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Family Firms and Investment–Cash Flow Sensitivity: Empirical Evidence from Canada

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Abstract : Family firm is the most common form of business organization in the world. Many family businesses rely heavily on their own capital to finance their expansion. This dependence on internal funds for their investment may be deliberate to maintain the family dominant position or involuntary as family firms have limited access to external funds. Our understanding of family firm's choice to fund their own growth using existing capital is somewhat limited. The aim of this paper is to study whether the presence of a controlling family in the company either mitigates or exacerbates external financing constraints. The impact of family ownership on investment–cash flow sensitivity is ultimately an empirical question. We use a sample of 406 Canadian firms listed in Toronto Stock exchange (TSX) over the period 2005–2014 in order to explore this relationship. We distinguish between three elements in the definition of family firms, specifically ownership, control and management, to explore the issue whether family firms are more efficient organisational form. Our research contributes to the extant literature on family ownership in several ways. First, as our understanding of family firm's investment cash flow sensitivity is somewhat limited in recession times, we explore the effect of family firms on the relation between investment and cash flow during the recent 2007-2009 financial crisis. We also analyse this relationship difference between family firms and non family firms before and during financial crisis. Finally, our paper addresses the endogeneity problem of family ownership and investment-cash flow sensitivity.
Keywords : family firms, investment–cash flow sensitivity, financial crisis, corporate governance
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