

Examination of innovation and effectiveness in the case of family businesses

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Abstract: The role of family businesses is significant in both the Hungarian and European Union economies. The issue of innovation is crucial for the survival and development of family businesses. For the development of family businesses, which are typically small and medium-sized enterprises, the willingness to innovate is essential. Therefore, in the course of my research, I examine how innovativeness is characteristic of family businesses, do SMEs plan to implement some kind of innovation in the near or distant future, and if so, from what source do they intend to finance it? In the course of my research, I will also investigate whether there is a relation between the innovation activity of enterprises and the efficiency of enterprises. The effectiveness of family businesses is examined by various side, not only financial, but also the effectivity achieved in the field of customers, for example.

Keywords: family business; small and medium enterprises; effectiveness; innovation

1 The concept and characteristics of innovation

Looking at the theoretical literature and its practical economic application, we can come across many approaches to the concept of innovation.

The emergence of the concept of innovation in economics is attributed to Schumpeter. In Schumpeter's (1939) approach, innovation is nothing more than some new combination of production factors, the implementer of which is the entrepreneur. Accordingly, the following cases of innovation can be distinguished:

- production of a new product or commodity, or an existing one in a new quality
- introduction of a new production or sales procedure
- new placement option, appearance on a new market
- of new procurement sources of raw materials or semi-finished products application
- introduction of a new organizational structure

The OECD and Eurostat (2005) also deal with the definition of the concept of innovation in the so-called Oslo Manual. Innovation in their approach

- "new or significantly improved product (goods or services) or process,
- new marketing method, or
- introduction of a new organizational method."

This is a significant change compared to previous formulations, because by omitting the term technology from the concept of innovation, it enables a broader interpretation of the concept and provides an opportunity to include smaller businesses and service sectors that offer lower research and development potential in the scope of innovation (MISZ, 2013).

The majority of researchers and economists interpret the concept of innovation according to a broader approach, including Chikán (1997), who says that innovation means a new, higher-quality satisfaction of consumer needs. This broad approach sets virtually no limits on how this "innovation" should take place. Not all economists agree with this approach, Kotler (1999) considers something to be an innovation only if it is a strategic novelty representing a high novelty value. Porter (1989), on the other hand, is satisfied with smaller innovations, which include the essence of innovation in the form of continuous improvements.

According to Pakucs (1999), innovation does not have to be new from a scientific point of view or reveal a completely unknown result, it is enough if it represents something new in a given market or area, it can even be a methodological procedure.

Rohács (2001) highlights that innovation does not only affect the scope of research and development, but can be interpreted in a significantly more extensive way: research - development - technical design - production.

Rohács (1997) points out that the product development cycle has now been significantly transformed, in the past the product was developed based on the developer's idea, the production technology was defined for this, which resulted in a cost, on the basis of which the price of the product was established, which price was tried to be accepted by the market. Nowadays, during product development according to the modern concept, they start from market conditions and needs. They assess what needs need to be met, in what form, under what conditions and at what price. After that, they create the requested product and try to produce it at the price expected by the consumer.

2 Method and Sample

2.1 Method

The research was conducted using an online questionnaire, following the principles of the snowball method. In this study, 2,183 valid questionnaires were processed, the majority of which were based on surveys of micro, small and medium enterprises. The results obtained are not representative. The obtained data were processed using the SPSS 25 statistical program package.

2.2 Sample characteristics

Based on the examination of the enterprises according to the number of employees, 74% of the sample were micro-enterprises, 20% were small enterprises, and 5% were medium-sized enterprises. Based on the categorization according to the number of employees, large companies accounted for nearly 1% of the sample. (Figure 1)

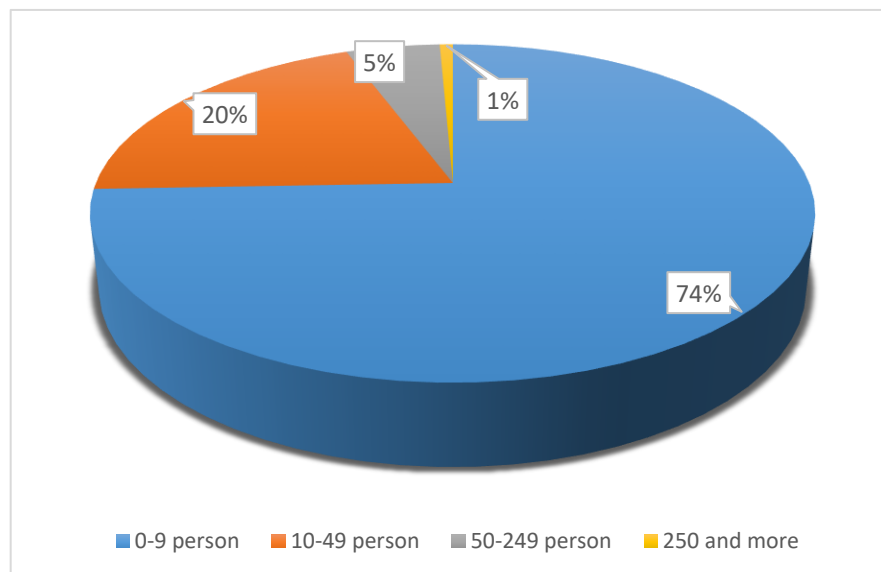


Figure 1
The number of employees of enterprises
Source: own research

The majority of the surveyed businesses are located in Budapest or Pest County (48.8%). The proportion of companies with locations in Northern Hungary is second largest (13.7%), followed by the Southern Great Plain region (9.6%). The

region with the fewest businesses is the Southern Transdanubian region, with nearly 5% (4.7%). (Figure 2)

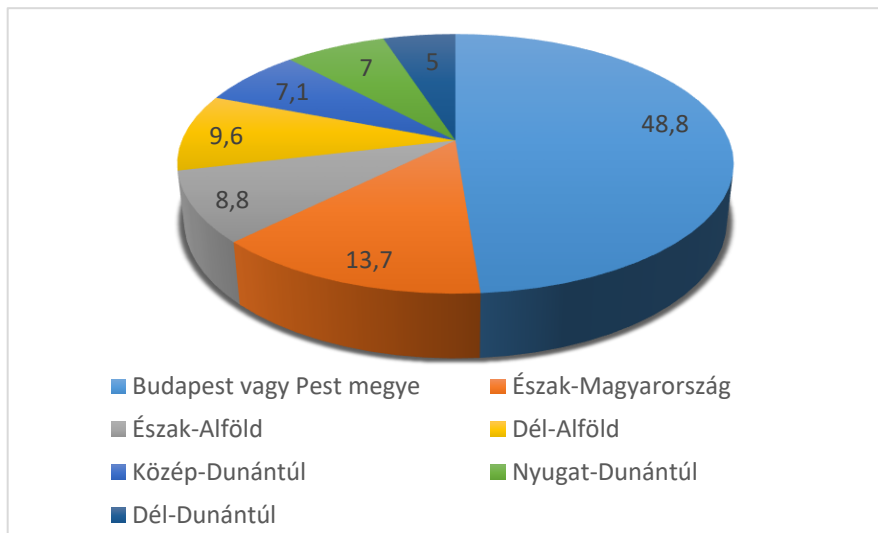


Figure 2
The region of activity of the enterprises
Source: own research

I also examined the composition of the sample based on the activities of the enterprises. According to this, a significant part of the enterprises (28.1%) are active in trade, 15.1% in the construction industry, and 14.7% in other services. The fourth most important is the manufacturing industry with 8.1%, followed by agriculture, fish and forestry with 7%. Accommodation services and catering account for 5.9% of the sample, financial services, real estate, economic consulting for 5.6%. Transport, storage, telecommunications and post accounted for 3.9%.

In terms of market presence, the dominant part of the examined enterprises (33.9%) is present in the market of consumer services, and 18.8% in the field of industrial services. 12.2% of them are involved in the production of consumer durables, and 2% of raw materials and components. 9.9% of the surveyed SMEs produce consumer goods. 3% of the enterprises dealt with the production of market production equipment. (Figure 3) The others marked the other category, but they had a problem identifying the market area, so in fact a significant part of the other category also belongs to the services market. Categorizing these businesses would have been a disproportionately large task, so I didn't do it.

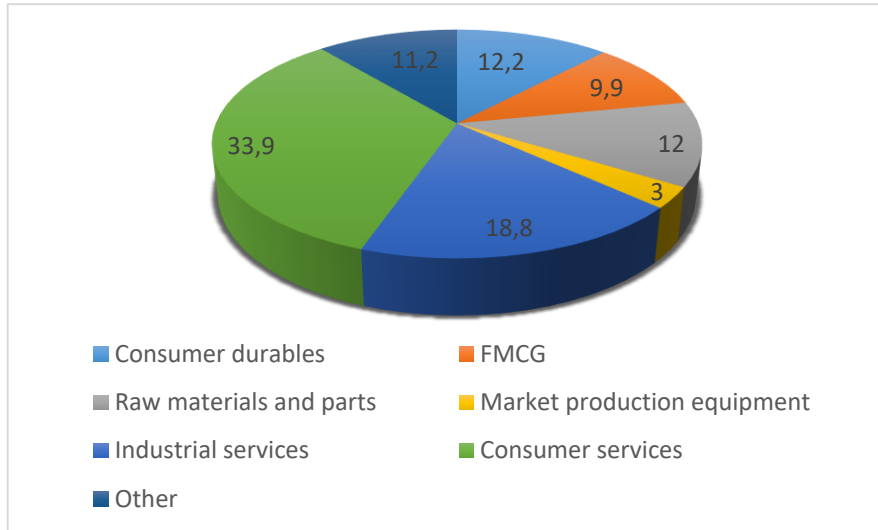


Figure 3
The market of the enterprises
Source: own research

3 Results of the examination

3.1 Examination of innovation in the case of family businesses

In my research, I also asked what entrepreneurs mean by the concept of innovation. The answers clearly indicate that the managers of SMEs are aware of the meaning of innovation, however, as is typical in professional circles, there is no agreement on the definition of the term.

Only 1.8% said they did not know what it meant. According to 41% of them, it means a major innovation in any area of the business, according to 37.2% of them, a minor innovation can also be considered an innovation, while 19.1% of them said that it is a revolutionary innovation in the technical area of the business. (Figure 4) The remaining respondents, who marked the other category, actually provided additional possible definitions of innovation.

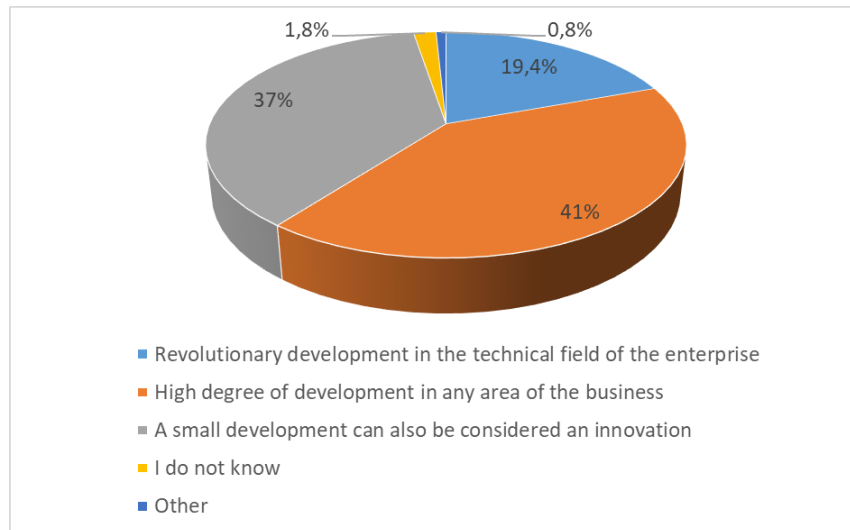


Figure 4
Innovation according to entrepreneurs
Source: own research

When asked whether their company plans to innovate in the near future, most respondents (38.7%) answered that within 2-5 years, 26.6% planned innovation within one year, 3.3% within 6-10 years within, and 1.2% of them saw reality beyond 10 years or formulated an intention in this regard. (Figure 5) From these answers, it can be deduced that a significant number of SMEs have already expressed a serious intention regarding the need to create innovation within their company. The innovation you want to implement in the short term, within a year, obviously already means a strong determination, but the intention expressed in relation to the medium-long term (2-5 years) already suggests a more serious consideration/determination. The intention of planning for a period beyond 6 years is still weak, it still carries a lot of uncertainty. 29.9% of enterprises do not plan to innovate. The reason for this may be that the company did not recognize the necessity or advantage of this for the business, but it may also be because the SME does not have sufficient resources to implement this, or does not want to get into debt if it had to use external resources.

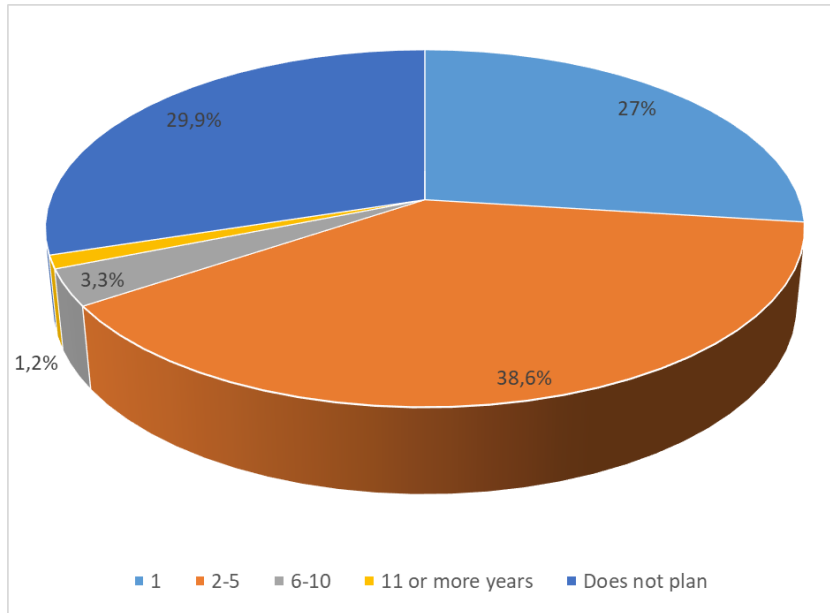


Figure 5
When do businesses plan to implement innovation?
Source: own research

It is also interesting to examine the source of those who plan innovation. Respondents could indicate several answers, but it is worth noting that only 12.8% of respondents were those who would at least partially finance the planned innovation with a loan. (Figure 6) 38.7% of the interviewed entrepreneurs were expecting some form of grant funding, and 13.9% were also expecting subsidies. The majority saw the solution for SMEs in their own capital. 49.7% of the entrepreneurs would like to solve the innovation at least partly from the profit previously generated and accumulated by the business, and 26.1% of them also plan to raise new capital for the purpose.

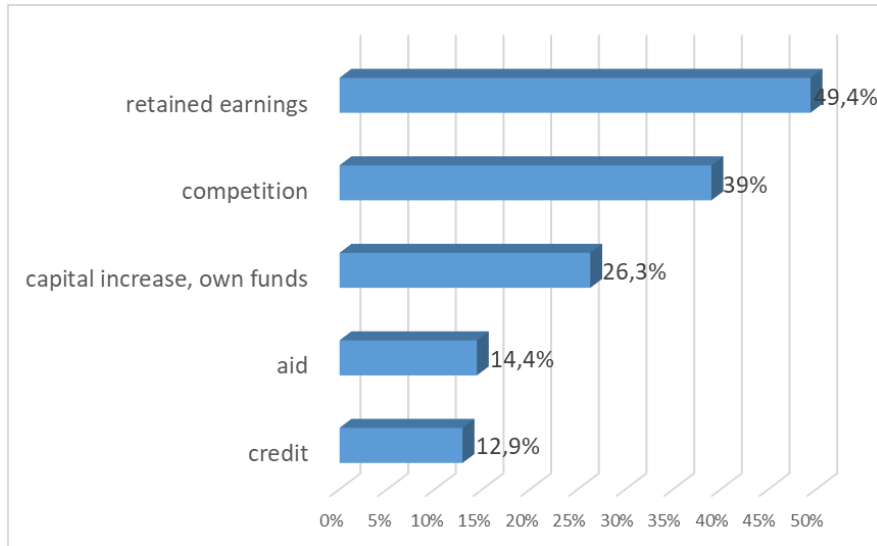


Figure 6
Source of planned innovation
Source: own research

3.2 Examination of effectiveness in the case of family businesses

Another area of my research is the effectiveness of family business. In this context, I examined the effectiveness in several aspects, creating 12 financial and non-financial indicators to examine the effectiveness. Using a five-point Likert scale, respondents were able to rate the performance of their own business (5 = much better, 1 = much worse). The indicators include some that measure the profitability of the business and others that measure customer satisfaction. Four indicators evaluated the profitability/profitability of the company (profit, profit margin, turnover, return on equity), three indicators evaluated the performance towards the customer (customer satisfaction, customer loyalty, customer trust), four indicators examined the performance of the producer/service provider (productivity, lead time, turnaround time, unit cost of goods/services) and I also asked about the growth of market share.

However, there was one question, separate in the later part of the questionnaire, which was aimed exclusively at how the entrepreneur judges the performance of the previous years of the company: did the company perform better or worse. This question also served as a control for the group of questions examining previous effectiveness, that is, whether the entrepreneurs' answers were consistent with each other.

In the case of the independent question, we can see that entrepreneurs typically judge their company's performance to be better compared to the previous period. According to 54.5% of the respondents, their business is performing better than in the previous period. According to 38.8%, their market situation has not changed. In contrast, only 6.7% of SMEs said that they perform worse.

So I used different indicators to examine how well the company performed in the last financial year compared to the previous year? (1 – much worse, 5 – much better)

The first indicator examines the profitability of the business, in sum: profit achieved. Based on the obtained results, we can see that the profits of the majority of enterprises have increased in recent years, compared to the profits of the previous year. 40.8% of them performed better in this area, while 15% of them admitted that they did much better. (Figure 7) So, more than 56% of them see a positive change in profits. More than a third of the respondents (35.7%) said that their company's profitability is in a similar situation. A total of 8% of entrepreneurs said that their profits had worsened in the past period, of which 1.8% said that they achieved a much worse result. (Figure 8) It should not be forgotten that the research covers a period of several years starting from May 2017, that is, the answers received show the trends of the previous few years.

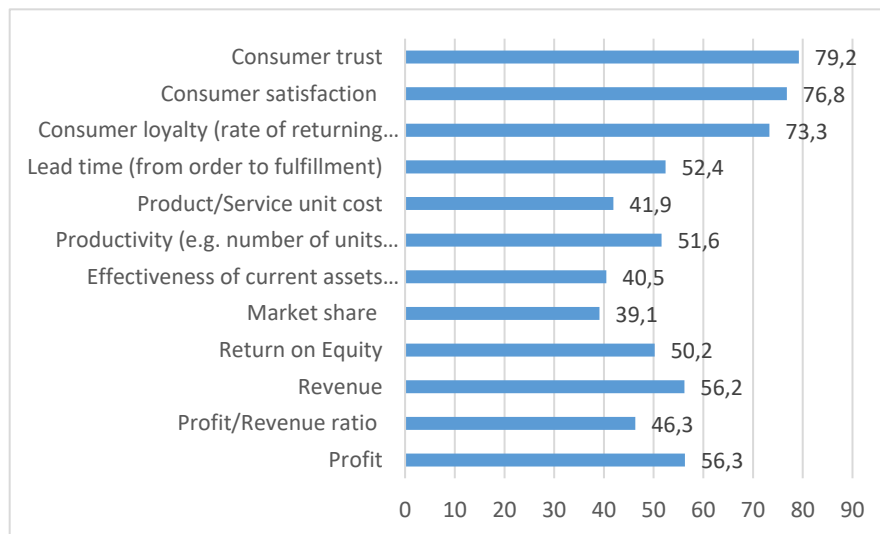


Figure 7

The proportion of those who perceive an improvement in their effectiveness

Source: own research

In the case of the profit margin, only 46.3% see that the situation has improved, while 45% say it has not changed, and 8.6% perceive a deterioration (of which 1.5% perceive a much worse result)

If we look at the development of sales revenue, we see that entrepreneurs paint a similar situation in the case of sales revenue as in the case of profit. More than 56% of them feel that sales have improved compared to previous periods, of which 13.5% see that the situation has improved significantly. According to 35.2%, the situation is similar to previous periods. Only 8.6% perceive that the situation has worsened, of which only 1.6% see it as significantly.

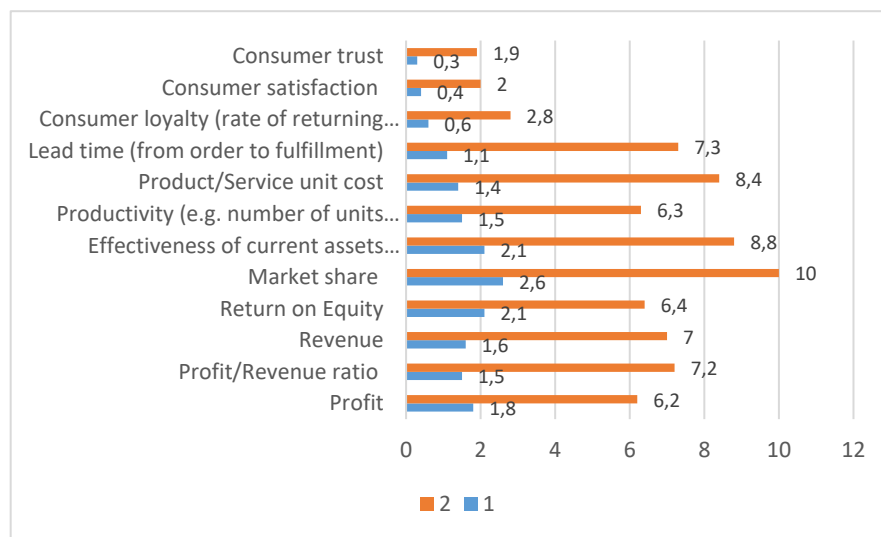


Figure 8
Percentage of those who perceive that their effectiveness has decreased
Source: own research

In terms of return on equity, 50.2% of enterprises perceive an improvement, 41.4% perceive neither an improvement nor a deterioration. 8.5% perceive deterioration.

In terms of market share, 39% perceive an improvement in SMEs, 48% see no difference compared to previous years. This category is much more difficult to define than profit or sales.

Regarding the efficiency of current asset management, the respondents consider that their money was tied up in current assets for a shorter period of time.

Regarding the production processes, I examined the evolution of three indicators: Productivity, product/service cost and order lead time. Entrepreneurs perceive an improvement in all three indicators. Business leaders (51.6%) perceive the greatest improvement in terms of productivity, 52.4% in terms of turnaround time, and 41% in terms of the cost of products and services.

I also measured the performance of businesses in relation to customers using three indicators: customer trust, satisfaction and loyalty. The majority of entrepreneurs

view these indicators very positively, however, it should be noted that we can only talk about real measurements in the case of SMEs in a very small proportion.

More than 73% of businesses, for example, notice an improvement in customer loyalty, of which 33% report a significant improvement. SMEs would perceive an even more significant improvement in terms of customer satisfaction, nearly 78% of them, and more than 79% of them in the case of customer trust, and even 41% of them a significant improvement.

3.3 Examining the relationship between performance and innovation activity

In the next step, I examined whether a relationship could be established between the planned timeframe for innovation implementation and SMEs' perception of their effectiveness. I hypothesised that firms that plan to innovate at a closer time horizon would be more likely to be perceived as more effective. In terms of effectiveness, I examined the 12 indicators mentioned earlier and their relationship with the planned timing of innovation. Significant relationships were found for all 12 indicators, with a weak but verifiable closeness. The results of the tests are summarised in Table 1.

Table 1 Relationship between the effectiveness indicators and the time frame of the planned implementation of the innovation

Metric	Cramer V	p
1. Profit	0,95	0,000
2. Profit/Revenue ratio	0,81	0,000
3. Revenue	0,108	0,000
4. Return on Equity	0,78	0,000
5. Market share	0,107	0,000
6. Effectiveness of current assets management (payback period of money tied up in current assets)	0,97	0,000
7. Productivity (e.g. number of units produced per unit of time)	0,97	0,000
8. Product/Service unit cost	0,78	0,000
9. Lead time (from order to fulfillment)	0,065	0,001
10. Consumer loyalty (rate of returning customers)	0,066	0,004
11. Consumer satisfaction	0,071	0,001
12. Consumer trust	0,062	0,012

Source: own research

3.4 Examining the relationship between the time horizon for the introduction of planned innovations and the demographic characteristics of firms

In my research, I hypothesised that certain demographic characteristics of firms have an impact on their propensity to innovate. For example, the geographical location or the area of activity of a business influences the intensity of innovation activation in family businesses.

Only in a few cases is there a link between the demographic characteristics of enterprises and the timing of planned innovation. Thus, a weak but highly significant relationship was found between the size of the enterprise and the time interval of the planned innovation ($CV=0.111$; $p=0.000$). In other words, the size of the enterprise may influence the time interval within which the enterprise plans to innovate. This may also be related to the capital strength of larger firms, for example, as a medium-sized firm is more likely to have the opportunity to innovate earlier than a micro or small firm.

I also looked at the relationship between the market of enterprises and the field of activity. Here, I have assumed that the sector of activity of the enterprise also influences the frequency with which enterprises undertake new development due to differences in the technological cycles of the industry. Unfortunately, I was unable to confirm this significantly on the basis of the research data.

Conclusions

My research has shown that the majority of family businesses recognise the need to innovate in their activities and that they are planning to innovate in the short to medium term. The majority of enterprises plan to finance the majority of their future development from their own resources, with a significant proportion of them being reluctant to borrow. A significant proportion would still rely on grants and subsidies.

My research has shown that there is a significant relationship between the performance of enterprises and their propensity to innovate. In other words, family businesses with a higher propensity to innovate were perceived as more successful than those with a lower propensity. Of course, we must take into account the limitations of the research, namely that the sample is not representative.

The link between demographic characteristics of family businesses and innovation propensity has been demonstrated in only a few cases. In other words, in the

majority of cases, the propensity to innovate is not significantly influenced, for example, by the geographical location of the enterprise or its field of activity.

I also examined the time to innovation in relation to the market situation. Here I basically assumed that firms in a more favourable market situation innovate more often. No significant relationship was found here either.

In conclusion, I consider that there is a need to further investigate and explore the innovation activities of family businesses in order to show that innovation has a positive impact on the performance of SMEs, and that it is important for family businesses to recognise the need to innovate in their operations, whether in the form of small improvements or novel solutions.

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