Spotlight
by CeFEO

How do family firms respond differently when facing an economic crisis?

Managing layoffs in time of crisis

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Economic crises, whether global or local, frequently disrupt businesses, leading to layoffs, reduced consumer demand, and financial strain. While all companies must navigate these tough times, family firms often handle such challenges differently. Given their unique blend of emotional and business considerations, the decisions they make—especially regarding employee layoffs—are shaped by the desire to maintain socioemotional wealth (SEW) and protect long-term legacy.

WHAT WE STUDIED

The study focused on understanding how family firms responded to the economic crisis, particularly in terms of layoffs, compared to non-family firms. The researchers examined over 121,000 privately held Swedish firms between 2004 and 2012, with a specific interest in how family control influences employee retention during a crisis. By using the 2007-2009 global financial crisis as a case study, they aimed to test whether family firms were less likely to engage in involuntary layoffs and how factors like rural versus urban settings influenced these decisions.

The research drew on theories like socioemotional wealth (SEW) and threshold theory, which suggest that family firms prioritize maintaining their non-financial wealth (like family reputation and employee relationships) during crises. However, when the crisis deepens, family firms may also adopt retrenchment strategies to protect their business's survival.

KEY INSIGHTS

1. Family Firms Are More Reluctant to Lay Off Employees

The study found that, generally, family firms are less likely to engage in involuntary layoffs during a crisis compared to their non-family counterparts. This reluctance stems from their desire to maintain SEW, which includes preserving long-term relationships with employees and sustaining their reputation within the community.

2. Crisis Forces Retrenchment Strategies

Despite this inclination to protect their workforce, family firms are not immune to economic pressures. When survival is at stake, family firms, particularly those in rural areas, may adopt retrenchment strategies like workforce reductions. However, these layoffs often occur as a last resort and are implemented with the long-term survival of the firm and the community in mind.

3. Rural vs. Urban Family Firms React Differently

Interestingly, the research revealed that family firms located in rural areas were more likely to lay off employees than those in urban areas during the crisis. This is because rural family firms often face greater resource constraints and depend more heavily on their local communities. In these areas, the loss of a family business can have devastating social and economic effects, leading owners to take more drastic actions, such as layoffs, to preserve the business in the long run.

4. Family Firms Have Higher Embeddedness in Communities

Family firms in rural areas exhibit higher levels of local embeddedness, meaning they are more closely tied to the well-being of their community. This makes the decision to lay off employees even more challenging, as it affects not just the firm but the entire community. However, in times of severe crisis, the need to ensure the firm's survival may outweigh concerns over immediate reputation or SEW loss.

TAKEAWAYS

For Family Business Owners

1. Preserving Relationships

Family firms should continue to prioritize their long-term relationships with employees, as these bonds often contribute to resilience during and after crises. However, owners must also recognize when protecting all jobs could jeopardize the business's survival.

2. Balancing SEW and Survival

Striking a balance between maintaining socioemotional wealth and ensuring business longevity is critical. Family firms should carefully assess when layoffs are necessary and communicate openly with employees to minimize damage to relationships and morale.

3. Rural Family Firms Need Special Attention

Family firms in rural areas, in particular, should be mindful of how layoffs impact the broader community. While difficult decisions may need to be made during a crisis, planning for the long-term survival of the firm and its role in the community can help mitigate some negative effects.

For Policymakers

Policymakers should recognize that family firms play a unique role in maintaining social and economic stability, especially in rural areas. Crisis relief packages could be designed with family firms in mind, helping them avoid drastic measures like layoffs while still securing long-term survival.

CONCLUSION

The behavior of family firms during crises provides key insights into how emotional and financial considerations intersect in business decisions. Family firms, driven by a desire to protect their legacy and maintain socioemotional wealth, tend to retain employees more readily than non-family firms, even during economic downturns. However, when survival is on the line, rural family firms may resort to layoffs to preserve the business's long-term viability.

These findings emphasize the need for family businesses to strike a careful balance between protecting relationships and ensuring survival. Moreover, they highlight the vital role family firms play in sustaining local communities, especially in rural areas where their embeddedness is stronger. As the global economy continues to experience crises, understanding these dynamics will be critical for supporting family businesses in maintaining both economic and social stability.

RECOMMENDATIONS

For family business owners, the key takeaway is to assess your priorities carefully during crises. While employee retention is crucial, ensuring the long-term survival of the business might sometimes necessitate difficult decisions. Open communication and strategic planning can help mitigate the negative impacts of layoffs. Policymakers should consider tailored crisis support for family firms, especially those in rural areas, to protect these essential economic drivers during turbulent times.

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