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FAMILY VARIABLES AND FIRM PERFORMANCE: EVIDENCE FROM KUWAITI LISTED FIRMS

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Article Info

Keywords: Family variables, firm performance, family ownership, family directors, family CEO, ruling family, corporate governance, agency conflicts, Kuwait.

Abstract

This study examines the impact of family variables on firm performance in Kuwait by investigating the relationship between family ownership, family directors, family CEO, and ruling family on the boards of directors and firm performance. Using data from 93 non-financial firms listed on the Kuwait Stock Exchange from 2016 to 2018, the results indicate that the presence of ruling family members on boards provided greater value for Kuwait's listed firms, while other variables produced mixed results. The study provides insights into the role of families in corporate governance in Kuwait and highlights the potential for agency conflicts among shareholders. The findings have implications for Kuwaiti families, regulators, and policymakers.

INTRODUCTION

According to agency theory, the board of directors is an effective mechanism for reducing conflicts of interest between managers and shareholders and among shareholders (Jensen & Meckling, 1976). Therefore, the board of directors is an important corporate governance mechanism for aligning interests between managers and all stakeholders. Previous studies have investigated the relationship between firm performance and several board variables, such as board independence, board size, family directors, role duality, board committees, board meetings, and board diversity. The current study focuses more on family variables to provide a clear understanding of this issue in Kuwait.

La Porta, Lopez-de-Silanes, and Shleifer (1999) found that families control 45% to 53% of listed firms in 27 developed countries. Claessens, Djankov, and Lang (2000) found that 67% of all listed firms in East Asia are family firms while Anderson and Reeb (2003) documented that 18% of the listed firms in USA are in families' hands. Jensen and Meckling (1976) argued that agency problems between agents and principals can be reduced when control and ownership are in the hands of the same person and families. Anderson and Reeb (2003) also argued that family members can lead to improved firm performance because they reduce agency problems within firms.

In the case of Kuwait, most listed firms are in the hands of large shareholders and family members have large shares and significant influence on firms' decisions (Al-Saidi & Al-Shammari, 2013). In Kuwait, family members participate on boards of directors as chairmen or CEOs; such involvement may affect firm performance as family members may act in their own interests only and take actions for self-benefits instead of the benefit of all shareholders. Thus, this study argues that such situations may lead to agency conflict among shareholders and may impact firm performance and value; therefore, it is imperative to examine the impact of Kuwaiti families on firm performance by determining the relationship between families and firm performance.

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The literature indicates that families can be involved in their firms through three mechanisms:
families' ownership concentration, board of director presentation, and family CEO. This study examines families' ownership concentration, family directors, ruling directors, and family CEO to establish a relationship with firm performance. To the best of the researcher's knowledge, this study is the first to consider all family variables in Kuwait, so the results could be useful for Kuwaiti families, regulators, and policymakers. The remainder of this study presents the literature review and hypotheses (section two), the data collection and analysis (section three), results (section four), and conclusion (section five).

Literature review and hypotheses

The main idea of agency theory is that a conflict exists between managers and shareholders and among shareholders and that such conflict will be detrimental to firm performance (Jensen & Meckling, 1976). Thus, having effective mechanisms for delegating management activities is the central concern of agency theory. Agency theory asserts that family directors provide firms with several benefits, such as a long-term view of wealth and consistency (Jensen & Meckling, 1976). In the United States, Demsetz and Lehn (1985) first examined the impact of ownership concentration among large shareholders. Omran, Bolbol, and Fatheldin (2008) examined the relationship between families' ownership concentration and firm performance in four Arab countries and found no relationship between them. However, Chu (2011) and Maury (2006) found a positive impact of this variable on firm performance

Shleifer and Vishny (1997) argued that boards with family members are less likely to be effective in removing a CEO in the case of poor performance. McConaughy, Walker, Henderson, and Mishra (2001) asserted that family directors provide American firms with greater value and enable them to operate with greater efficiency and fewer debts. Previous studies that have examined the relationship between family and firm performance (see Table 1) have found mixed results: either a positive impact on firm performance (e.g., Anderson & Reeb, 2003) or no or a negative impact on firm performance (e.g., Stewart & Hitt, 2012).

Meanwhile, Sciascia and Mazzola (2008) studied the impact of family CEO on firm performance and found a linear relationship. Che and Langli (2015) studied the relationship between family firms and firm performance and found that family directors and family CEO positively impact firm performance. According to Maury (2006), when a family owns more than 30% of a firm or a family member is the CEO, the firm's performance (Tobin's Q and ROA) increased. Villalonga and Amit (2006) showed that a family CEO positively impacts firm performance, but descendants negatively impact firm performance. Alzahrani and Ahmad (2015) studied the situation in Saudi Arabia and found that royal family directors and Saudi family directors positively affected firm performance.

Only a few studies in Kuwait have empirically explored the impact of family variables (see Table 2). Al-Shammria and Al-Sultan (2010) examined the impact of family directors on voluntary disclosure. AlSaidi and Al-Shammari (2013) examined the relationship between family directors and bank performance, whereas Al-Shammria (2014) examined the impact of family directors on risk disclosure. Finally, Al-Farih and Al-Mutawa (2017) examined the impact of family directors on voluntary disclosure. Thus, retesting some corporate governance mechanisms using different countries may lead to alternative descriptions of the family variables on boards in the case of Kuwaiti listed firms and firm performance. The current study explores interactions among the variables of family involvement using four variables related to family: family ownership, family directors, family CEO, and royal family directors. Consistent with agency theory, the study's hypotheses are as follows:

H1: A positive relationship exists between family ownership and firm performance.
H2: A positive relationship exists between family director and firm performance.
H3: A positive relationship exists between family CEO and firm performance.
H4: A positive relationship exists between the ruling family and firm performance.

Table 1.

Previous Studies on Family Impact on Firm Performance

Authors	Country	Family variable	Performance measure	Sample	Main results
Alzahrani and Ahmad (2015)	KSA	Royal directors	Tobin's Q, ROE	573 firms 2007–2011	Positive

Habbash and Bajaher (2015)	KSA	Family directors	ROA	338 firms 2006–2009	Positive
Abu-Tapanjeh (2006)	Jordan	Family directors	Net sales	39 firms 1992–2004	No relation
McConaughy et al. (2001)	US	Family members	MB and stock returns	1986–1988 OLS	Positive relationship
Villalonga and Amit (2006)	US	Directors, CEO	Tobin's Q	1994–2000 Fortune 500	Positive relationship
Barontini and Caprio (2006)	European countries	Family directors	Tobin's Q and ROA	675 firms Fixed effect	Positive relationship
Ben-Amar and Andre (2006)	Canada	Family member	Abnormal returns	327 firms 1998–2002	Positive
Sunday (2008)	Nigeria	Family member	ROA, ROE, stock return	1996–2004 89 firms	Positive relationship
Maury (2006)	European countries	Ownership and CEO	Tobin's Q and ROA	1672 firms	Positive relationship
Chu (2011)	Taiwan	Ownership and CEO	Tobin's Q	386 firms 2002–2007	Positive
Elhabib et al. (2015)	Oman	Ruling director	Tobin's ROA	84 firms 2003–2012	No relation
Omran et al. (2008)	4 Arab countries	Family ownership	Tobin, ROA	2002	No relation
Anderson and Reeb (2003)	USA	Director, CEO	Cash flow on total assets	252 firms 1993–1998	Positive

Table 2.

Previous Studies in Kuwait that Examined the Impact of Families

Authors	Sample & method	Type of variables	Objective
Al-Saidi and Al-Shammari (2013)	Banks, 2SLS	Family directors	Impact on firm performance
Al-Farih and Al-Mutawa	Non-financial firms, OLS	Family directors (2017)	Impact on disclosure
Al-Shammria and Al-Sultan (2010)	Listed firms in 2007, OLS	Family directors	Impact on disclosure
Al-Shammari (2014)	109 listed firms in 2012, OLS	Family directors	Risk disclosure

Data collection and analysis

After excluding all the financial listed firms and firms with no information, 93 non-financial listed firms remained from 2016 to 2018. Of the 119 non-financial listed firms total, 26 firms with insufficient data were excluded, leaving 93 listed firms (57% of all firms listed on KSE). This study examined the relationship between family and firm performance in Kuwait. To enhance the understanding, the following regressions were conducted:

TQ (model 1) = $\alpha + \beta 1FOC + \beta 2FD + \beta 3FCEO + \beta 4FRUL + \beta 5DT + \beta 6FS + \beta 7IT + \varepsilon$

ROA(model 1) = $\alpha + \beta 1FOC + \beta 2FD + \beta 3FCEO + \beta 4FRUL + \beta 5DT + \beta 6FS + \beta 7IT + \varepsilon$ Table 3.

Study Variables

Variables	Definitions
Dependent variables Tobin's Q (TQ)	Market value of the firm + total debt ÷ the book value of total assets

Return on assets (ROA)	Net income ÷ total assets
Independent variables	
Family ownership (FOC)	Total ownership concentration by families (more than 5%)
Family directors (FD)	Ratio of family directors to all directors on the board
Family-CEO (FCEO)	Dummy variable for having a family CEO: 1 if the family member is also the CEO and 0 otherwise.
Ruling family (FRUL)	Dummy variable for existence of a ruling family director: 1 if the firm has a ruling family on the board and 0 otherwise.
Control variables Debt	
(DT)	Total debt ÷ total assets
Firm size (FS)	Natural log of total assets
Industry type (IT)	Classification of non-financial listed firms (9 sectors)

In these regressions, the independent variables were Tobin's Q and return on assets (ROA) whereas the independent variables were ownership concentration by families, family directors, family CEO, and presence of the ruling family. The study also used three control variables: debt ratio, firm size, and industry type. Table 3 presents more information about the variables used in this study. All data were collected from the firms' annual reports and the KSE website's online data. However, in terms of ownership concentration, the researcher collected the data directly at the end of each year and created a database for ownership concentration in KSE for 2016 to 2018. The researcher also collected data on the family-related study variables from annual reports. In a country like Kuwait, collecting such data is very difficult and time-consuming because some families remove their names and use the firm's name in their transactions or appoint foreign persons to take care of their businesses for security purposes. Thus, in some cases the researcher visited several firms to collect the data face to face or otherwise excluded the firm from the sample.

Results

4.1 Descriptive analysis

According to Haniffa and Hudaib (2006, p. 1047), "since the multivariate regression is used to test the hypothesis, assumptions of multicollinearity, normality, homoscedasticity, and linearity are also tested." As Table 4 demonstrates, the correlation matrix for the variables showed no multicollinearity problem among variables. Gujarati (2003) and Brooks (2002) argued that studies can consider multicollinearity as a major problem if the relationship among independent variables exceeds 80%.

Table 4.

Pearson Correlation Matrix for 101 Firms from 2012 to 2015

	TQ	ROA	FOC	FD	FCEO	FRUL	DT	FS
TQ	1							
ROA	0.412*	1						
FOC	0.061	-0.065	1					
FD	-0.072	0.010	0.41**	1				
FCEO	0.002	0.035	0.197**	0.556*	1			
FRUL	0.056	0.088*	0.001	0.030	0.134**	1		
DT	0.015	0.013	0.153**	0.133**	-0.023	-0.023	1	
FS	-0.029	0.87*	-0.011	0.136**	0.128**	0.128*	0.500**	1

Notes: ***, ** , * Significant at the 0.01. 0.05, and 0.10 levels, respectively (two-tailed).

In terms of other econometrics problems, as Table 5 shows, issues of homoscedasticity, autocorrelation, normality, and linearity were not met. The analyses of residuals, plots of Q-Q, and studentized against predicted values as well as the analyses of skewness and kurtosis identified the problem of normality for the data used. Thus, three variables were transformed into normal scores. Table 5.

Descriptive Statistics for All Variables

Variables	Sample	Mean	S.D.	Min	Max	Skewness	Kurtosis
TQ	93	1.15	1.31	0	11.3	5.7	31.817
ROA	93	0.05	0.15	-0.29	0.98	4.33	22.77
FOC	93	8.9	14.5	0	0.60	1.9	2.8
FD	93	0.20	0.20	0	0.83	0.828	-0.016
FCEO	93	0.32	0.46	0	1	0.759	-1.429
FRUL	93	0.15	0.36	0	1	1.879	1.1537
DT	93	0.43	0.21	0	1.12	0.260	-0.548
FS	93	191811	386000	0	3945137	5.48	29.33

Table 5 further indicates that the Kuwaiti firms did better on market measures than accounting measures (Tobin's Q mean = 1.15; ROA mean = 0.05). The mean value for ownership concentration by family was 8.9%, family directors on boards was 20%, family CEO was 32%, and ruling families was 15%. Finally, the debt ratio had a mean value of 43% whereas the mean value of firm size was KD191811.

4.2 Discussion

Table 6 presents the OLS regression for all four variables of family involvement related to firm performance. The study found a negative impact of families' ownership concentration on firm performance based on Tobin's Q, although such an impact did not exist based on ROA. Thus, Hypothesis 1 was rejected. This finding is consistent with agency theory, which states that large shareholders create a "tunneling" problem among shareholders. Although Omran et al. (2008) found no impact of families' ownership concentration on firm performance in four Arab countries, while, Maury (2006) and Chu (2011) found a positive impact. This study found such results probably because the Kuwait government introduced new rules for corporate governance in 2016 and we still need time to determine the rules' influence on large shareholders who have thus far worked in an environment with weak legal protections.

Regarding Hypothesis 2, the study found that family directors positively affect firm performance based on ROA only; however, this relationship is insignificant based on Tobin's Q. Again, this is consistent with agency theory, which argues that family directors positively affect firm performance. Thus, the second hypothesis is supported. This finding is consistent with the studies of Habbash and Bajaher (2015), Ben-Amar and Andre (2006), Sunday (2008), Chu (2011), Maury (2006), McConaughy et al. (2001), Villalonga and Amit (2006), and Barontini and Caprio (2006). Thus, Kuwaiti family members likely improve the firm because they have long and strong relationships with firms and consider their firms to be their second home.

Table 6.

Analysis of OLS Results for 93 Firms from 2016 to 2018

Tobin's Q		ROA	
Variables	T-Value	Variables	T-Value
FOC	-1.790*	FOC	-0.704
FD	0.383	FD	1.887*
FCEO	2.716**	FCEO	0.063
FRUL	2.348**	FRUL	2.089**
DT	-7.262***	DT	-2.837***
FS	-0.367	FS	-5.422***
IT1	-2.867***	IT1	1.345
IT2	0.512	IT2	0.054
IT3	-1.791*	IT3	1.202
IT4	-1.519	IT4	1.294
IT5	-1.158	IT5	-0.456
IT6	-2.160*	IT6	1.412

IT7	-2.532**	IT7	0.478
IT8	-3.905***	IT8	0.650
R^2	0.29	R^2	0.14
Adjustment R^2 F-Value	0.27 16.177	Adjustment R^2 F-Value	0.12 7.085

Notes: ***, ** , * Significant at the 0.01. 0.05, and 0.10 levels, respectively. The excluded dummy variable for industry classification is the technology sector (sector nine)

In terms of Hypothesis 3, this study found that the family CEO positively impacted performance based on Tobin's Q only, whereas the relationship is insignificant based on ROA. This finding is consistent with the studies of Barontini and Caprio (2006), Maury (2006), Chu (2011), and Anderson and Reeb (2003). In Kuwait, family CEO probably has a positive impact on firm performance because the majority of Kuwaiti families give this position to their descendants while considering qualifications and skills. This finding is also consistent with Hypothesis 2—namely, that a good director selects a good CEO to protect their names and reputations.

Regarding Hypothesis 4, this study found that ruling family directors in Kuwait positively impacted firm performance based on both performance measures. Thus, ruling family directors play an effective role in firm performance. This finding is consistent with Hussain, Islam, Gunasekaran, and Maskooki's (2002) study, which demonstrated that one member of the ruling family in a Saudi bank stopped the issuance of the bank's annual account for several years, until the government removed him from his position of authority. In the same country, Alzahrani and Ahmad (2015) studied the relationship between the ruling family directors and firm performance and found a positive impact on firm performance. However, Elhabib, Rasid, and Basiruddin (2015) studied the situation in Oman to determine royal directors' effect on firm performance and found no significant impact on firm performance.

In term of the control variables, the results indicate that debt ratio and firm size negatively affect firm performance, which means that Kuwait banks do not play an effective role in improving firm performance, which is inconsistent with agency theory (Jensen & Meckling, 1976) but consistent with Haniffa and Hudaib's (2006) findings. This study also found that small firms are better for Kuwaiti investors, which is consistent with agency theory; in large firms, managers have greater discretion that leads to higher monitoring costs (Jensen & Meckling, 1976). Haniffa and Hudaib (2006) found that small firms perform better. Finally, for industrial variables, the study found only five sectors (i.e., oil and gas, industrial, consumer services, telecommunications and real estate) negatively affect firm performance based on Tobin's Q only; when considering ROA, all sectors showed no impact on firm performance.

In short, reviewing previous studies in term of families' variables produced mixed results. Recently, James (2020) presented a comprehensive literature review to understand the impact of board structure on firm performance and found no end to this debate. James (2020, p. 7) stated that:

could it be that firm performance is unrelated to board structure or board composition and has more to do with unique organizational and national culture and philosophy? Culture takes years to develop and is not changed by the appointment of a few new directors.

Consistent with this view, many researchers have argued that failing to find consensus about the relationship between board variables and firm performance stems from two reasons. First, there are big differences among countries' cultures, ownership structures, systems of corporate governance, and company laws. Second, using different performance measures, independent variables, samples, and years might also affect the study results. The impact of family board variables on firm performance or value is still unclear in Kuwait, which has different families, regulations, cultures, and ownership structures. Thus, previous studies' results cannot be generalized to Kuwait's situation.

Conclusion

Kuwaiti families can be involved in listed firms through four mechanisms: family ownership, family directors, family CEO, and ruling family. This study is the first to examine all four of these mechanisms of family involvement in Kuwaiti listed firms. The study found that only ruling family members are positively associated with both performance measures; other family variables produced mixed results. However, this

study has several limitations-namely; it is applicable to Kuwaiti non-financial listed firms, so generalizing the results may be relevant to countries with a similar environment as in Kuwait. This study also ignores the issues of endogeneity and causality between firm performance and family variables. Further research could examine the relationship between firm performance and family variables in one of the GCC countries or by using another regression technique (i.e., 2SLS) to test endogeneity and causality problems.

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