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Entrepreneurship Theories and Family Business

Louangrath, P.I. ★

About the author

★Louangrath, P.I. is an Assistant Professor in Business Administration at Bangkok University, Bangkok, Thailand. He could be reached by email at: Lecturepedia@gmail.com

ABSTRACT

The scope of paper is to review the theoretical foundation for entrepreneurship and its connection to family business. We reserved the theoretical materials in part 3 because we want to defined the concept in part 1 and see the developmental path of a successful entrepreneur in part 2. In part 3, we provide the theoretical basis for their development. In the last installment of this series, part 4, we will explore how family business functions within the larger "system" context or the economy. We examined the theories from the European continent, and contrasted with the American perspective. These theoretical perspectives are classical in a sense that they are old, but their explanatory power remains as forceful as they were in their time. Research in entrepreneurship remains unorganized.

Keyword: entrepreneurship theory, family business

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1.0 INTRODUCTION

In order to gain a better understanding of the operation, functions, structure, organization, and organization of the family business, it is imperative that we understand relevant theories that help explain family business. Family business is a midway between entrepreneurial enterprise and a more organized SME. As such it is in the crossroad of being classified and not much research interests may be given to the issue. For that reason, ion order to examine the theoretical foundation for the family business, it is necessary to ask "what is the origin of family business?" This is a fair question. The position taken by this book is that in order to understand family business, it must be put context of its developmental stages. Family business is a business in transition between entrepreneurial enterprise and a formalized SME or fully developed corporation. As such, multiple theoretical approaches may be used. At the most basic level, family business may be explained by entrepreneurial theories. At a more sophisticated level, the theories of firm may be used to explain the existence of family business. There is no such a thing as a "theory of family business." The study of family business is not an independent discipline equip with its own theories. As a business entity in transition, family business borrows the explanation from several sources. This paper takes a brief tour through various theoretical arguments to explain the existence of family business.

2.0 THEOREIS OF ENTREPRENEURSHIP

2.1 The Continental European School of Thought

Since the Industrial Revolution, continental Europe has provided the academe with the riches of her fountain of knowledge. From the classical economist, we meet three colossal of the past: Adam Smith, Richard Cantillon and Jean-Baptiste Say. Much of the theoretical proposition from the European continent on entrepreneurship was pre-industrial revolution. The growth of entrepreneurship, and its transformation into family business, came about after the second industrial revolution. Despite this lack of foresight, earlier works of Smith, Cantillon and Say still rings the truth in explaining small scale businesses. Although the term family business and entrepreneurship never seem too have been treated separately by these authors, it goes without saying that during that period entrepreneurship and family business, so long as it is a sole proprietorship, both are synonymous.

2.2 Adam Smith's "The Wealth of Nation" as the Theoretical Source

Smith puts great reliance on the individual self interest as the driver for the nation's economy.
Smith wrote:

> "It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages." Smith, A., 1976, *The Glasgow edition*, vol. 2a, pp. 26–7.

The words of Adam Smith echoes through the pages of history that the wealth of a nation depends on the industry of her people. That industry lies in the work of the individual makers and shakers of the economy; these are the entrepreneurs who organize their labor and capital into the productive process to produce goods and services in the economy. The definition of this individual endeavor was best described by Smith in the book: *The Wealth of Nation* in which Smith wrote:

> "As every individual, therefore, endeavours as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of the greatest value; every individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other eases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it. I have never known much good done by those who affected to trade for the public good. It is an affectation, indeed, not very common among merchants, and very few words need be employed in dissuading them from it." (Smith, 1976, 1980).

Smith spoke to the idea of optimality in employing the individual labor and capital to produce the highest level of production. The amalgamation of this production contributes to the wealth of the nation. Long before the advent of macroeconomics, Smith foresaw the role of the entrepreneur in the economy.

Smith did not use the word family business in his writing; however, family business would have come to dominate the economic life of Europe long after Smith's publication in 1776.

Nevertheless, for his recognition of the role of the individual in the economy, hence entrepreneurs, Smith is thought of as a founding theorist who helped explain the role of the entrepreneur in the economy. As for family business, it is applicable only by extension of the term. There was no theoretical contention by Smith. As posited by this book, family business is the extension of success of the individual entrepreneur. Therefore, having laid the foundation for the individual entrepreneur as the creator of value, Smith secured for himself a place in history of economic thoughts.

In 1776, through *The Wealth of Nation*, Smith paints for use a clear picture of the entrepreneur pursues his self-interests, in the process society benefits from it. As many and more individuals are doing the same thing (wealth accumulation and value creation), the whole nation benefits from it. This pursuit of self interest resulted in the benefit of society became known as the invisible hand of the market. In like manner, lacking the available records and argument, we must extend the argument to the family business enterprise.

If the family business is a successor in interest by the extension of the success of the individual entrepreneur, the pursuit of self interest by the entrepreneur remains in the new business entity. The term “entity” would have to enter the language describing this pursuit of self interest because it is no longer the individual, but the family unit that acts as a single unit. By extension of Smith’s logic, the family business acts to promote its self interests and in so doing also benefits society. Under this theoretical rubric the idea of good governance or “best practice” is something of a modern invention. Although Smith did not touch upon the idea of ethics, it was implied that the earnings of the individual pursuit for self interest was within the bound of reasons.

2.3 Cantillon’s Theory of Entrepreneurship

Richard Cantillon was credited for coining the word ‘entrepreneur’ (Brewer, 1988). The term was later popularized by Jean-Baptste Say. Cantillon classified economic agents into two types: wage earners working for employers are fixed income earners, and entrepreneur who are self-employed. These self-employed people were classified as non-fixed income earners (Hülsmann,, 2002; Rothbard, 1995). This classical definition of the entrepreneur remains a working definition today. The Cantillon entrepreneur was a man of uncertainty. This definition of the entrepreneur does not seem to permit success or stages of development of the entrepreneur. Under the Cantillon definition, an entrepreneur is a class of person so fixed in society that entrepreneurship is an immovable profession. However, as we know today that an entrepreneurship has a life cycle. It goes through the birth and death just like any other ‘being.’

Cantillon saw the entrepreneur as a risk taker. By its own purpose, the objective for the entrepreneur to take risk is to gain in return. The risk taking activity of the entrepreneur is an investment. Like all investment activities, it involves risk. There is a risk of loss; so too was there the risk of gain. When the entrepreneur is successful, what does he do with the money? Cantillon did not provide us with details of reinvestment and growth of the enterprise run by the entrepreneur. For this reason Cantillon’s attempt was a good beginning but it did not get us far in the theoretical foundation for the work on family business.

Success in entrepreneurship of the entrepreneur led to something. What did the success of the entrepreneur lead to? Cantillon did not answer this question because for Cantillon it did not matter where does the success lead to? being classed as an entrepreneur, the success of the entrepreneurship would still not allow the entrepreneur to escape his class. The successful entrepreneur may reinvest his money into larger operations and involved more family members in the enterprise; this expansion was not important. For Cantillon the enterprise remains a risk taking activity by a person or group of persons classed as ‘entrepreneur.’ Cantillon’s idea does not help us in our attempt to understand the creation of the family business. For Cantillon entrepreneurship and family business were one and the same. We know today that they are not the same.

The concept of family business did not exist at the time of Cantillon’s writing. Cantillon himself did not foresee the rise of family business. In fact even in modern time, writers tend to overlook the role played by family business. The theory of firm is a hall mark of failure in modern time. Modern theory of firm skips a development stage from the entrepreneur transforming itself directly from an individual into firm. This is a leap of faith that has never been questioned. Before the firm becomes a firm, it must go through stages of development. It has to start with someone. *That* some one is an entrepreneur; when his enterprise becomes a success he then involves people within his circle, naturally family members. This is the birth of family business in its most primitive form.

2.4 Jean-Baptiste Say's Theory of Entrepreneurship

Say claims that the entrepreneur is a planner who shifts resources from an area of low productivity to a higher area of productivity. Assume that this activity is successful, what becomes of the entrepreneur? Does he involve other people close to him, i.e. family member? If the entrepreneur is truly a planner he must have foreseen that acting alone would be less effective and inefficient then he would involve other people in the activity. Say does not write that the successful entrepreneur involve family members in the activities; thus giving rise to family business. However, in comparison to Cantillon's classification of the entrepreneur as a static status, Say's version of the entrepreneur as a planner provides the possibility that absent direct expression that 'a successful entrepreneur evolves into a family business' there is always a possibility that entrepreneurship evolves.

Like Cantillon the concept of family business also escaped Say's writing. Absent any evidence of such anticipation, we could only surmise that Say also did not see the forthcoming of the family business. After the industrial revolution, family business and entrepreneurial activities flourished in Europe and the US, interest in research seems to focus on the "firm" rather than the individual entrepreneur and his transformation from the sole proprietor to a multi-stakeholders enterprise involving family members. Had Say and Cantillon seen the economic development of the 20^{th} century, they would have written their theories differently.

2.5 Reconciling Cantillon and Say's Theories

Cantillon saw the entrepreneur as a risk taker. Say saw the entrepreneur as a planner (Brewer, p. 51). These terms are not the same; however, the entrepreneur does both: planning and taking risk. By definition an entrepreneurship is the taking of risk and the risk taking conduct involves a certain degree of risk evaluation. This evaluation is part of the planning undertaken by the entrepreneur. Cantillon and Say belong to the same group of theorists in the early period who attempted to explain entrepreneurship and its role in the economy. In a less developed economy Europe, and in less developed economies of today's world, the role of the entrepreneur is vital to the economic life of a nation. However, in the preindustrial revolution era, neither Cantillon nor Say could have anticipated the developmental path to be taken by the successful entrepreneur.

Entrepreneur who succeeds tend to outgrow his mantel. Growth means that the entrepreneur expands the scope of his operation. In additional to being a risk taker as defined by Cantillon, the entrepreneur may become a planner. As part of that planning, the entrepreneur also must have entertained the thought of involving other people in the enterprise. The most obvious people that the entrepreneur would involve in the enterprise would be family members. The close association among family members helps the entrepreneur to engage his business more effectively. The birth of the family business was a natural development. However, during the time of Cantillon and Say, this process was not anticipated. As for Cantillon's focus on risk taking and Say's focus on planning, both are correct because an entrepreneurial enterprise is a 'one man show.'

The introduction of the family business reduces the direct involvement of the entrepreneur. With the increase stakeholders in the business, the family business is more formalized than the naked entrepreneurship which the 'owner-operator-manager' runs the show. In a family business, the identity of the entrepreneur is subsumed under the rubric of the new organization. Recall that the entrepreneurial enterprise is unorganized and the family business introduce the first form of organization to the business. The formality of structure restrains the entrepreneur's risk taking activities and helps the business to stay focus on a particular line of business. In fact, this developmental stage explanation may help link family business to the theory of firm. Recall that in the theory of firm, Coarse argues that firms arise from comparative advantage in cost reduction. The production of a certain items outside of the firm is cheaper to produce; therefore, the firm needs outside producers to produce for it. As the result, as more and more firm look for outside producers to meet their needs, more firms are established. In the same light at the family business stage, the family business also starts to concentrate on doing what it can do best. This functional differentiation and concentration of skills allows the family business to flourish.

It has been concluded that neither Cantillon nor Say anticipated the rise of family business can their writing on entrepreneurship serve as the building block for a theory in family business? We cannot the contribution made by Cantillon and Say on the theory of entrepreneurship. By virtue of the fact that family business grows out of the success of an entrepreneur, both Cantillon's and Say's works still play an important role in our understanding of the family business.

The family business is still a risk taker and a planner. In its most simple form and structure, family business is small. As a small enterprise it is exposed to risk. Therefore, the family business is still a risk taker. Antillon's characterization of the entrepreneurial character is still valid. The family business is endowed with limited resources. As part of the informal sector, the family business relies almost exclusively on private source of capital, i.e. a common source of capital comes from family or personal savings. As such, family business must carefully plan the allocation of its resources. Unlike a corporation who operates on an annual budget, most family business operates on a tight budget that may be counted as month-to-month or day-to-day.

To look at successful family business that had evolved into a large enterprise, but still closely held within family members is not interesting. Success stories can be found every where. However, success stories that are told objectively could hardly be found. Therefore, the story of family business struggling to make ends meet provides more information from which researcher can learn. Family business has very limited resource. This resource limitation constrains its operation, and to a large extent confines its success within a certain boundary. New opportunities may surface, but the family business must turn another cheek because there are no available resources to pursue these opportunities. Whatever small amount of resources it has are already tied to the current operation.

3.0 THE AMERICAN SCHOOL OF THOUGHT

The American society and economy puts a greater emphasis on individual success. This has produced a culture that nurture of entrepreneurial spirit. The American approach to explain business success starts with the simple form of business: individual entrepreneurs and family businesses. This emphasis is exemplified by successive presidential campaigns soliciting the support of business owners at the grass root level. The American approach to entrepreneurship fits well with the creation and development of family business. The developmental path of the family business is simplified to the success of the entrepreneur individual in the family who, upon the success of his own risk taking, incorporates members of the family into the enterprise. It is at this juncture of entrepreneurial development that many family businesses are born.

3.1 Peter Drucker: System Exploiter Converting Source to Resource

According to Peter Drucker an entrepreneur is someone who can turn the current source into resources. By extension, since the family business is an outgrowth of a successful entrepreneur, family business is also an entity that can turn a source into resource. However, there is a fine distinction between Drucker's envisage of the resourcefulness of the entrepreneur and the family business. In entrepreneurship, the turning of a source into resources comes from the entrepreneur's inventive spirit, i.e. an entrepreneur always looks for opportunities to exploit. However, a family business becomes inventive not because it look for any opportunities that come its way, but inventiveness in family business in its resource management comes from necessity and the drive to survive and succeed. Necessity in family business is driven by constrained resources. Its capital structure is restricted to personal savings and private funding. Being part of the informal sector, the family business remains an enterprise too risky for conventional lending institutions, such as banks.

Survivorship is as important as entrepreneurship. A family business undertakes risk. The risk exposure involves all family members who are involved in the enterprise. The stakeholders are risk takers in the family business. The immediate goal of the family business is to survive in the market. If the family business survives the competition, it can sustain itself. Once it survives, it is driven to succeed. The drive to succeed in family business gives the impetus to all stakeholders to focus on one target: succeed and expand.

Expansion is a natural tendency for a successful organization to develop. Success that does not lead to expansion would bring stagnation. Expanding into the new frontier in business forces the family business to engage itself in the market more actively. As it expands the breath of its business into the greater sphere in the industry and market, the family business soon sees its limitation in size, scope, speed, and strategy to compete against more organized organization: corporation. Facing such a threat, the family business turns inward and rethinks strategy. This process forces the family business to adopt the prior thinking mode of fighting for *survivorship*. As the family business struggles to survive with its already expanded operations, the pressure to become more inventive and innovative in thinking and resource allocation becomes ever keener than before. This cycle of success, expansion, contraction and innovation keeps repeating itself. With each come back, the family business renew its energy and foresight in the market. As time passes, it accumulates more knowledge on how to compete, survive, and innovate. In time, it out performs the competition and graduate itself to the next stage of development: SME. Like the entrepreneur from whom it evolved, family business is a resourceful entity. This characteristic is a key to its success in business and, thus, helps it evolve.

3.2 John McClelland: Needs Achiever

The need to achieve is the driver that helps organizations to succeed. McCelland speaks of the need to achieve by the individuals. This theory may be applied to organizations. An organization is comprised of individuals. If these individuals are achiever they will drive the organization to achieve success. This logic is not a complicated argument. To apply it to the family business helps explains how the innate entrepreneurial character of the business owner now runs the family business still remains the driving force of the new entity.

In family business, every stakeholder is an achiever. The need to achieve in family business is driven by fear of failure as much as it is by the love for success. However, for the general public the consequence of failure is easily forgotten. For the family business, the sting of failure meat shared pain among all stakeholders. The tolerance for failure is very limited. The family business puts its life's savings and all its possessions and assets into the enterprise. The failure of the enterprise means the dissolution of these possession and assets. Therefore, the fear of failure is a driving force for the family business to succeed. The family business has the love for success no less than any organization. However, unlike other entities, the fear for failure is more intense. Failure in a corporation may be tolerable. The corporation will survive failure. The individual manager may be replaced, but the organization moves on with a clean slate and looks forward to a better day. However, the family business does not have that luxury because, unlike the corporation who has easier access to bank credit and alternative source of capital, the family business is completely exposed and vulnerable. The effect of failure even in one operating period determines the life and death of the family business. McClelland's idea of the need to achieve is for self gratification. However, for the family business the need to achieve is dictated by its own survivor.

3.3 David Shapero: Risk Taking

Shapero defines the success of the entrepreneur by its risk taking trait. In family business this trait is also present. In modern risk management, spreading the risk is one means of managing risk. In family business, the risk is spread among members of the organization. All stakeholders in the family business are risk takers. Some stakeholders in the family business may not hold an ownership in the enterprise, but may have loaned money or made some kind of contribution to the enterprise with the expectation for something in return. As stakeholders these people take risk. For the family business, the involvement of many people in the enterprise does not hold reduce the risk, it only spread the mental burden of the risk to everyone among in the group. Whatever risk the family business has, it still retains fully.

Risk is defined as the uncertainty of an occurrence or nonoccurrence of an event which affects the standing of the subject (person exposed). The involvement of many people in the enterprise does not help reduce risk, it merely spread the burden of risk to all stakeholders. *Is there is difference in risk exposure by an entrepreneur and the family business*? The entrepreneur's risk is characterized by two factors: (i) the entrepreneur is the only person who carries the burden of the risk, and (ii) the entrepreneur engages his enterprise without a sense of direction, i.e. no focus on any particular business. By definition a specialist cannot be called an entrepreneur because an entrepreneur is someone who seeks and exploits opportunities. The family business, on the other hand, shares the burden of risk among family members who became stakeholders in the enterprise. Secondly, the risk exposure is reduced by the mere constraint of the family business. The natural liberty of roaming the market of the entrepreneur is confined to a defined business model limiting the family business to engage the market with well defined scope and scale. This focus of the family business allows it to harness its resources and move towards a set goal: survival and success.

3.4 Innovation Economics

Innovation economics appears to be a new school of thought in the mainstream economics. Innovation economics is defined as: the economic doctrine that uses the combination of knowledge, technology, entrepreneurship, and innovation as the drivers for economic growth (Antonelli, 2003). David Ahlstron wrote that: "the main goal of business is to develop new and innovative goods and services that generate economic growth while delivering benefits to society" (Ahlstrom, 2010). As an outgrowth of entrepreneurship, family business strives to achieve these goals: new and innovative goods and services.

Some goods and services provided by the family business may be 'new.' However, many family businesses do not involve the introduction of new invention into the market. Many of the products and services introduced by the family business are already in existence. The repackaging and delivery of these goods and services may be innovative. In the food industry for instance, the concept of a restaurant is nothing new. The restaurateur sells cooked foods and customers pay for the food. This business model becomes innovative when the family restaurant provides home cooked meal and a cozy eatery to customers. The introduction or repackaging of the product and services differentiates the family owned restaurant from franchise fast food eateries. This example illustrates that the family business actively participates in innovation economics. Economic growth stemming from this type of business seemed to have been overlooked by classical economics (Hicks and Holland, 1977; Kaldor, 1956; Pastinetti, 1959-60; 1977).

3.5 Imitation Economics

If innovation is the introduction of new and creative thinking of the entrepreneurial spirit, there is also another business model that may help explain the success of some family businesses: *imitation economics*. Innovation requires thinking; a special kind of thinking: inventive and creative thinking. However, in the less developed economies, there is an easier way to reach the target: survival and success in the market by means of imitation.

Unlike innovation which requires creativity and inventiveness, imitation economics is a copycat economy. This lack of originality may leads to success of some businesses, but the 'success' comes at the expense of someone else hard work. It is an outright stealing of other people's ideas. This unethical business model also finds its way into the real of family 'business.' These criminal activities deserve punishment. Like other criminal activities, intellectual property theft is a multibillion dollar industry.

3.6 The Austrian School of Thought

The Austrian school of economic thought based its economic theories on the ‘purposeful actions the individuals’ (Boettke, 2008). Despite the earlier reluctance by the classical and mainstream school of economic though, Austrian economics is now part of the mainstream economics (Birner and van Zijp, 1994). The application of Austrian economics to family business comes from Schumpeter’s writing on entrepreneurship (Birner and van Zijp, 1994). The application of Schumpeter’s claim of innovation in entrepreneurship has a theoretical relevance to family business because family business grows out of entrepreneurship.

3.7 Schumpeter’s Creative Destruction and Innovation

The original theory of entrepreneurship was laid by Joseph Schumpeter, a prominent economist of the Austrian Economic School of Thought. Schumpeter’s analysis of economics focuses on individual action. Two key concepts were introduced by Schumpeter: innovation and creative destruction. *Innovation* refers to the inventive spirit of the entrepreneur which is the driving force of economic growth and development. Creative destruction refers to the ceaseless competition of the market economy compels all players in the economy to continually invent new technology, products and services in order to survive the competition. As new technology, or product and services are introduced into the market, older technology, or products and services become obsolete. The competition that forces the business owners to be innovative in creating new products and services helps destroys the existing order. This process is called creative destruction.

In the context of family business, the owner of the family enterprise has to maintain vigilant on innovation. Recall that innovation is comprised of two elements: (i) input innovation which focuses on cost reduction, and (ii) performance innovation which focuses on increasing output. Input innovation is consistent with all forms of business. An entrepreneur looks for means to reduce cost in order to increase profit. The family business search for ways to reduce expenses in order to keep cost down and stay competitive by passing the savings to consumers by means of price reduction. SMEs and corporation also work towards cost reduction through process improvement and shorten the channels between the products and consumers or cheaper source of raw materials. As part of the overall corporate strategy, corporations also aim to reduce cost. Cost reduction that leads to the creation of competitiveness of the entity defines one form of innovation called input innovation. In the family business, cost reduction is a vital interest for the enterprise because the family business is always vexed with resource constrain. The allocation and utilization must produce the optimal yield. Input innovation is consistent with this drive by the family business.

Performance innovation, also called output innovation, is concerned with the creation of optimal output. Production efficiency is defined as the production of output at the highest level at any given level of input. Although performance innovation may be the ultimate target of every form of organization, it is more so for the family business. The limited scope of the family business allows it to stay focus. The limited resources of the family business force it to be circumspective in resource utilization. The typically small size of the family business affords it to be flexible in face of changing market condition. Most family businesses are not considered factor intensive; therefore, it could adapt to the changing operating environment more easily than a larger entity, such as a larger SME and corporation where long-term asset commitment in a certain project may prevent it from quick divestiture.

4.0 INNOVATION IN FAMILY BUSINESS

4.1 Input Innovation in Family Business

The first type of innovation is called input innovation. Input innovation is “cost cutting without the sacrifice of quality.” Cost cutting is the main driver for business logistics. The main objective of business logistics is to improve profit. One means to improve profit is to cut cost. A family business is the type of business that is defined by limited resources. As a small entity, the family business is easily managed. Members of the organization are mostly related within the circle of the management team; therefore, communication is more effective. In addition, the level of bureaucratic complexity is less cumbersome in family business than in other highly structured organization, such as an organization.

The objective of the family business is to create value. Value creation may be achieved through input innovation. Input innovation is cutting cost. Cost cutting may contribute to the improvement of output efficiency. Efficiency is the absence of waste. Economic waste tends to occur where there is abundance of resources and the organization is large. In family business, the organization is relatively small and the resource is not abundant. All family business during its first generation of operation faces a constant challenge of resource limitation. This internal constraint forces family business to be efficient in resource utilization. Efficiency is defined as the use of minimum input to produce optimal output. Efficiency is the indicator of input innovation and input innovation is the measure of success for family business.

4.1 Output Innovation in Family Business

To put it simply, output innovation is to product more output with the same level of input. In order to produce more with the same level of input, the agent must improve work process. Generally, in larger corporations innovation comes from research and development (R&D). However, in family business, process improvement does not come from such a formal structure. Most success of the family business comes from experience. Through experience, and thus the application of the learning curve, cost is reduced. Cost reduction leads to an increase in output.

Most family business lacks the formal training and R&D, how can innovation be possible? Family business is masterful in resource management. Resources are limited and the family business always finds ways to sharpen its skill to achieve efficiency in resource utilization. In s doing, the family business becomes the resourceful in raising its productivity level. The drive for the family business to be innovative is its resource limitation. This limitation coupled with its needs to survive and succeed provides the ingredients for success in family business.

4.2 Creative Destruction in Family Business

Both the American and Austrian Schools of Thoughts credit the small business, i.e. family business and entrepreneur to the innovative spirit that moves the economy. These are the people at the grass root level who create jobs and serves earn the bread and butter for the economy. Schumpeter introduced the idea of "creative destruction" as a means to describe the life and work of the small enterprise of the individuals and family business. Although Schumpeter did not name "family business" directly in his description of creative destruction, all SME, family business and entrepreneurial enterprises are included in that process.

Competition in the market leads to the creative process among players in the market. New technologies are introduced. As soon as these technologies are introduced into the market, the owner of the technology will retain exclusive ownership of that technology for a period. This exclusive ownership provides incentive for people to be creative and innovative. However, the monopoly to the technology is not long lasting. As the exclusivity is the incentive for the owner of technology to be innovative, it is serves as an incentive for other players to enter the market. Thus, market innovation for better technology always breaks new frontier. As new technologies are put forth in the market, the old ones become obsolete. The process continues. This process is called creative destruction.

Creative destruction has a role to play in the family business. In order to survive the competitive, family business must be innovative. Some family businesses are short lived because they cannot change or keep up with the competition. As the result, they become victim of the so-called creative destruction. Successful family businesses are those that can survive the competitive by being creative in producing and present their products, and pursuing the market through active engagement. Active engagement means that the family business owner must engage all stakeholders in the organization to look for opportunities in the market, and inwardly each member of the organization must also look for better ways to do business, i.e. cost cutting.

4.3 Application of Schumpeter's Theory to Family Business

As the founding father of the concept of innovation and creative destruction, Schumpter left a lasting legacy in the filed. Schumpeter's concept is divided into two elements: Mark I and Mark II. In Mark I, Schumpeter argues that innovation comes from entrepreneurs whom Schumpeter said are the people who possessed the 'wild spirit' (*Unternehmergeist*). At a later stage of his career, during his tenure at Harvard University, Schumpeter proposes that the entrepreneurial spirit still exists among corporate leaders. Success in Mark I is carried on the legacy in Mark II where corporate leaders further push innovation through resource allocation for research and development.

Both Mark I and Mark II can be incorporated into the family business. As a small enterprise, the family business is forced to be innovative in its market. Most of the product and services offered by family business are generally not new or novel in a sense that they are repackaged product and services. This constraint is further complicated by the fact that family business has limited resources and is semi-structured. One way to stay afloat in the market in face of competition is to innovate. As the family business becomes successful and expand into SME and finally corporation, Mark II can appear with resource allocation to research and development.

4.4 The Thinking of Mixed Schools

In every field of studies, there are schools of thought that help explain the basis of the theoretical foundation for the subject matter. In business management, there is no exception. However, within business management field, there seems to be a theoretical void when the subject of family business is brought up. What is the theory that governs family business? There is no one answer to this question. Family business is an entity in transition between the developments of the successful entrepreneur into SMEs; however, prior to becoming SME, family business seems to be the temporary resting ground to collect momentum for further push to the next stage of development. For that reason, in our attempt to study family business, theories from entrepreneurship and theory of firms are drawn to our aid. Some of these explanations do not belong to any group and can stand on their own in explaining the life and being of the family business.

4.5 Systematic Approach: Explorer, Exploiter & Protector

The development of business may be divided into three stages: system explorer, system exploiter, and system protector. At the first stage, the system explorer is best exemplified by the entrepreneur who looks for opportunities. An entrepreneur looks for opportunities and engages every opportunity that he could afford so long s there is a probability of gaining a success from the enterprise. The enterprise of the entrepreneur is undefined.

As the entrepreneur becomes successful and that success is sustained, he may involve people within his circle of influence. The people whom the entrepreneur recruits for his enterprise are family members. This is the birth of the family business. The family business help shape the enterprise to stay focus on a particular business. The family business is a system exploiter because it focuses on a business that it sees as profitable. The family will remain a system exploiter throughout its life and even when it transforms itself into some thing more structured and organized: SME. The family business exploits the system by intensifying its efforts, investment, and innovative efforts to create value. Value creation is the key to success at this stage of the business.

The family business creates value through input innovation and output innovation. In input innovation, the family business creates value through cost reduction. Cost reduction allows the business to sell at a lower price. Competition based on price allows the company to increase revenue and, thus, create value. Output innovation also has the same effect on value creation. The increased productivity of the family business allows the business to sell more and create value. As the success of the family business is sustained, it moves up a stage in development in becoming and SME. The successful SME will also move up a stage of becoming a corporation.

During the SME stage, the business carved for itself a territory in the market called market share. The family business now fights to protect its market share. The mode of conduct of the business now is classified as system protector. It becomes more conservative in its thinking. It becomes less entrepreneurial, and to a large extent, system protectors will not take risk. Risk avoidance generally leads to the lack of innovation. Without innovation, the organization becomes stagnant and will be threaten with outside competition. In order to protect its territory, large resources are required. Even so, the protection is an upstream better. Schumpeter's creative destruction process plays out its role. Unless the business responds appropriately, it will perish in the process.

Therefore, system protector is not a sustainable strategy for the business. The family business finding itself defending against the competition is a system protector. In order to maintain its position in the market, it must re-invent itself in the market by becoming a system exploiter. In order to be a system exploiter, the family business must be able to mobilize faster in order to keep up with the market change. Faster mobilization requires the organization to be lean. Lean organization requires the loosening of the organizational structure and allowing the management to be innovative and inventive in producing and presenting its products to the market. From this process analysis, system exploiter appears to be the most effective model for the family business to sustain itself in the market. System explorer is not sustainable because the wild spirit of the entrepreneur creates a business without clear direction. Without clear direction, the business soon hits a dead end. System protector is a mature stage of development, but it is a defensive posture that would soon succumb to the pressure of creative destruction exerted by the market.

4.6 Value Optimization: Steepest Ascent and Steepest Descent Models

Optimization is a theoretical field in operations research that deals with minimization and optimization (*See* Bhati, 2000; Bronson, 1982; Hiller and Liberman, 1990; Marlow, 1993; Papadimitriou and Steiglitz, 1998; Polak, 1971). Although it is highly technical, dealing with mathematical models using calculus of variations, control theory, convex optimization theory, decision theory, game theory, linear programming, Markov chains, network analysis, optimization theory, queuing systems, etc., it may be a relevant tool to our analysis of family business to the extent that innovation concerns family analysis.

Recall that innovation deals with the minimization of input cost and optimization of output or performance. Optimization theory is an effective tool for performance analysis of family business. Although family business is small and may not need sophisticated theoretical tool for its operation, there might be cases where the family business grows as big as a large corporation but remains closely held within family circle. In that case, conventional corporate tool for business operations and analysis, such as operations research (Bazaraa *et al.*, 1993; Bronson, 1982; Chong and Zak, 2001), may be of interests to family business. We leave this issue to other sections of the book dealing with *optimization* and *operations research*.

4.7 Stakeholder Theory

The stakeholder theory was introduced by Edward Freeman in 1984 to help explain correct the inadequacy of the firm theory (Laplume *et al.*, 2008). The traditional theory of firm defines stakeholders as the company management and the shareholders. The company management holds a fiduciary to the shareholder: a duty to maximize the shareholder's wealth. Freeman's theory of stakeholders includes the followings as stakeholders: governmental bodies, political groups, trade associations, trade unions, communities, financiers, suppliers, employees, and customers (Freeman, 1984).

The stakeholder theory is also applicable to the family business. At the first degree of relationship, the stakeholders in the family business are those who contributed money to the enterprise, holds interests in the ownership of the enterprise, and those who working within the family business organization. At the second degree of relationship, the stakeholders are people who come into direct contact with the family business. These people include suppliers, customers and state compliance authorities. In the third degree of relationship, the stakeholders may include everyone else not listed in the first and second degrees. In this sphere of influence model, the family business sets itself up as a more structured than the entrepreneur who was freer to act without any concerns for stakeholders' interests.

As members within the sphere of influence of the business, stakeholders can be asset and liability to the business. The more expansive the sphere the more the business has to live up to the varied expectation of each group. However, if the sphere of influence is too limited or narrowed, the business may limit its own future. Therefore, in order to succeed, family business owner must balance interests and responsibilities in serving these its stakeholders. As the family business grows, this responsibility becomes greater and the sphere of influence of stakeholders will also expand, in order to maintain its position the family business must push itself to the next level of development: SMEs and finally corporation.

5.0 CURRENT RESEARCH TREND IN ENTREPRENEURSHIP

The Current research Trend and Theories

What is the current research trend on family business? Family business is not an independent field of discipline. It is part of the rubric of a larger and undefined field of entrepreneurship and SMEs. Most research focused on the more structured business; the theory of firm is more targeted on well established organization, such as corporation. Entrepreneurship, on the other, had a good start with Cantillon, Say, and Schumpeter, but the excitement seemed to fizzle in the early 1930s after the Great Depression. Family business is a semi-organized structure that is in transitional stage between an entrepreneurship and an SME. For that reason, it is commonly overlooked.

Research must be guided by theories. These theories must be able to substantiate by empirical data. As part of the informal sector, data of family business is not available for analysis. Moreover, the link between family businesses and the academia is also undefined. Whereas larger corporation who are more endowed with financial resources are more attractive to academic researchers, family business is not attractive due to its informality and lack of funding for the academia.

5.1 Qualitative Research

Qualitative research is a research method based on *positivism*: society and human behavior may be model mathematically and verified through empirical data (Cohen and Maldonado, 2007). In its purest form of positivism, intuitive and introspective knowledge is rejected. August Comte, one of the earlier proponents of positivism in qualitative research, argued that much like the physical world, society can be mathematically model and explained through empirical data (Macionis, 2012). This approach to positivism was explained by an English theoretical physicist and cosmologist, Stephen Hawking, thus:

> "Any sound scientific theory, whether of time or of any other concept, should in my opinion be based on the most workable philosophy of science: the positivist approach put forward by Karl Popper and others. According to this way of thinking, a scientific theory is a mathematical model that describes and codifies the observations we make. A good theory will describe a large range of phenomena on the basis of a few simple postulates and will make definite predictions that can be tested… If one takes the positivist position, as I do, one cannot say what time actually is. All one can do is describe what has been found to be a very good mathematical model for time and say what predictions it makes." Stephen Hawking (2001). The Universe in a Nutshell. p. 31. ISBN 0-553-80202-X.

According to Hawking's positivism and the common sense of August Comte, Albert Einstein general theory of relativity is also a qualitative model. Qualitative research is considered valid so long as it employs scientific methods and is subject to verification (Lincoln and Guba, 1985). However, much of qualitative research of today does not meet the earlier period's strenuous standard: member check, interviewer corroboration, peer debriefing, prolonged engagement, negative case analysis, auditability, confirmability, bracketing, and balance. For that reason, qualitative research does not command the trustworthiness of the scientific community.

In family business research we are faced with the same predicament. As part of the informal sector of the economy, family business data collection and availability are not adequate for quantitative analysis. Even for qualitative research, researchers are not adequately trained for the task. Researchers in this field would mostly be drawn from social science background these researchers may not be adequately train in scientific methods. Qualitative research that is laden with intuition and the so-called "interviews" are mostly subjective and lack scientific validation by empirical data.

5.2 The Failure of Case Studies

Attempts had been made with case studies. Almost without exception, these attempts failed. Business case studies grew out of the teaching method employed at the Harvard School of Business. Case studies grew out of the teaching method used in the American law schools. To avoid reading long cases, law school textbook authors redact case opinions (judgment of the court). These redacted court opinions are put into a textbook. Each law book contains well over 500 pages. For convenience, students summarize the long court opinion into a *case brief*. The case brief is comprised of the following elements: issue, rule, analysis, and conclusion. A 50-page court opinion is generally summarized into one page. Without knowing the components of case briefing, many writers attempt in writing business cases which turn out to be uninteresting and without structure.

In family business, there may be literature in the field which attempts to explain family business through case studies. These attempts are failure on display in real time. In order to write a case successfully, the writer must know the theory explaining the issue. In this case, what is the theoretical foundation for family business? Lacking the answer to this question, no matter how many attempts are made in case studies on family business, they will all fail. There are success stories. These cannot be classified as case studies. They are the narrative of the company history with no theoretical context.

5.3 Quantitative Research

Quantitative research is the systematic empirical investigation of social phenomena using statistical, mathematical or computational techniques (Given, 2008). A survey of research in sociology between 1935 and 2005 found that two-thirds of the research used quantitative methods (Hunter and Leahey, 2008). Between qualitative and quantitative methods, quantitative method would be preferable because the theory is supported by theory and the theory is supported by empirical data. Pure qualitative method lacks the degree of objectivity requires for scientific objectivity. Quantitative research in family business is a challenge because family business is part of the informal sector. Formal data collection of family business is lacking. Therefore, researchers tend to engage in interview survey---which lacks scientific objectivity and the ability to be replicated.

The foundation of quantitative research is constructing the theoretical modeling. The modeling is to be followed by empirical data. The theoretical foundation is not a problem in family research. However, the data collection to confirm data becomes problematic because the informality of the family business makes data collection difficult. The unstructured nature of the family business and their wide spread locations may make data collection not accessible.

6.0 CONCLUSION

The attempt to put family business into a theoretical frame work is not an easy task. The paper starts with the review of various entrepreneurship theories to help connect entrepreneurship to family business. The rationale for this connection is that this book takes a position that family business does has its origin, and that origin lies in the growth of an entrepreneur. Successful entrepreneur expands his business to include family members. Although there might be cases where the family business did not start from the growth and success of an entrepreneur; the family business may come about through inheritance, transfer, acquisition, succession, or the business may have started out as a full scale family business. However, these cases are not the most prevalent. The most prevalent form of family business is one who follows through the successive stage of development from an entrepreneurial enterprise run by an individual to a family business where the ownership may be shared by family members and stake holders increases from the entrepreneur sole proprietor to joint ownership. Research in this area is sparse. The available literature cannot provide definite theoretical framework to help explain the operation, structure, organization, and functions of the family business. The tension between qualitative and quantitative approach to research remains an active issue. However, in the final analysis, empirical data augmented with quantitative model would win the argument. The current trend is the use of mixed-method or purely quantitative (Diriwächter and Valsiner, 2006). Pure qualitative research will soon fall out of favor due to its lack of objectivity.

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