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Do Nonfamily Managers Enhance Family Firm Performance?

Hanqing Fang · James J. Chrisman · Joshua J. Daspit · Kristen Madison

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Abstract Prior studies find that nonfamily managers enhance family firm performance, yet other studies note that family firms have difficulty attracting high-quality nonfamily managers, often settling for average-quality nonfamily managers. Given these findings, how is it possible that average-quality nonfamily managers enhance family firm performance? We address this paradox by theorizing that lower-performing, rather than higher-performing, family firms are more likely to benefit from employing nonfamily managers. Using a sample of 324 small family firms, we find that family firms with below-

average performance significantly benefit from employing nonfamily managers, whereas family firms with above-average performance do not experience the same benefit. We attribute the difference to the presence of family-management capacity constraints in lower-performing family firms. For family firms with such constraints, the employment of nonfamily managers is more beneficial than it is for higher-performing family firms, which are not bound by these constraints.

Keywords Family firms · Nonfamily managers · Human capital · Performance · Labor market sorting

JEL classifications D21 · L25 · L26 · M13 · M51 · O51

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1 Introduction

A firm is considered a family firm when a family, or a small number of families, hold controlling ownership and when a vision exists for how the firm will benefit the family, potentially across generations (Bennedsen et al. 2010; Chua et al. 1999). Although family involvement may provide a firm with advantages (Habbershon et al. 2003), the involvement of the family in the firm also presents potential liabilities. One noted liability is that family members may not possess the knowledge and skills required for obtaining superior firm performance. To overcome this family-management capacity constraint (Carney 2005), some family firms hire nonfamily managers to gain access to valuable managerial resources that do not exist, or are in short supply, within

the family (Cucculelli et al. 2019; Dekker et al. 2015; Stewart and Hitt 2012). Indeed, research suggests that the involvement of nonfamily managers can positively affect family firm performance (e.g., Fang et al. 2016; Tabor, Chrisman, Madison, & Vardaman 2018).

However, another body of work suggests that family firms face difficulties when seeking to hire nonfamily managers. Those difficulties are attributed to the family firm's reluctance to use incentive compensation for nonfamily employees (Memili et al. 2013), the pursuit of family-centered noneconomic goals that do not benefit nonfamily employees (Chrisman et al. 2012), and a propensity to engage in bifurcation bias, which is the preferential treatment of family members over nonfamily members (Verbeke and Kano 2012). Because of these tendencies, the most qualified and industrious nonfamily managers are likely to eschew employment in family firms, thus requiring family firms to hire from a labor pool composed of proportionally fewer highly qualified candidates compared to the labor pool available to nonfamily firms (Chrisman et al. 2014; Schulze et al. 2001).

These divergent findings lead us to explore the following paradox: *If family firms are constrained in their ability to hire high-quality nonfamily managers, then under what circumstances do nonfamily managers enhance family firm performance?*¹ To resolve this paradox, we argue that whether nonfamily managers enhance family firm performance depends on the relative quality of both the nonfamily managers and the family managers in the firm. Specifically, we theorize that the extent to which nonfamily managers contribute to family firms depends on the extent to which the firm suffers from a family-management capacity constraint. Family firms with below-average performance are assumed to have more severe management capacity constraints than family firms with above-average performance. In other words, given the attenuated labor pool facing family firms, we suggest that hiring nonfamily managers benefits family firms with below-average performance more than family firms with above-average performance because the former suffer from more pronounced

family-management capacity constraints than the latter. Our theoretical arguments are supported using a sample of 324 small family firms and a two-stage regression analysis that controls for potential endogeneity. Robustness tests confirm these results.

Our study contributes to the literature by resolving the paradox of how nonfamily managers enhance family firm performance if those managers are largely average, rather than high, quality. While our findings confirm that, in general, the proportion of nonfamily managers in a family firm is positively associated with family firm performance, further analyses suggest that this relationship only holds for family firms with performance below industry averages; no relationship is found between the proportion of nonfamily managers and firm performance among family firms with performance above industry averages. We suggest that this occurs because nonfamily managers of average quality have a greater potential impact on family firms that suffer from family-management capacity constraints, in general, nonfamily managers of average quality cannot contribute as much to firm performance when family managers are already superior in quality. These findings explain the paradox of why and when nonfamily manager involvement benefits some family firms despite family firms facing difficulties hiring the most qualified nonfamily managers.

2 Literature review and hypotheses

The involvement of a family in a business has the potential to yield distinctive advantages given the valuable resources that manifest via social capital (Pearson et al. 2008), patient financial capital (Sirmon and Hitt 2003), and human capital (Dawson 2012) to name a few examples. However, despite the potential for competitive advantage, the family's involvement in the firm also creates the potential for competitive disadvantage. This might occur when a family firm is managed exclusively by kin who may lack the managerial resources required for the family firm to achieve superior performance (Cucculelli et al. 2019). In other words, family firms may experience family-management capacity constraints (Carney 2005).

To overcome such constraints, a common solution is for family firms to enhance their managerial resources by hiring nonfamily managers. Family managers tend to possess valuable, but relatively homogeneous, knowledge given their long-term experience with the family firm (Chirico et al. 2011) and limited outside experience

¹ Managerial quality refers to the skills, abilities, experience, and qualifications of an individual to perform managerial work. Although we recognize that the quality of individual managers varies, we assume that, in general, the nonfamily managers employed by nonfamily firms are of higher quality than the nonfamily managers employed by family firms. This aligns with prior studies, which suggest that the average quality of the managerial labor pool available to family firms is lower than that available to nonfamily firms (Chrisman et al. 2014; Schulze et al. 2001).

(Gedajlovic et al. 2004). As such, nonfamily managers can enhance family firm performance through their diverse knowledge and experience (Binacci et al. 2016; Chirico 2008; Harper 2008). Family managers also tend to lack the knowledge necessary to manage complex, high-growth organizations (Barr et al. 1992), especially in industries with a strong technological orientation (e.g., Carney 2005; Verbeke and Kano 2012). Nonfamily managers can help family firms overcome such cognitive limitations by providing knowledge resources beneficial to understanding the complexities associated with firms that are growing rapidly or competing in dynamic settings.

Furthermore, nonfamily managers tend to have more professional education and more experience than family managers (Dyer 1989). This suggests that only family managers with rare ability or training may be able to compete with the high-quality nonfamily managers who have risen through the ranks based on merit rather than family membership (cf., Pérez-González 2006). Perhaps this difference in ability is one reason why nonfamily CEOs possess a greater propensity for risk-taking (Huybrechts et al. 2013), which enables the business to act on current industry opportunities and avoid potential competency traps that might occur due to limited understanding of contemporary industry conditions.

Understanding that not all resources come from within the firm, nonfamily managers can also provide family firms with access to a broader network of external resources. Because family members often have ties to similar individuals and organizations, external networks of kin tend to be redundant, which limits the scope of access to external resources. Nonfamily managers, however, possess network ties that are dissimilar to those of family managers. Classen et al. (2012) find that the number of nonfamily managers in a family firm is positively related to the breadth of external search for innovation opportunities, and Daspit et al. (2019) suggest that nonfamily involvement enhances a family firm's ability to acquire and assimilate new, external knowledge via a potential increase in absorptive capacity, underscoring the value of network-based resources contributed by nonfamily managers.

Finally, the involvement of nonfamily managers tends to be associated with professional management practices (Lien and Li 2014; Stewart and Hitt 2012). The involvement of nonfamily managers in family firms is often related to the development of high-performance work systems and relevant human resource policies, such as

performance evaluation and incentive compensation systems, which breed accountability and reduce bias between family and nonfamily employees (Madison et al. 2018). Nonfamily involvement and professional management systems provide informal and formal monitoring that acts to reduce the incidence of resource expropriation, which occurs when excessive control and entrenchment of family managers encourage them to commandeer firm resources for the private benefit of themselves and their families (Bozec and Laurin 2008; Distelberg and Sorenson 2009; Oswald et al. 2009). Thus, given that family firms may experience managerial capacity constraints when relying on kin, involving nonfamily managers provides access to new and diverse knowledge resources, experiential resources gained from working outside of the family firm, access to additional resources from expanded networks, and more efficient use of internal resources within the firm. Indeed, prior work has shown that the performance of family firms improves when they hire a professional CEO but not when they appoint a family heir (Chang and Shim 2015). Taken together, these theoretical arguments and prior research yield the following baseline hypothesis:

Hypothesis 1. The extent to which nonfamily managers are involved in the family firm is positively related to family firm performance.

Our baseline hypothesis is that nonfamily managers have a positive effect on family firm performance because nonfamily managers help overcome the family-management capacity constraints mentioned so often in the literature (e.g., Carney 2005; Verbeke and Kano 2012). However, a closer examination of the impact of nonfamily managers is warranted because family firms face a restricted labor market when hiring nonfamily managers and have varying levels of family-management capacity constraints. In other words, we suggest that the benefit from hiring nonfamily managers primarily exists when the quality of the resources offered by nonfamily managers exceeds those possessed by the family firm's family managers.

Family firms are well-known for their pursuit of family-centered, noneconomic goals oriented toward building socioemotional wealth (Chrisman et al. 2012; Gómez-Mejía et al. 2011; Gómez-Mejía et al. 2007). These goals include maintaining control of the firm, exercising familial influence, developing a family

legacy, and pursuing transgenerational succession (Berrone et al. 2012; Hammond et al. 2016). Accordingly, family managers tend to favor strategies that support the achievement of these goals (Chrisman et al. 2012; Molly et al. 2019) and are averse to strategies that hinder such achievements (Gómez-Mejía et al. 2007; Gómez-Mejía et al. 2010). Nonfamily managers, however, are more motivated to pursue economic goals—goals from which they are more likely to benefit—and as a result, their drive to pursue economic goals is not perfectly aligned with the dual economic and noneconomic goals of family firm owners. Further, nonfamily managers may be held to a higher performance standard than family managers and may not be fully compensated for their contributions (Chrisman et al. 2014). Therefore, even though nonfamily managers may have expertise that contributes to the achievement of economic goals, their expertise may not help family firms achieve noneconomic goals, and further, this expertise may not be adequately rewarded (Chrisman et al. 2014; Lee et al. 2003). As a result, nonfamily managers are more likely to seek employment in nonfamily firms, where greater goal compatibility and a greater likelihood of being rewarded for their contributions exist. Since the labor market is competitive, this suggests that the highest-quality nonfamily managers are more likely to work in nonfamily firms than in family firms.

Nonfamily managers may also forgo working in family firms because of the possibility of bifurcated treatment between family and nonfamily members (Verbeke and Kano 2012). For instance, family owners may refrain from monitoring, evaluating, and disciplining family managers if they perceive that those actions might harm familial relationships (Gómez-Mejía et al. 2001). Family managers may also receive preferential treatment in the form of perquisites, higher salaries, and other private benefits regardless of their contribution to the firm (Bertrand and Schoar 2006). Further, the family's desire to retain control of the firm often translates into fewer advancement and ownership opportunities for nonfamily managers (Gedajlovic and Carney 2010; McConaughy 2000; Schulze et al. 2001; Verbeke and Kano 2012). Unfortunately, the impact of bifurcation bias is felt more strongly by highly qualified nonfamily managers who would derive the greatest benefit from its absence.

On the other hand, family firms are known for providing nonpecuniary inducements, such as greater job security and organizational support, to nonfamily managers.

These inducements are attractive to all nonfamily managers but may not be as attractive as higher pay, incentives, and promotion opportunities to higher-quality managers (Block et al. 2016; Hauswald et al. 2016). Higher-quality managers are more likely to benefit than average-quality managers from pecuniary inducements; however, nonpecuniary inducements are accessible to all managers equally regardless of qualifications or performance (Chrisman et al. 2014). Indeed, Chrisman et al. (2017) find that labor productivity is affected most by incentive compensation, followed by higher pay, and least by benefits programs; this ordering is attributed to how much employees' qualifications and performance influence the rewards they obtain from these inducements.

In all, due to incongruent goals, asymmetric treatment, fewer advancement opportunities, and decreased likelihood that their experience can be leveraged, the most qualified nonfamily managers are reluctant to work in family firms and prefer opportunities in nonfamily firms. In other words, the most qualified nonfamily managers sort themselves out of the family firm labor market, leaving an attenuated pool of nonfamily managers whose qualifications are, on average, lower than those who seek employment in nonfamily firms (Chrisman et al. 2014).²

Because the nonfamily managers who are likely to be available to family firms are generally only average in quality, we suggest that the positive relationship between nonfamily manager involvement and firm performance is not observed in all family firms, partially because the variance in the quality of family managers is quite high (cf., Block et al. 2011). Family firms with high-quality family managers already possess the management capacity needed to achieve superior firm performance and may only hire nonfamily managers to gain legitimacy or fill managerial gaps in the firm owing to a shortage of family managers (Chrisman et al. 2014; Stewart and Hitt 2012). For example, research suggests that the involvement of founders (Adams et al. 2009) and later-generation family managers (Sciascia et al. 2014)—who are likely to have more experience and a refined management capacity—is positively related to firm performance. Moreover, the tenure of family

² Although the quality of individual managers will differ, we assume nonfamily managers in family firms are average in quality to distinguish their skills, abilities, experience, and qualifications both from nonfamily managers in nonfamily firms who are likely to be higher in quality and from high- and low-quality family managers in family firms.

managers reduces the negative impact of excess family control on performance (Goel et al. 2011). In these instances, nonfamily managers are less likely to improve firm performance since there are few or no family-management capacity constraints to overcome.

However, family firms with family-management capacity constraints can benefit from hiring nonfamily managers with average qualifications because these average qualifications are likely to be higher than the existing qualifications of family managers. When this is the case, the involvement of nonfamily managers is expected to improve family firm performance. Therefore, compared to family firms with above-average performance, family firms with lower-quality family managers, and correspondingly lower performance, are more likely to reap the benefits of nonfamily manager involvement. Accordingly, we hypothesize:

Hypothesis 2. *The extent to which nonfamily managers are involved in family firms is positively related to family firm performance when family managers are of relatively lower quality but not when family managers are of relatively higher quality.*

3 Methodology

Multiple sources of data were used for the study: data on small family firms were acquired from the U.S. Small Business Development Center (SBDC), and to control for endogeneity, data from both the U.S. Census and the U.S. Bureau of Economic Analysis were used. The data came from a larger project designed to assess the effectiveness of the SBDC's counseling services. In 2009, surveys were distributed to the entire population of 58,127 firms that received 5 or more hours of support from the SBDC in a previous period. Overall, 9411 responses were received, for a response rate of 16.2%. The main informant of the survey was the principal manager and primary owner of the firm. Aligned with the definition of family firms, we excluded observations (1) with less than 50% family ownership, (2) with no family managers, and (3) where the respondent did not consider the firm to be a family firm or did not intend to pass the business on to a family successor, as well as those (4) with no employees, no reported sales, or with missing data relevant to the

study. These exclusions ensure the sample only includes family-owned and managed firms with at least one family manager and a transgenerational succession intention. However, these exclusions also limited our final sample to 324 family firms.

The family firms in the sample are relatively young (average age = 10.27 years) and small (average size = 15 employees), making the impact of each manager correspondingly greater. One-third of the firms indicated they are in service industries. Retail and manufacturing firms constituted 17% and 15% of the sample, respectively. The remaining firms reported they compete in a variety of other industries. Of the firms in the sample, 43% are located in the South, 20% in the Midwest/North, 13% in the East, and 24% in the West. On average, family ownership is nearly 93%, and nonfamily managers comprise nearly 16% of the management team.

We conducted tests to assess the potential of nonresponse bias. Nonresponse bias did not appear to be an issue after an examination of *t*-tests comparing early and late respondents to the survey among the variables of interest (Kanuk and Berenson 1975).

3.1 Measures

3.1.1 Dependent variables

To assess performance, respondents were asked to indicate the range that best estimated the firm's sales growth and return on sales (ROS) over a 3-year period. The choices were <0%, 0%, 1–5%, 6–10%, 11–15%, 16–20%, and >20%. These indicators were coded 1 to 7, with higher scores indicating higher levels of performance. Sales growth and ROS represent different aspects of firm performance; thus, using both indicators in separate analyses provides a more complete understanding of the effect that nonfamily manager involvement has on family firm performance.

3.1.2 Independent variable

Following prior literature, we operationalized nonfamily management as the proportion of nonfamily managers relative to all managers employed in the firm (Fang et al. 2016). Accordingly, respondents were asked to indicate the number of nonfamily managers and the number of family managers in their firm. We used these responses to calculate the percentage of nonfamily managers in each family firm.

3.1.3 Grouping variable

Since we did not have direct measures of managerial quality, we made two important assumptions. First, we assumed the quality of the management team was reflected by the relative performance of the firm compared to industry competitors. Second, we assumed that being drawn from a smaller labor pool, the across-firm variance in the quality of family managers was greater than the variance in the quality of nonfamily managers.

To assess whether family firms were performing below (or above) industry averages and, thus, were likely to have (or not have) family-management capacity constraints, respondents were asked to compare their firm's sales growth and ROS to industry competitors over the past 3 years in separate questions. Responses were provided on a 5-point scale, with the choices being *Much Below*, *Below*, *Similar*, *Better*, and *Much Better*. These indicators were coded 1 to 5, respectively. From these data, we divided the sample into two groups that included below and above-average industry performance. The average sales growth compared to competitors was 3.19, and the average ROS compared to competitors was 3.46. Thus, for each measure, firms providing responses of 3 or lower were considered below average, and those providing responses of 4 or above were considered above average.

3.1.4 Control variables

We controlled for percentage of family ownership, firm age, firm size (log of the total number of employees), industry (retail, manufacturing, and service industries were measured as dummy variables; "other industries" served as the reference group), and geographic area (East, South, and Midwest/North were measured as dummy variables; West served as the reference group).

3.1.5 Instrumental variables

We controlled for endogeneity because the results may be affected by reverse causality or latent factors that were not included in the model. For example, lower performance may prompt firms to hire more nonfamily managers. Similarly, a variety of strategic decisions may be related to firm performance and the willingness of family owners to employ nonfamily managers. Thus, controlling for endogeneity is especially important given the cross-sectional nature of the study.

We identified four instrumental variables that are likely to be strongly related to the focal variable (the proportion of nonfamily managers in the family firm) but likely to be unrelated to the dependent variables (sales growth, ROS).³ Two instrumental variables (i.e., educational expense per household and population density in each state) were obtained from the U.S. Census and U.S. Bureau of Economic Analysis databases. Two additional instrumental variables (i.e., the average size of the management team and the span of management control by industry in each state) were obtained from the SBDC database. Because our instruments represent averages in the industries and/or states in which the firms in the sample compete, they are unlikely to be associated with the performance of the sample firms since they would impact all firms in an industry and/or state in the same manner.

Educational expense per household was calculated using the total educational expense (thousand dollars) in each state divided by the total number of households in each state. This variable signals the quality of the educational system, which may affect the supply of nonfamily managers in each state with at least average qualifications and, in turn, the willingness of family firms to hire them. However, education expense per household is unlikely to directly influence the performance of individual firms within a state, and given the size of the firms in the sample, competition among firms in the sample across states would be uncommon. As expected, the correlation between educational expense and the nonfamily management variable ($r = 0.17$) is much higher than the correlation between educational expense and sales growth ($r = -0.02$) and ROS ($r = 0.03$).

Similarly, population density (log of total population divided by area in each state) may increase the overall supply of nonfamily managers and should be positively

³ It is important to note that the instrumental variables may be indirectly related to the dependent variables. This is to be expected because the instrumental variables should be related to the nonfamily manager independent variable, which, in turn, should be related to the dependent variables. However, this should not invalidate our instruments because other than through the explanatory variables included in the second stage regression, they are uncorrelated with performance (Adams et al. 2009). It should also be noted that, by definition, the instrumental variables are related to the proportion of family managers in a family firm, which is the inverse of our independent variable (i.e., 1—proportion of nonfamily managers). However, we do not consider this to be a problem since our purpose is to identify instruments that will limit the effects of endogeneity on the relationship between the nonfamily manager variable and the sales growth and ROS variables.

related to the employment of nonfamily managers. By contrast, there is no reason to expect a direct relationship between population density and sales growth or ROS. Indeed, the correlation between population growth and nonfamily management is 0.19, whereas its correlation with both sales growth and ROS is -0.02 .

Span of management control is measured as the average employee to manager ratio in each industry in each state. This variable signals the demand for nonfamily managers (a higher ratio indicates lower demand) and should be negatively related to the employment of nonfamily managers as confirmed by our correlation analysis ($r = -0.13$). However, as confirmed by the correlations, there is no reason to presume that span of control is strongly related to sales growth ($r = 0.06$) or ROS ($r = -0.01$).

Finally, the average size of the management team is calculated as the average number of managers for all firms in each industry in each state. This variable captures the average demand for managers in each industry in a state. Given that the number of family members is limited by the size of the family, the average size of the management team should be positively related to the proportion of nonfamily managers in family firms, which is confirmed by the correlation analysis ($r = 0.20$). On the other hand, the average size of the management team in an industry in a state should not be related to firm performance, and, as expected, the correlations between this variable and sales growth ($r = 0.09$) and ROS ($r = 0.08$) are relatively low.

3.2 Data analysis

Following Hamilton and Nickerson (2003), we analyzed our data using a two-stage regression approach with instrumental variables. Variance inflation factors were all less than 5.00. The White method was used to control heteroscedasticity. In the first stage, the instrumental and control variables were used to estimate the predicted value of nonfamily manager involvement. In the second stage, the dependent variables were regressed against the predicted nonfamily manager involvement variable obtained in the first stage and the control variables to test Hypothesis 1. To test Hypothesis 2, we divided the sample into firms with performance above and below industry averages using the grouping variables and reran the analysis for each group.

4 Results

Table 1 provides descriptive statistics and bivariate correlations among the study variables. As expected, the nonfamily manager involvement variable is positively correlated with both performance measures. Additionally, as discussed above, all four instrumental variables are significantly correlated with the independent variable but not with the dependent variables. Table 2 provides the distribution of nonfamily managers across the full sample of family firms, those performing below industry averages, and those performing above industry averages.

Table 3 summarizes the regression results. Standardized betas are reported. In the first stage, the estimated coefficients of all four instrumental variables are significant in the expected direction, further supporting the soundness of the selection criteria. In the second stage, we tested the hypothesis that the involvement of nonfamily managers is positively related to family firm performance using the predicted value of the independent variable from the first-stage regression. In support of Hypothesis 1, nonfamily manager involvement has a significant and positive effect on both sales growth ($\beta = 0.110$, $p < 0.001$) and ROS ($\beta = 0.074$, $p < 0.05$).

After dividing the sample by the grouping variable, we found that the positive effect of nonfamily manager involvement is significant only for family firms that have performance below industry averages (sales growth: $\beta = 0.147$, $p < 0.01$; ROS: $\beta = 0.095$, $p < 0.01$). For family firms with performance above industry averages, the effect of nonfamily manager involvement is not significant (sales growth: $\beta = 0.033$, $p > 0.10$; ROS: $\beta = 0.053$, $p > 0.10$). Furthermore, t -tests indicate that the betas of the nonfamily manager involvement variable are significantly greater in the regressions of firms with performance below industry averages than in the regressions of firms with performance above industry averages for both dependent variables (sales growth: $t = 3.750$, $p < 0.001$; ROS: $t = 4.272$, $p < 0.001$). Hence, Hypothesis 2 is supported.

4.1 Robustness tests

We conducted several robustness tests to ensure the reliability of our results.⁴ First, to ensure our results

⁴ Full results of the robustness tests are available from the lead author upon request.

Table 1 Descriptive statistics and bivariate correlations

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
1. Sales growth ¹	1.00															
2. ROS	0.42	1.00														
3. Nonfamily management	0.09	0.10	1.00													
4. Family ownership	-0.03	0.02	0.13	1.00												
5. Firm size (log of employees) ²	-0.19	-0.05	0.07	0.06	1.00											
6. Firm age	0.08	0.02	0.22	-0.04	0.35	1.00										
7. Retail	-0.04	-0.02	-0.04	0.13	-0.07	-0.04	1.00									
8. Service	0.00	0.03	0.01	-0.03	-0.13	-0.17	-0.32	1.00								
9. Manufacturing	0.07	0.04	0.02	-0.03	0.09	0.05	-0.19	-0.30	1.00							
10. East ³	-0.04	-0.07	0.00	0.11	0.10	-0.15	0.05	-0.10	0.07	1.00						
11. South	0.06	0.08	-0.06	0.03	-0.14	0.10	0.03	-0.01	-0.10	-0.33	1.00					
12. Midwest/North	-0.01	-0.02	0.08	-0.10	0.18	0.11	-0.02	0.00	0.06	-0.20	-0.43	1.00				
13. Educational expense ⁴	-0.02	0.03	0.17	0.01	-0.03	-0.09	0.01	0.08	-0.01	-0.11	-0.16	-0.09	1.00			
14. Population density (log)	-0.02	-0.02	0.19	0.00	0.07	-0.08	0.00	-0.04	0.01	0.33	0.03	0.07	-0.28	1.00		
15. Span of management control	0.06	-0.01	-0.13	0.00	0.06	0.44	-0.07	-0.13	0.04	-0.09	0.09	-0.01	-0.03	-0.04	1.00	
16. Average management team	0.09	0.08	0.20	-0.06	0.26	0.34	-0.11	-0.13	0.09	-0.08	-0.06	0.23	-0.10	0.07	0.03	1.00
Mean	4.54	4.06	0.16	0.93	2.10	10.27	0.17	0.33	0.15	0.13	0.43	0.20	0.94	4.74	4.23	3.38
Median	4.50	4.00	0.00	1.00	2.08	6.00	0.00	0.00	0.00	0.00	0.00	0.00	0.64	4.55	3.39	3.00
Min	1.00	1.00	0.00	0.50	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.25	1.72	0.50	2.00
Max	7.00	7.00	0.88	1.00	5.35	107.00	1.00	1.00	1.00	1.00	1.00	1.00	5.03	6.97	21.00	7.00
Standard deviation	1.91	1.78	0.27	0.15	1.05	13.12	0.37	0.47	0.36	0.34	0.50	0.40	1.46	0.91	5.17	1.75

¹ Correlations that are > 0.11 have p values < 0.05

² The descriptive statistics for Firm Size measured by the number of employees (NOT logged) are: mean=15.51; median=8.00; Min=1.00; Max=210.00; S.D.=24.41

³ Regional dummy variables are coded as follows: *West* is used as the base reference;

East: Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Vermont, Virginia, and West Virginia;

South: Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Mississippi, New Mexico, North Carolina, Oklahoma, South Carolina, Tennessee, and Texas;

Midwest/North: Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, Ohio, and Wisconsin; and

West: Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, North Dakota, Oregon, South Dakota, Utah, Washington, and Wyoming

⁴ Educational expense per household measured in thousands of dollars

Table 2 Distribution of nonfamily managers

Nonfamily managers		Sales growth				Return on sales					
		Full sample		Below industry-average performance		Above industry-average performance		Below industry-average performance		Above industry-average performance	
Number of nonfamily managers in the family firm	–	No.	Percent	No.	Percent	No.	Percent	No.	Percent	No.	Percent
0	–	177	54.63%	88	57.52%	89	52.05%	107	55.15%	70	53.85%
1	–	67	20.68%	37	24.18%	30	17.54%	46	23.71%	21	16.15%
2	–	40	12.35%	13	8.50%	27	15.79%	21	10.82%	19	14.62%
3	–	15	4.63%	6	3.92%	9	5.26%	8	4.12%	7	5.38%
4	–	10	3.09%	2	1.31%	8	4.68%	5	2.58%	5	3.85%
5	–	7	2.16%	3	1.96%	4	2.34%	5	2.58%	2	1.54%
>5	–	8	2.47%	4	2.61%	4	2.34%	2	1.03%	6	4.62%
Total	–	324	100%	153	100%	171	100%	194	100%	130	100%

were not affected by regression to the mean, we used Propensity Score Matching (PSM), to identify a sample of nonfamily firms that we matched with our primary sample of family firms with respect to the performance and control variables. The results of a matched-sample regression are consistent with the primary results: both hypotheses are supported. Furthermore, the PSM results provide additional assurance that endogeneity, as well as regression to the mean, does not influence the findings.

Second, we use several alternative measures of key variables, which include (1) the actual nonfamily involvement variable rather than the predicted value and (2) the number of nonfamily managers in the management team rather than the percentage. Furthermore, we use several alternative ways to specify the sample. For example, we relax the constraint of at least one family manager ($n = 357$). We also analyze family firms with fewer than 100 ($n = 319$), fewer than 50 ($n = 304$), and fewer than 20 employees ($n = 265$). In each case, the regression results are consistent with our hypotheses. In addition, we investigated whether there was a nonlinear, inverted-U relationship between nonfamily manager involvement and firm performance because a possible alternative explanation for our findings is that there are limits to the number of nonfamily managers that family firms can gainfully employ before experiencing diminishing returns. However, consistent with our theoretical assertions, our analysis shows that the relationship is linear rather than nonlinear.

Third, we compared the proportion of nonfamily managers in family firms with above- and below-average performance. We found no statistical difference in the proportion of nonfamily managers between family firms with above-average performance and those with below-average performance. This finding suggests that the results pertaining to Hypothesis 2 are likely driven by the relative quality of the nonfamily managers and the family managers rather than the proportion of nonfamily managers involved in family firms with above and below-average performance. Thus, the results of the analyses appear to be both empirically and theoretically robust.

5 Discussion

The involvement of nonfamily managers is a prominent issue for family firms (Benavides-Velasco et al. 2013; Tabor et al. 2018) given that nonfamily managers are often critical to the professionalization efforts, growth, and performance of these organizations (Stewart and Hitt 2012). However, prior studies provide paradoxical insights. Even though nonfamily managers are believed to generally enhance family firm performance, family firms are often compelled to hire from a restricted pool of nonfamily managers who are not as qualified, on average, as those available to nonfamily firms, which would seem to limit the value family firms gain from hiring nonfamily managers. To resolve this paradox, we examine the conditions in which family firms

Table 3 Regression results

Sample	First-stage regression	Second-stage regression					
	Whole sample	Whole sample		Below industry-average performance		Above industry-average performance	
Dependent variables	Nonfamily management	Sales growth	ROS	Sales growth	ROS	Sales growth	ROS
Independent variable:							
Nonfamily management ¹		0.110***	0.074*	0.147**	0.095**	0.033	0.053
Control variables:							
Family ownership	0.165	-0.078	0.040	-0.079	0.001	-0.059	0.149
Firm age	-0.048	-0.272***	-0.052	-0.214*	-0.078	-0.210 [†]	-0.007
Firm size	0.255**	0.169**	0.045	0.095	0.013	0.035	-0.070
Retail	-0.004	-0.040	0.020	-0.051	-0.004	-0.065	-0.085
Service	0.071	-0.032	0.064	-0.038	0.025	-0.041	0.027
Manufacturing	0.028	0.077	0.098	0.028	0.044	0.184**	0.173*
East2	0.014	0.003	-0.089	-0.162	-0.160 [†]	0.191*	0.167
South	-0.059	0.007	0.028	-0.138	-0.129	0.198 [†]	0.215 [†]
Midwest/North	0.019	-0.004	-0.020	-0.195	-0.121	0.188 [†]	0.105
Instrumental variables:							
Educational expense	0.094*						
Population density	0.079*						
Span of management control	-0.082***						
Average management team	0.106***						
Sample size	324	324	324	153	194	171	130
Adj. R2	0.102	0.094	0.031	0.092	0.041	0.118	0.111
F-Statistic	2.829	3.255	0.999	1.440	0.795	2.035	1.381

¹ Predicted value from the first stage regression

² Regional dummy variables are coded as follows: *West* is used as the base reference.

East: Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Vermont, Virginia, and West Virginia;

South: Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Mississippi, New Mexico, North Carolina, Oklahoma, South Carolina, Tennessee, and Texas;

Midwest/North: Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, Ohio, and Wisconsin; and

West: Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, North Dakota, Oregon, South Dakota, Utah, Washington, and Wyoming

Standardized estimation coefficients are reported; *** $p < 0.001$; ** $p < 0.01$; * $p < 0.05$; [†] $p < 0.10$

experience positive performance effects from nonfamily manager involvement.

We hypothesize and find that nonfamily manager involvement generally improves family firm performance. We then conduct a more nuanced investigation wherein we theorize that the effect of nonfamily manager involvement on family firm performance is only relevant for family firms with performance below industry averages where family-management capacity constraints are likely to be more pronounced. In such

situations, even nonfamily managers of average quality can make an impact given that they are likely to be more qualified than a firm's family managers. Indeed, our results indicate that nonfamily managers have a positive effect on family firms with performance below industry averages but not on family firms with performance above industry averages. Two-stage least square and PSM controls suggest that reverse causality, omitted variable bias, and regression to the mean are likely not the source of this relationship.

5.1 Contributions

This study contributes to family firm research in several ways. First, we confirm the general, positive effect that nonfamily manager involvement can have on family firm performance. We elucidate the benefits that nonfamily managers offer to family firms given that some family firms experience managerial capacity constraints due to the limited outside experience, professional education, and access to external resources of family managers. Specifically, we argue that nonfamily managers provide family firms with knowledge resources and other benefits that are less available (or unavailable) in the absence of those managers. This argument aligns with prior studies that suggest nonfamily managers enhance the performance of family firms (e.g., Dekker et al. 2015; Madison et al. 2018; Patel and Cooper 2014; Tabor et al. 2018).

Second, we investigate the paradox of how family firms can experience enhanced performance even though the nonfamily managers hired are likely to be only average in quality. To this end, we suggest that highly qualified nonfamily managers sort themselves out of the family firm labor market owing to goal misalignment, asymmetric treatment, and fewer advancement opportunities. Accordingly, we hypothesize and find that nonfamily managers significantly influence family firm performance only in family firms with below-average industry performance. We argue that this finding occurs because nonfamily managers with an average-level of qualifications are generally more qualified than the family managers in lower-performing family firms. Therefore, this finding resolves the nonfamily manager paradox by demonstrating that family firms can experience positive benefits from nonfamily manager involvement, but this benefit is limited to family firms that suffer from family-management capacity constraints. Although this seems like an obvious conclusion, it has remained hidden in prior literature, which has not taken the quality of family managers or the performance of the family firm into account. Indeed, the literature to date illustrates an instance of when misleading conclusions can be reached when the aspects of family firm heterogeneity are not explicitly considered.

Third, the findings of this study have potentially impactful economic and societal implications. Family firms are considered “the backbone of private industry and a key target for policies aimed at increased

employment and economic growth” (Andersson et al. 2018, p. 540). More than 80% of U.S. businesses are small family firms and more than one-third of *Fortune 500* companies are family firms (Chu 2009). Research estimates that U.S. family firms contribute 64% of the GDP and employ 62% of the U.S. workforce (Astrachan and Shanker 2003). In Europe and Asia, family firms represent approximately 40% of all firms and are a key source of employment and economic growth (Chu 2009). Because of the impact family firms have on economies (Memili et al. 2015), understanding the drivers of their performance, especially those related to the workforce, is necessary. Our theoretical assertions are built on the notion that family firms are likely to have difficulty attracting high-quality nonfamily managers but that average-quality nonfamily managers can still make a positive impact on lower-performing family firms. Since the results support our hypotheses, we argue that high-performing family firms should be encouraged to be more effective in signaling the opportunities available to high-quality nonfamily managers and ensuring that they deliver on their promises to these managers.

5.2 Limitations and future research

Although this study offers important insights, limitations exist. First, the SBDC population primarily consists of small firms. Thus, caution should be exercised when generalizing these findings to larger family firms. In addition, although the sample is of reasonable size and given that prior work suggests that SBDC clients are generally representative of the population of small firms in the USA (Chrisman et al. 2012), a need remains for further research to ensure that the findings are not an artifact of the sample. Conclusions based on a sample of small firms in the USA may underestimate the distinctions of certain family attributes across different cultures, which may be critical to family firm performance. For example, in economies with underdeveloped property rights, the potential for nonfamily managers to act opportunistically may negate the value of their potentially greater managerial resources. In such a situation, the relationship between nonfamily manager involvement and family firm performance may disappear entirely (cf., Ilias 2006). On the other hand, in some cultures, the inclusion of nonfamily in the firm may help mitigate resource expropriation by nuclear and distant

kin, which may lead to a more positive influence on family firm performance (e.g., Daspit and Long 2014).

Second, other variables that influence family firm performance, beyond those considered, are undoubtedly present. For example, certain family and management attributes—such as family size, family structure, generational stage, founder status, management tenure, succession intentions, and kinship networks—may affect family firm performance. More importantly, however, we were not able to directly measure the quality of the nonfamily or family managers in our sample. Instead, based on prior literature, we assume that the nonfamily managers are, in general, of average quality, falling somewhere between that of the most capable and least capable family managers. Given the importance of nonfamily managers, research that expands on these insights by measuring and comparing the actual quality of family and nonfamily managers in family firms and between family and nonfamily firms would be useful.

Third, while hiring nonfamily managers is a step toward professionalization, we are not able to observe the extent to which the family firms in the sample are professionalized. Although the inclusion of nonfamily managers is one indicator of professionalization (Stewart and Hitt 2012), consideration should also be given to financial control systems, human resource control systems, and the extent to which authority is decentralized (Benavides-Velasco et al. 2013; Chrisman et al. 2016; Dekker et al. 2015). Similarly, further research on how the design of compensation packages affects nonfamily manager involvement and family firm performance remains a fruitful area of research not captured in our study. For example, Block (2011) suggests that short-term incentives have a greater impact on the behavior of nonfamily managers (positive in terms of short-term performance, negative in terms of the pursuit of the firm's long-term goals) than family managers, but this theorizing has not been empirically tested. Furthermore, although family managers appear to have higher performance-based compensation than nonfamily managers in developing and emerging markets (Nyantakyi 2016), more research is needed to determine the extent to which the compensation of family and nonfamily managers is influenced by bifurcation bias (Verbeke and Kano 2012) rather than variations in ability and effort.

Fourth, we do not account for the idiosyncratic preferences of nonfamily managers in the labor market. Hauswald et al. (2016) note that applicants who value

conservation (i.e., tradition, conformity, security) or self-transcendence (i.e., benevolence, universalism) tend to be more attracted to family firms. While this could ameliorate, or (more likely) exacerbate, the sorting effect discussed in this investigation, future studies are encouraged to take a more refined approach to examining the influence of the preferences and quality of nonfamily managers in the labor market. Likewise, obtaining a better understanding of the conditions in which more qualified nonfamily managers may be attracted to family firms is also important. Here, a perspective that accounts for perceived person-organization fit (Kristof 1996) might yield valuable insights.

Finally, the data analyzed in this study are cross-sectional, which means we cannot establish causality but can only draw theoretical inferences from the empirical relationships. Although controlling for endogeneity partially mitigates the problems of reverse causality and omitted variable bias, longitudinal data would allow for more detailed insights into the mechanisms through which the involvement of nonfamily managers is related to family firm performance. Additionally, future studies that assess a broader array of family firm performance measures are encouraged. In our study, both sales growth and ROS are used to offer insight into firm performance; however, using other measures of economic and noneconomic performance will contribute to a better appreciation of the impact of nonfamily manager involvement.

Aside from future research that improves on our research design, other opportunities remain. For instance, even though the involvement of average-quality nonfamily managers is beneficial to some family firms, understanding how family firms can attract better-quality nonfamily managers is an area worthy of further investigation. As noted, Chrisman et al. (2017) find evidence that, in decreasing order of importance, incentive compensation, higher pay, and benefits packages that act as pay substitutes have a greater effect on labor productivity in family firms than in nonfamily firms. This appears to be because such compensation not only aligns the interests of owners and managers but also increases the attractiveness of family firms as employers to nonfamily managers, thus reducing the sorting effect discussed above. Such mechanisms may assist family firms in recruiting better-qualified nonfamily managers. Unfortunately, research also suggests that the greater a family's involvement in the firm, the greater their focus on preserving socioemotional wealth, which reduces the

probability that incentives will be offered to nonfamily managers (Memili et al. 2013). Additional research is needed to understand how family firms can preserve socioemotional wealth while simultaneously benefitting from the involvement of nonfamily managers.

Qualitative studies could also be useful given that there are many gaps in knowledge concerning the roles of nonfamily managers and how those roles emerge and evolve. For example, qualitative research might be useful to understand how, to what extent, and in which situations nonfamily managers are ceded power. We find that the involvement of nonfamily managers is significantly related to performance when the family firm performs below the industry average; however, precisely how power is transferred to nonfamily managers in a way that enhances the achievement of economic goals without undermining the achievement of noneconomic goals (if that is indeed possible) needs to be studied. For example, can a temporary leadership or seat-warmer role be an effective way to utilize nonfamily managers (Lee et al. 2003), and if so, how can this be accomplished without demotivating family managers?

6 Conclusion

Prior research has yielded paradoxical insights suggesting that nonfamily managers enhance family firm performance even though family firms have difficulty attracting high-quality nonfamily managers. We attempt to resolve this paradox by theorizing that nonfamily manager involvement is only significantly related to firm performance in family firms with family-management capacity constraints, as exemplified by performance below industry averages. We argue that this is because family firms with deficiencies in the managerial resources of family members benefit from hiring average-quality nonfamily managers given that the capacity of the family to manage the family firm is below average. Thus, this study offers insights into why and when nonfamily managers affect family firm performance and creates a foundation to support future investigations.

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Data Availability Data available upon request

Code availability Code available upon request

Declarations

Competing interests The authors declare no competing interests.

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