimates (FBs: comparisons by company size)

Variables		Hypothetical sign condition of coefficient	Total of responding companies	Less than 100 employees	100 - less than 200 employees	200 employees -	
Innovativeness	Stance toward new product/service development	+	0.322 *	0.198	0.406	1.021 *	
Managerial structure	The composition of board of directors (1)	+ or -	0.287 *	0.439 **	-0.477	1.007	
	The state of consensual decision-making	-	-0.060	0.103	0.275	-0.820 *	
	The "CEO's aide" (1)	+	0.213	0.300 *	-0.059	0.537	
	Managerial accounting	+	0.383 ***	0.535 ***	0.103	0.602	
	Rules on administrative authorities	+	0.163	0.035	0.291	0.529	
	External directors/auditors	+	0.083	-0.035	0.508	0.069	
	Internal whistle-blowing systems	+	-0.090	-0.519 **	-0.450	0.755 **	
Corporate philosophy	Efforts to instill corporate philosophy	-	-0.606 **	-0.538 *	-1.010 *	-0.876	
	Alteration of corporate philosophy	+	0.292 ***	0.339 **	0.484 **	0.261	
Managerial succession	Pattern of succession	-	0.012	-0.263	0.528	0.715	
	Preparations for succession	-	0.160	0.370	-0.870	0.722	
	Involvement by the preceding CEO after succession	-	-0.125 *	-0.157 *	-0.033	-0.124	
	No. of years elapsed since managerial succession	-	-0.284 *	-0.096	-0.785 **	-0.300	
	5 years - less than 10 years	Base category	+	-0.139	-0.365 *	0.118	-0.223
	10 years - less than 20 years	+	0.192	0.071	0.240	0.194	
20 years - less than 30 years	+	0.213	-0.016	0.506	-0.491		
30 years -	+						
No. of observations			723	395	186	142	
Prob > chi2			0.000 ***	0.000 ***	0.000 ***	0.000 ***	
Pseudo R2			0.130	0.148	0.210	0.317	

Notes: 1. Descriptions on the dummy variables regarding industrial sector, the metropolitan area, company size and company history have been omitted.

2. The ***, ** and * are the results of t-tests, indicating levels of significance at 1%, 5% and 10% respectively.

Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

4. Conclusion

In this paper, we selected the following four factors which are thought to have important implications for FBs to succeed and develop their business over the long term: “innovativeness”, “managerial structure”, “corporate philosophy, and “managerial succession”. We then explored, using statistical analysis methods, whether there are correlations between these factors and corporate growth potential. Although the results of analysis regarding each of the variables are set forth under Section 3, we shall provide a brief summary of our findings below.

Firstly, the results of our analysis confirmed a clear correlation

between the variable regarding corporate philosophy and growth potential of FBs. More precisely, we found a significantly low performance among companies which “do not engage in efforts to instill corporate philosophy”. The findings suggest the importance of efforts to share the common values in the corporate philosophy – regardless of what that may be – within the company in day-to-day operations. Furthermore, we found that performance was significantly higher among companies which had “altered their corporate philosophies in the past”. Putting aside the question of whether a company had altered the essential core value of its corporate philosophy, the results suggest that the addition of values to keep in touch with the times and the modernization of the language used to express the philosophy lead to a better understanding of the company both within and outside of the company and ultimately raise its performance.

Secondly, turning to managerial succession, the results suggest that post-succession conditions have a greater impact upon performance than prior preparations. We found that performance tends to be lower among companies with a short history (number of years) since generational transition, indicating that there is a certain adjustment period until management returns to its normal course of business under the succeeding CEO. Moreover, in the case of relatively new FBs which may barely be described as “established” with second or third generation CEOs, the results suggest the possibility that the strong involvement of the preceding CEO in management even after succession serves as a negative effect upon performance.

Thirdly, in particular with respect to established FBs, growth potential tends to be higher among companies taking a positive stance toward the development of new products and new services (innovative companies). The findings shed light upon the fact that many established companies advocate a “tradition of continuous innovation” and that a large number of established companies have expanded their business through unremitting efforts toward innovation.

Lastly, we could not find a significant correlation with growth potential for many of the variables regarding managerial structure. That said, the results indicate the possibility that the adoption of “managerial accounting”, which is a basic system for managerial control, serves to lift corporate growth potential. Furthermore, the findings also indicate the possibility that the importance of the “CEO’s aide” who acts as a valuable assistant to the CEO tends to increase in small and medium-sized FBs.

As stressed in Section 1, the analysis of factors including corporate philosophy is one of the prominent characteristics of this paper. The findings provide us with keen insight regarding the important role of corporate philosophy in the performance of FBs.

On the other hand, due to the usage of the *MHRI Survey* questioning respondents on a wide range of potential factors affecting corporate performance, the framework of the analysis has become rather diffuse. Accordingly, this paper could not probe into the depths explored by preceding works. This in turn provides us with a target for further research. Looking forward, we wish to conduct a more focused study on the factors behind the continuous development of FBs on the basis of new data and surveys, for example by specializing on corporate philosophy.

Appendix Table 1: Definition of variables

	Classification	Variables	Hypothetical sign condition of coefficient	Value of variables	Source of data	
Dependent variable	Performance after succession	Change in number of employees after succession		1: Upward trend 0: Flat or downward trend		
Independent variables	Innovativeness	Stance toward new product/service development	+	1: Positive stance toward new product/service development 0: Passive stance toward new product/service development		
		Managerial structure	The composition of board of directors	+ or -	1: Dominated entirely by members of the founding family 0: Existence of director(s) from outside the founding family	
			The state of consensual decision-making	-	1: No rush to make a decision until a consensus can be discerned 0: "Exercise of leadership", or "no regular meetings for consensual decision-making"	
			The "CEO's aide"	+	1: Existence of a person acting as the CEO's aide 0: Absence of a person acting as the CEO's aide	
		Managerial accounting	+	1: Established by the current CEO 0: "Have not established" or "established during or prior to the preceding CEO"		
		Rules on administrative authorities	+	1: Established by the current CEO 0: "Have not established" or "established during or prior to the preceding CEO"		
		External directors/auditors	+	1: Established by the current CEO 0: "Have not established" or "established during or prior to the preceding CEO"		
	Internal whistle-blowing systems	+	1: Established by the current CEO 0: "Have not established" or "established during or prior to the preceding CEO"			
	Corporate philosophy	Efforts to instill corporate philosophy	-	1: Not engaged in any particular efforts to instill the corporate philosophy 0: Engaged in efforts of some sort	MHRI Survey	
		Alteration of corporate philosophy	+	1: Altered their corporate philosophy in the past 0: Have never made alterations to their corporate philosophy		
	Managerial succession	Pattern of succession	-	1: Intra-family succession 0: Extra-family succession (including patterns other than intra-family succession)		
		Preparations for succession	-	1: No special preparations 0: Preparatory measures of some sort were taken		
		Involvement by the preceding CEO after succession	-	1: Extremely weak involvement by the preceding CEO 2: Slightly weak involvement by the preceding CEO 3: Slightly strong involvement by the preceding CEO 4: Extremely strong involvement by the preceding CEO		
		No. of years elapsed since managerial succession	- (Dummy variables for "less than 5 years")	With respect to the five options to the question, "how many years have elapsed since managerial succession from the preceding to the incumbent CEO?" ("less than 5 years", "5 years - less than 10 years", "10 years - less than 20 years", "20 years - less than 30 years" and "30 years or longer"), we set dummy variables with "1" for companies which fall within the purview and "0" for companies which do not fall within the purview for all five factors, with the dummy variable for "5 years - less than 10 years" as the basic category		
	Control variables	Generation of CEO (company history)		1: 2nd generation 2: 3rd generation 3: 4th generation 4: 5th- 9th generation 5: 10th generation -		
Company size			Logarithmic conversion of the number of employees			
Industrial sector dummy			4 categories (manufacturing, wholesale and retail trade, restaurants, services, others)	Teikoku Databank		
Metropolitan area dummy		1: Metropolitan area (Tokyo, Kanagawa, Saitama, Chiba) 0: Areas other than metropolitan area				

Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

Appendix Table 2: Descriptives (FBs)

	Variables	No. of samples	Mean	Standard deviation	Minimum	Maximum
Innovativeness	Stance toward new product/service development	810	0.90	0.30	0	1
Managerial structure	The composition of board or directors	798	0.14	0.34	0	1
	The state of consensual decision-making	814	0.13	0.34	0	1
	The "CEO's aide"	815	0.82	0.38	0	1
	Managerial accounting	812	0.33	0.47	0	1
	Rules on administrative authorities	812	0.33	0.47	0	1
	External directors/auditors	804	0.14	0.34	0	1
	Internal whistle-blowing systems	808	0.12	0.33	0	1
Corporate philosophy	Efforts to instill corporate philosophy	813	0.06	0.23	0	1
	Alteration of corporate philosophy	810	0.46	0.50	0	1
Managerial succession	Pattern of succession	808	0.91	0.29	0	1
	Preparations for succession	826	0.07	0.26	0	1
	Involvement by the preceding CEO after succession	813	1.99	0.79	1	4
	No. of years elapsed since managerial succession (note)	816	2.60	1.26	1	5
Others	Generation of CEO	826	1.92	1.04	1	5
	Company size (logarithmic conversion of no. of employees)	826	2.01	0.34	1.50	3.10

Note: The values of the variables are as follows: "less than 5 years" = 1, "5 years – less than 10 years" = 2, "10 years – less than 20 years" = 3, "20 years – less than 30 years" = 4, "30 years –" = 5

Source: Mizuho Research Institute Ltd., *Questionnaire Survey on the Continuous Development of Companies*.

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Notes:

- 1 The terms “top management”, “top senior management”, and “CEO” will be used interchangeably in this paper.
- 2 For example, growth potential was higher among companies with person(s) acting as the CEO’s aide.
- 3 Examples of preceding works on established companies which have conducted questionnaire surveys are Kanda and Iwasaki (1996), Yokozawa (2000), Tokyo Shoko Research (2003) and Takeda (2004). None of the foregoing have conducted comparisons with relatively young companies.
- 4 Kanda and Iwasaki (1996), Yokozawa (2000), Takeda (2004).
- 5 The percentages of “companies performing well” were as follows: 57.6% among companies taking an “innovative” stance toward the development of new products/services, 50.8% among companies taking a “balanced” stance, and 31.8% among companies taking a “conservative” stance.
- 6 In the *MHRI Survey*, we asked “how the number of employees (including fixed–term employees such as part–time employees and contractual employees) has changed during the period from succession by the incumbent CEO to the present”. Here, we shall use the number of employees as a proxy indicator for corporate performance

- and shall refer to “companies which have seen their number of employees increase since succession by the incumbent CEO” as “companies performing well”.
- 7 The percentage of “companies performing well” was 42.9% in the group which said that “emphasis is placed upon discussions among members and the CEO does not rush to make a decision until a certain direction can be discerned”. This was approximately 10% pt lower than other groups.
 - 8 The percentages of “companies performing well” were 50.9% in the group which said that there are “CEO’s aide(s) within the company” and 42.9% in the group which said that there are no such persons.
 - 9 Internal whistle–blowing systems are systems enabling employees (and other persons) to notify any violations of laws or fraudulent acts within the company to contacts within or outside the company. Japanese companies – mainly listed corporations – are stepping up the introduction of the system as part of their efforts in pursuit of “compliance” with laws and regulations in recent years.
 - 10 For example, with respect to managerial accounting, the percentages of companies performing well were as follows: 68.3% in the group which responded that “(the system was) established by the incumbent CEO”, 39.2% in the group which said that “such systems/rules had existed since the late CEO”, and 46.0% in the group which “do not have such systems/rules”. Similar tendencies were revealed with respect to the other systems/rules.
 - 11 The percentages of companies performing well were as follows: 42.6% in the group which responded that “the corporate philosophy has never been altered since establishment”, in contrast to 62.3% in the group which responded that “the corporate philosophy had never been altered in the period up to the previous CEO but had been altered since the incumbent CEO took office”, 51.3% in the group which responded that “the corporate philosophy had been altered in the period up to the previous CEO and had also been altered by the incumbent CEO”, and 49.4% in the group which responded that “the corporate philosophy had been altered in the period up to the previous CEO but has not been altered by the incumbent CEO” .
 - 12 Refer to Horiuchi and Noda (2008) for responses regarding “managerial succession from the incumbent CEO to the successor”.
 - 13 The percentages of companies performing well were as follows; 60.6% in the group which responded that “the predecessor did not participate at all in decision–making and refrained from providing virtually any instruction/advice”, marking a 20% pt gap from 40.5% in the group which “the predecessor continued to hold substantive decision–making rights” (the group of companies with the strongest involvement by the preceding CEO).
 - 14 Given a high correlation (over 0.5) between the rules on personnel affairs and the rules on administrative authorities, the variable on the rules on personnel affairs was excluded to avoid multicollinearity.
 - 15 Bennedson et al. (2006), Pérez–González (2006), Yasuda (2008), Morikawa (2008).
 - 16 Small and Medium Enterprise Agency (2004), Yasuda (2005).
 - 17 According to the Small and Medium Enterprise Agency (2004), performance tends

to decline during a period of three years after managerial succession. The decline in performance may not be discerned from the fourth year onward. In addition to the foregoing, Yasuda (2005), Yasuda (2008), Kawakami (2005) and Okamoto (2006) also indicated the existence of such an adjustment period.

- 18 This is done to control, as much as possible, the impact upon corporate performance by “economic conditions at the time of succession” which is an exogenous factor.



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