The Pivotal Role and Pervasive Influence of Business Groups in East Asia

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Abstract

The role, power and dominance that business families play in economic development in East Asia require thorough consideration. This paper seeks to explain the pivotal role family-owned East Asian business groups have in contributing to economic development in the region and their dominance of the private sector. By their size and scope the pervasive influence of business groups in the East Asian region can be interpreted to be detrimental to the development of more rigorous, objective ethical and governance standards, and weaken the independent institutions that will uphold and enforce these standards. This paper concludes that business groups will remain the dominant form of private sector organising in the region and suggests various avenues of further research in this area.

Keywords: East Asia, business groups, private sector, corporate governance, family business owners, economic development

Introduction

Concentration of ownership in the East Asian private sector is manifested in the corporate form known as the business group. Family-owned business groups, also known as family-owned conglomerates, dominate the private sector landscape of the region with exemplars being the Japanese pre-war *zaibatsus* (Miyajima and Kawamoto 2010), post-war *keiretsus* (Lincoln & Shimotani) Korean *chaebols* (Chung 2005) and Taiwanese *guanxigiye* (Amsden 2001: 236). Their size, scale and scope mean that, aside from government, they are the most influential and economically important institutions in these countries. Business groups are "collections of firms bound together in some formal and/or informal ways, characterised by an 'intermediate' level of binding…they are the outcome of investments by a single family or small number of allied families who, once having acquired the component companies, keep them together as a coherent group among which personnel and resources may be shifted as needed. Yet the individual companies continue to keep some separate identity." (Granovetter 2001: 69-70). In other words, they are "legally independent companies [that] utilise the collaborative arrangements to enhance their collective economic welfare."(Colpan & Hikino 2010: 17)

The paper poses the following question: Why does the family-owned business group form persist throughout the East Asian private sector?

In seeking to answer the above question, this paper is structured as follows. Firstly, a short history of prominent business groups in the region is examined and in some cases, how state-led development policies of the region and how they established and affected business groups are also summarised. As this is but a sliver of the plentiful state-development policy literature of the region, the paper seeks to limit the discussion to the interaction of the state with business groups. Secondly, the theoretical perspective of business groups is developed and to show how they differ from the Western organising of corporate governance. Thirdly, the structure of business groups is explained and why they dominate the region thus due to institutional environment weaknesses is explored. The structure of groups, especially for largely conglomerates, is largely helped by having their owned and controlled bank at the centre of the group. Then, the investment strategies of holding companies are analogous to the way an investment manager treat its fund portfolio. Tying all this together from the macro to the micro environment, the paper looks at the economic implications of the dominance of business groups in the region and also proposes future research in the area especially with the emergence of China's own business groups. Finally, the paper concludes by summarising why it is important for business groups need to be studied in order to understand the role they play in the region.

Origins of East Asian Business Groups

The origins of business groups in the region can be pinpointed to different catalysing events and upheavals in East Asian history such as colonialism, war, post-war colonialism and independence. Some business groups emerged from 19th century trading houses established by British, Dutch, Japanese and Spanish colonialists. In the 20th century, some business groups emerged in the wake of political destabilisation in 20th century China with the post-Chinese civil war and Chinese Cultural Revolution era catalysing the exodus of entrepreneurs throughout the region with the emergence of ethnic-Chinese owned business groups. Lastly, the rise of Japanese foreign investment (encouraged by its government) in the latter half of the 20th century under the 'flying geese' model (UNCTAD 1993) also favoured investment in by-now well-established family-owned business groups in the region as the Japanese *keiretsu* form attracted like with like. (Bello 1992; Hart-Landsberg & Burkett 1998)

The emergence of business groups in the following selected Asian countries is briefly mentioned:

Hong Kong

As a former British colony, some of today's Hong Kong business groups descended from the 19th century trading houses established by British colonialists to conduct trade with a weakened imperial China after the Opium War. Business groups that exist today from this period include the privately-owned Swire Group[1] while another (albeit listed) counterpart, the Keswick family-controlled Jardine Matheson Holdings[2] was the subject of a historical novel "Noble House" by James Clavell as a testament to the influence it wielded on the island. What catalysed these historically British groups' expansion was their consolidation of capital in Hong Kong after the emergence of the Communist Party in China as a political force with mainland interests divested or expropriated.

Similarly, British-ruled Hong Kong was perceived as a stable location and became one of the first places for the mainland Chinese entrepreneurial class to immigrate to in the wake of Japanese colonialism, World War Two and increasingly, the unknown force of Mao Zedong and his policies. Business groups originating from this period include Li Ka Shing's Cheung Kong Holdings[3]and Lee Shau-Kee's Henderson Land.[4] An important distinction that can be made between these British and Chinese business groups is the former have been a family business operation for several generations, while the latter groups are still controlled by their founder-owner entrepreneurs.

[1] Swire Group (2012) About Swire – Our Story http://www.swire.com/eng/about/story.htm accessed 14 June 2012

[2] Four members of the Keswick family currently sit on the board of directors of Jardines http://www.jardines.com/the-group/directors.html (accessed 14th June 2012)

[3] Cheung Kong Holdings (2012) Chairman's Profile http://www.ckh.com.hk/eng/about/about_chairman.htm accessed 14th June 2012

[4] Henderson Land (2012) About the Group http://www.hld.com/en/about/profile.shtml accessed 14th June 2012

Indonesia

The origins of today's Indonesian business groups were an outcome of the nationalisation of Dutch properties in the 1950s after the country's war of independence. President Soeharto's lengthy rule in the latter half of the 20th century allowed the consolidation and expansion of favoured and politically-connected groups.

One such group was the Salim Group which flourished under Soeharto's regime (Sato 1993). Salim Group is the country's biggest conglomerate with "interests in in agriculture, food, automobile manufacturing, building materials industry, chemical, banking and financial services, resorts and hotels, real estate and industrial parks, resources and international trade, distribution and retail, communications and media industry, charitable and public welfare."[5] It was founded by another ethnic Chinese Sudono Salim whose son Anthony now runs the group and navigates through the sometimes murky world of Indonesian politics.[6]According to Sato, the Salim Group is emblematic of favoured business groups under Soeharto's rule:

> "The 'pursuit of market domination' seen consistently throughout the development of the Salim Group can be understood as the manifestation of the group's own power: 'politically affiliated power' and 'conglomerate power'. These two hallmarks of Salim Group have been possible because of Soeharto's rise to power and because of the 'full-set' industrialisation strategy that has been promoted by Soeharto's government. In this era the Salim Group is a symbolic economic actor of Indonesia during the Soeharto era." (1993: 441)

Malaysia

The dismantling of the British colonial empire after World War saw immense structural socio-political changes occurring after the divestment of Malaya. Two new states were created from this former colony with the establishment of Malaysia and the creation of ethnically Chinese-dominant Singapore after the latter was politically ousted from the former. The winds of history also made an impression on the commercial actors in the region with one such group, the conglomerate Kuok Group, able to surf the tide of change.

The Kuok Group has its origins in the early 20th century when Kuok Keng Kang fled an economically depressed mainland China to seek his fortune in the British colony. During the Japanese occupation of Malaya, Kuok's son Robert became an apprentice at Mitsubishi. This exposure to a Japanese

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[5] Business Week (2012) Salim Group http://investing.businessweek.com/research/stocks/private/snapshot.asp?privcapId=9682271 accessed 23 April 2012

[6] Saragih, BBT (2012) Chinese tycoons join politics for survival, Jakarta Post, 24th January http://www.thejakartapost.com/news/2012/01/24/chinese-tycoons-join-politics-survival.html accessed 23 April 2012

diversified conglomerate allowed Robert Kuok to modernise the family business and when his father died in 1949, he inherited the leadership mantle of a group largely comprised of agricultural interests. (Heng 1999: 163) Kuok took advantage of the process of decolonisation in Malaya and diversified into trade, shipping, oil and made most of the retreat by British companies such as Tate and Lyle (Heng 1999: 162) in the sugar trade.

Kuok expanded in the region and formed ventures with other ethnically-Chinese business families in other industrial sectors such as media and property. (Heng 1999: 163)

Privatisation under the rule of Mahathir in the late 20th century led to the evolution of a conglomerate structure and strategy similar to the Japanese form:

> "…the typical conglomerate was inclined to adopt a familiar strategy: deal in property and real estate, build up construction capacity, lobby for infrastructural and utility works, secure a banking or finance arm or a brokerage licence, buy up plantations, diversify into tourism, and enter newly privatised areas like telecommunications and social services…In effect, they evolved into a privileged league of private oligopolies which benefited from the fragmentation of state monopolies." (Khoo 2000: 219)

Indeed, the close form of ties between a few Malaysian business families and the state have been characterised as either being rentierist, distributional-coalitionist or indeed, cronyist. (Khoo 2000: 222)

South Korea

The nexus of state-led industrial development policies and business group development could not be more exemplified by the experience of South Korea. From its very beginnings, chaebols were inextricably linked to its political masters. The government unequivocally played a pivotal role in their establishment, development and expansion. The chaebol form had its origins under Japanese colonialism and was heavily influenced by the keiretsu structure. When Japanese rule ended, the colonialists' properties were seized with "industrial interests sold far below the market value" (Kim 2004) to favoured participants. This formed the basis of the emergence of the chaebol. As Lim (2003) narrates:

> "In the post-war environment, the Rhee government sold "vested properties" of formerly Japanese-owned industrial properties taken over by the US military government and subsequently transferred to the new Korean government. The Rhee government set the conditions for the sale of these properties so as to preclude competitive bidding and to favour the interim plant managers as well as the politically well-connected....Certainly not everyone who was privileged to pick up an industrial property at a fire-sale price had the

> entrepreneurial talent to build a business empire. But vested properties provided the initial base for many of the largest chaebol."

Hence, the chaebol emerged out of favourable government policies which also included low interests rates from Korean banks. In a financial coup, in the 1950s, South Korean commercial banks were privatised and the recipients of this process explicitly favoured the chaebols. From Lim again:

> "Using political connections, top industrial capitalists borrowed money from the banks in order to make bids for the ownership of the same banks. When bank privatization was completed in 1957, all major commercial banks were under the control of the industrial capitalists."(2003:42)

By the 1970s, export-oriented government policies were in full-swing which allowed the chaebols to expand with the backing of state banks. This strategy allowed chaebols to internationalise while their financing was being underwritten by the government. However, the South Korean government did impose a measurement of "export performance" which allowed the policymakers to objectively assess whether the expansion of its stable of national champions overseas were successful.(see Lim 2003: 44)

The reciprocal benefit from the private sector in pursuing or aligning itself with the government policies of the day, Amsden notes, led to mutually beneficial progress and successful outcomes. The governments of the region disciplined capital as well as labour. Thus selective relationships and attachments with certain business groups allowed their progress to occur and their form to continue despite reaching a middle-class type of development.

However, this close nexus between politics and business did unravel and by the time of the 1997 East Asian crisis, the concentration of economic power and the management culture of dynastic dictatorship in the chaebols saw the "too big to fail" (Kim 2004: 12) nature of this private sector form of organising with immediate short-term severe effects for the rest of Korea's economy and society. Questions of legitimacy and financial sustainability hung over the partnership that had underpinned Korean's economy for the latter half of the 20th century: "…much of the '*chaebol* problem' encompassing both moral hazard and corporate governance issues, remained unsolved even as the economic crisis of 1997 approached." (Lim 2003: 49) For other countries and their business groups in the region, the troubles of the Korean chaebol instigated an inward-looking search for reform.

Thailand

Modern enterprise in this country can be traced to close interaction with Chinese entrepreneurs and Western trading houses in the mid-19th Century (Falkus 1989: 120). In the 20th century, these Western

(mostly British) properties were nationalised and under military rule, the nationalised enterprises formed alliances with ethnic Chinese-owned industrial interests.

In Pananond's 2004 resource-based view study of a Thai business group owned by the Chansiri Family, Thai Union Frozen Products (Asia's largest canned tuna exporter), the author writes, "large family business groups are likely to stay as a dominant form of firms in Thailand because the business group structure responds effectively to the institutional context of developing economies such as Thailand…[and they] can be best understood as an institutional innovation for internalising the returns that accrue from operations in the imperfect market conditions of less developed countries." Not surprisingly, the familial-based society of Thailand resonates in the business group as "it is an organisational form that has been shaped by the sociological patterns of relationships in that specific society." (2004: 73)

The realisation that these groups dominate a large part of the private sector means foreign investors in the region must interact and form relationships with these groups as they do form a formidable barrier to entry due to: "the information asymmetry between local and foreign firm benefits diversified business groups at the expense of foreign multinationals and domestic non-diversified firms (2004: 74)

Pananond further expounds, "the large and diversified business group does have a rationale for its development and continued existence, especially in Asia and Latin America where the institutional context is often characterised by market imperfections and familial ties and the business group structure is an appropriate organisational response to the environment in which it develops." (2004: 74)

Indeed, given the sometimes politically unstable environment of Thailand with military interventions occurring when the civil government fails to promote social harmony, it is notable the intersection of political-business ties under the prominent Shinawatra family who owns one of Thailand's largest conglomerates, Shin Corp through its holding company In Touch.[7] More notably it was founded by ethnic Chinese Thaksin Shinawatra who became Prime Minister of the country, was later deposed and whose sister Yingluck was later elected as Prime Minister in 2011.

China

China's communist party also became interested in forming business group structures in its 1997 plan albeit with ownership still linked to the party. This was done in large part to consolidate its various industries and partly propelled by nationalistic pride to have Chinese industrial giants enter the

[7] In Touch Company (2012) Corporate website http://www.intouchcompany.com/index_en.asp accessed 23 April 2012

Fortune 500. (Amsden 2001: 275). In 2011, 61 Chinese companies had reached the Global Fortune 500 although the ranking system favoured companies that specialised by industry and less by conglomerate structure.[8]

Theoretical Perspectives of Business Group Development

The post-Chinese civil war and Chinese cultural revolution era were catalysts that saw the emergence of ethnic-Chinese owned business groups especially in Taiwan, Thailand, Malaysia and Indonesia. Forming alliances with ethnic Chinese entrepreneurs became the trademark for much of the region's business groups as they expanded under institutionally weak post-colonial and post-war governments.

This form of picking national winners was hypothesised by Amsden (1995) under the principle of reciprocity. Amsden strongly argues the principle of reciprocity as explaining the basis of the region's industrial and economic development as opposed to its peers in South America during the same period. The government expected benefits from subsidies being given to selected "winners" or "supporters" of its industrial policy programs by tracking and ensuring performance standards were met.

The politically-connected, diversified business group was a success for an export-oriented industrial policy that fostered economic development and allowed some countries to lift their citizens out of poverty. However, the reliance on such opaque forms of private sector organising with unpredictable political ties (such as those that occurred under the crony capitalism regime of Indonesia and Philippines) provoked questions of viability and acceptance of whether this form of organising in the hands of a few, arguably, oligarchical families is best for long-term economic industrial development.

As the previous sections looked at the macro view of the business group largely through the lens of historical policies and institutional environment, this section seeks to explain the theoretical views behind their continued existence and endurance especially with regards to their governance structures.

The use of agency theory to explain the corporate governance of private sector companies is well-established.(Berle & Means 1993; Achilan & Demsetz 1972; Demsetz 1983; Fama & Jensen 1983; Jensen & Meckling 1976; Boyd & Hoskisson 2010) The application of agency theory is commonly represented in studies of corporate America and Anglophone countries where research primarily looks at the relationship between principal and agent – mainly the financial principals (such as shareholders with their representatives on the board of directors), and the managerial agents (that of executives and managers).(Mace 1971; Lorsch & MacIver 1989; Clarke 2004) The challenges in agency theory's applicability have become more obvious with its widespread use in the last quarter of a century to

[8] CNN Fortune (2011) Global 500 By Location: China http://money.cnn.com/magazines/fortune/global500/2011/countries/China.html accessed 23 April 2012

explain control – or lack thereof – and costs in principal-agent relationships. Given major American listed corporations have widely-dispersed ownership and generally do not have a dominant owner-manager, this ownership composition does not hold in other parts of the world especially in Asia. In countries where family-owned and family-managed corporations dominate, the premise of agency theory disappears as there is unity in strategic decisions: "Clan control implies goal congruence between people, and therefore the reduced need to monitor behaviour or outcomes."(Eisenhardt 1989:64)

Nevertheless studies of corporate governance have expanded internationally, consequently broadening the theory's scope and audience. Despite the anomaly of agency theory's application, there is persistence in its use in studies where ownership and control is one and the same (see Schulze et al 2001). Tsai et al applied an agency theory perspective to the CEO tenure of two different groups of Taiwanese firms: one family-owned, the other non-family-owned and found that family control serves as the crucial monitoring factor that is generally absent in widely-dispersed ownership corporate forms (2006: 26). Dharwadkar et al looked at the failure of privatisation in emerging economies from an agency theory perspective. The weak corporate governance structures within companies and lack of recognition of property rights in the external environment of most emerging economies resulted with an agency problem unique to developing economies - that of expropriation due to "the weak governance context when large or majority owners assume control of the firm and deprive minority owners the right to appropriate returns on their investments."(2000: 660) Young et al (2008) supported the principal-principal problem of owner vs. owner value expropriation to differentiate this from the traditional Western agency problem of owner vs. agent. Agency theory remains a powerful and influential theory to study corporate governance. However it is problematic to apply this theory in countries where firms have high ownership concentration and how it explains the phenomenon of business groups.

The East Asian model is characterised by family control and high ownership concentration.(Claessens et al 2000) Control and ownership is not separated. Most large firms are family-owned, and are usually not listed or partially listed on the stock exchange. Stock exchanges are relatively new and underdeveloped. Control is through pyramid structures and cross-holdings. There is a long-term focus on wealth-building. In comparison to other models, firm and financial information is less publicly available. A small number of families control the economy and government officials directly participate in the control of the sector, suggesting the existence of crony capitalism. Countries belonging to this model include Hong Kong, Indonesia, Malaysia, Singapore, South Korea and Thailand. The Philippines definitively falls under this model.

Other theoretical perspectives provide a more compelling reason why business groups should exist, evolve and are the common form of private sector organising in the region. Explaining business group

development is a source of rigorous debate. A variety of theories proffer different perspectives to their enduring existence. Millar et al (2005) posit the relationship-based nature of corporate governance in the region in the absence of institutional transparency, while Khanna and Yafeh propose a triangular perspective on business group development: the structure of the group depends on the extent of horizontal diversification, vertical integration and financial involvement; the control depends on family involvement and degree of pyramidal ownership; and the relationship of the business group with the state.(2010: 578) On a more macroeconomic vein, Chung looked at different theories such as institutional failure, transaction cost, resource-based and social capital to provide perspectives on business group development in Japan and Korea (Chung 2005) while Young et al (2008) supplemented this with their principal-principal agency perspective. The following table summarises their theoretical perspectives:

<insert Table 1 here>

For the most part, except for agency theory, the theoretical perspectives on business group development show how important the external, political environment is in determining business group development as the establishment of business groups in the wake of historical crises expounded earlier in this paper explained. Indeed, "[t]he nature of institutional country effects in which business groups are embedded…shapes the governance of business groups and their member firms."(Boyd & Hoskisson 2010: 691) They "internalise functions for which no external market or supporting institution exists."(Colpan et al 2010: 7) Another perspective of Table 1 is shown in the following figure that shows the concentration of ownership of business groups in the following Asian countries has an inverse relationship with the level of institutional and regulatory development in these states.[9]

<insert Figure 1 here>

The more concentrated the ownership - and indeed the wealth - the less progress there is in institutional reforms in the areas of judicial efficiency, the rule of law and absence of corruption. The top 15 family-owned business groups in the more developed countries of the region such as Hong Kong, Japan and South Korea control less than half of the total value of listed corporate assets as opposed to their counterparts in the less developed countries. Higher business group concentration is a strong indication of the instability of the political and institutional environment for the size of business groups allows them to withstand the vagaries of uncertainty. This has strong implications for studies of other business groups around the world especially for family-owned business groups in the erstwhile politically turbulent Latin America and Middle East regions. Strong public sector institutions allow the private sector to do what they do best: allocate goods and services efficiently.

[9] p.28 in Claessens, S. (2003) Corporate Governance and Development http://www.ifc.org/ifcext/cgf.nsf/AttachmentsByTitle/Focus_1_CG_and_Development/$FILE/Focus_1_Corp_Governance_and_Development.pdf accessed 20 June 2011

Weak public sector institutions distort the groups' ability and capacity, with rent-seeking, revenue collection avoidance[10] and political influencing flourishing as a way to protect their family owners' interest.

The institutional perspective sees business groups as filling in the voids due to inefficiencies in a country's capital, labour and product markets. The market failure perspective supports this notion of business groups as filling in the institutional voids. The lack of trust in the political environment means the ability to transact commercially and with confidence with well-connected and well-established (albeit complex) entities supports to overcome this impediment. As a result, the market failure theory endorses the transaction costs theory which states business groups are more economically efficient in such a prevailing environment. In addition, the resource-based and social capital theory of business groups lends support to the efficiency and value creation argument.

Underpinning the principal-principal agency perspective is the realisation that the institutional framework is grossly underdeveloped, corrupted, lacking and non-existent in some countries. There exists little trust in the public or regulatory arms of the state as regulators remain vulnerable to politicisation and face undue influence or corruption by certain interests. However, at the same time this reinforces the perception that corporate governance in the business groups and their boards are heavily influenced by the owning and controlling shareholders and remain mere "rubber stamps" of the dominant owner/s. (Young et al 2008)

Therefore, the agency problems present in Anglo-American countries rarely exist in Asian companies. It is also worth noting, in studies of business groups in developing economies, their relationship with the state is fundamental. It is this relationship that determines why the other non-agency theories provide a more useful explanation of this phenomenon. In most Asian countries, the relationship business groups have with the state determines and influences the manner by which these companies operate.

Carney supports this notion by proposing four hypotheses of business group development in Asian business groups: institutional voids, life cycle, state-led industrialisation, and crony capitalism (Carney 2008: 602). Of the four, two are most pertinent in a developing country situation such as in Indonesia and the Philippines: that business groups fill the institutional void (Carney 2008: 598) with the provision of infrastructure which is normally the realm of the state, and the proliferation of crony

[10] The fall in revenue collection is indicative of a loss in trust and confidence in the government executive and/or public sector as related in the following situation in Central America:
"Álvaro Uribe, Colombia's stern former president, who made his country safer and also implemented a similar transfer programme, has become the hottest conference speaker in Central America. Businessmen in Guatemala last October loudly applauded his message about security; but when he exhorted them to pay their taxes, he was met with silence. Even in Costa Rica, "Tax evasion is the national sport," says Ofelia Taitelbaum, the ombudsman." http://www.economist.com/node/18558254?story_id=18558254 accessed 28 April 2011

capitalism in the post-dictatorship era which has allowed the endurance of some business groups. The state played a dysfunctional role in these countries (Granovetter 2001: 97). Yet dysfunctional business-state relationships are far from unidirectional as business groups with enough extraterritorial might and political connections can play a pivotal role in overthrowing the elected government of the day as in the case of the Chile's Allende government (Zeitlin et al 1974) and some Philippine business groups actively supported the removal of Marcos in the dying days of his dictatorship.

For other countries in the region namely Taiwan, South Korea and Japan, they were beneficiaries of state-led industrialisation as their governments were actively interventionistd (Fligstein 1996). The relationship between the private sector in those countries and their governments were mutually beneficial (Zhang 2005), united by a common goal towards greater economic development and providing this distinct form of Asian capitalism (Granovetter 2001: 71-73; Whitley 1994). Finally, Carney's hypothesis of business groups as part of the life cycle proposed business group formation and affiliation by entrepreneurs was important in developing countries, but they could also "frustrate continued economic development by inhibiting the entry of new firms into the economy." (Carney 2008: 603)

The Dominance of Business Groups and their Structure

Ownership concentration is a manifestation of economic control[11]. In the ground-breaking study by Claessens, Djankov and Lang (2000) of 2,980 East Asian listed corporations, they found more than two-thirds of firms are controlled by a single shareholder. The table below shows the percentage of concentrated ownership across the region ranging from Japan where only the top 15 families control 2.1% of that country's GDP to Hong Kong where the top 15 families control over four-fifths of that island state's wealth:

<insert Table 2 here>

There is little evidence of any significant changes in the concentration of ownership amongst the leading families in East Asian countries in the last decade even after the 1997 East Asian Crisis and 2008 credit crisis. The 1997 East Asian Crisis and the collapses of Enron and WorldCom heightened the awareness that poorly run and weakly managed business groups in the region need to institute robust controls that promote transparent and accountable decision-making.(Faure 2002; Reed 2002; Trivellato 2002) dHowever, while political discourse improved due to the contagion effect of the crisisd (Derichs & Heberer 2002),apart from notable internal improvements of some Korean chaebols both financial crises - reiteratively - did not lead to fundamental, structural reform of the ownership concentration of Asian business groups

[11] For different classifications of control of a company, see Berle and Means 1933 and Sales, A. (1979) La Bourgeoisie Industrielle au Quebec, Quebec: Les Presses de L'Universite de Montreal

It was also notable that during the crisis of 2008-09, Asian family-owned business groups confidently managed to weather the storm. Indeed, these groups proved resilient in the aftermath of both crises with some opportunistic business groups consolidating their interests in the insurance sector after the bailout of American Insurance Group (AIG) and its divestment of extensive Asian interests in 2009. The owners of these Asian business groups remain solidly family-based.

According to the previously mentioned 2002 World Development Report, there is a link between high concentrated corporate ownership and the efficacy of legal protection in countries. That is, "concentrated ownership tends to substitute for weak legal protections" (2001: 58). This view complements and supports resource dependence theory and the resource based view of the firm in developing countries: where there is an unstable political environment, the conglomerate form is the preferred method of organising. Investors in weak institutional environments also play a premium on firms who are part of conglomerates due to the perception that "concentrated ownership delivers great benefits when those owners in control have appropriate incentives and when owners outside the firm have more leverage."[12] This was supported by a McKinsey study that showed an average premium of 24% an investor would pay for a well-governed company in the Asia region.[13]

However, the dominance of family-owned business groups means their treatment of minority shareholders can be less than satisfactory and is a pressing corporate governance issue in countries with concentrated ownership. Even where the prevalence of business groups is a private response to weak government institutions, the concentration of wealth in a few people, families or groups is a "formidable barrier to policy reform" and could negatively affect "the evolution of the legal and other institutional frameworks for corporate governance and the manner in which economic activity is conducted."(Claessens et al 2000: 110) Business groups are a form of organising that try to mitigate uncertainty especially where the country has a dominant public sector and government executive. By being part of a business group, transaction costs between affiliated companies are lower and being part of a group may help overcome market failure problems, allows the transfer of managerial talent across businesses, and share other resources between affiliated companies (Kim et al 2004). The might of business groups and conglomerate power also allows competitive advantage over single firms. As business groups dominate industries, being affiliated with a business group allows a company access to the network and resources available within that group. Being part of a business group builds up and consolidates the social capital amongst members.

In terms of structure, business groups in the region that are vertically integrated reflect a great degree of control by owners and Leff saw their structure as substitutes for the imperfections in the capital

[12] World Bank 2001: 58
[13] McKinsey (2002) Global Investor Opinion Survey: Key Findings http://www.mckinsey.com/clientservice/organisationleadership/service/corpgovernance/pdf/globalinvestoropinionsurvey2002.pdf accessed 11th June 2010

market.(1978: 661-675). While business groups may be the most *efficient* form in an *inefficient* market, because of their size, domestic business groups have an almost unassailable advantage over new entrants with foreign ownership restrictions in developing economies – in most cases - unilaterally favouring domestic participants. Below is a figure showing the structure of two Filipino business groups with their listed and unlisted companies across different industrial sectors:

<insert Figure 2 here>

In the Philippines, listed business groups tend to be in the mature phase of their life cycle. They privately build up their businesses before utilising the capital market to unlock the market value of their assets. Business groups list one business after another and not at the same time. Therefore, a business group's portfolio has assets that are listed and others that remain private. In the above figure, the Ayala Group has 5 listed and 4 unlisted companies, while the SM Group has 6 listed and 4 unlisted companies. Both Ayala and SM groups are family owned by the Zobel de Ayala and the Sy Families respectively. As Guillen points out, in sectors where foreign investment is restricted, domestic business groups that have proliferated under such protectionist policies will be reluctant to lose this 'asymmetrical' position. Foreign entrants have little choice but to collaborate with them, thus ensuring the continuation of the status quo of the dominance and entrenchment of business groups. (Guillen 2000: 376)

The strong ambivalence towards the economic power and domination of a few select economic groups have been articulated by Kang et al (1991)'s book on chaebols, which posed the question on whether they were "the locomotive of growth or the personification of avarice" (Lim in Haggard 2003: 50, endnote 1) in South Korea, and more provocatively and recently and by Khanna & Yafeh in their 2007 article entitled *"Business groups: paragons or parasites."*

Perhaps this is a crude dichotomy, but it does highlight the difficult behaviour patterns at opposite ends of the ethical and governance spectrum in Asian business groups. Khanna and Yafeh conclude that both types of business groups exist: business group paragons are the ones who have a good reputation premium and are well known to practice good corporate governance (Carney 2008: 597) while the parasitic business groups rarely observe corporate governance standards and depend largely on the largesse of their political connections (Faccio 2006) and superior contacts to sustain the viability of their companies (Fisman & Khanna 2004: 621). This parasitic view of business groups provide support for Carney's hypothesis that some business groups emerged due to the reciprocal nature of crony capitalism. The common principal-agent problem common in Anglo-American countries are not present in the Asia as most owners are themselves part of management. In most cases, the control of business groups has not been decoupled from the owners. Unlike their widely-owned and -held non-family and listed Anglo-American counterparts, out of control managerial

remuneration is less of an issue and a long-term outlook on the group of companies allows a lengthier strategic planning, albeit conservative, process.

The Central Role of Business Group-Owned Banks and Investment Strategies

A core aspect of a business group's structure is its bank-based model of financing. Having a bank at the centre of a business group allows a highly controlled form of financing to mitigate the effects of inefficient capital markets and high transaction costs. The bank-based model of financing is not new. Lamoreaux's study of 19th century New England documented banks of kinship groups were at the core of financing affiliated firms as this provided stability, strength and long-term investment horizons.(1986: 659, 666) Sales' study in Quebec also found that the intense concentration of banking and industrial capital allowed investment in developing large projects. (1979: 296)

The parallels between business groups in developing economies and the then developing economy of the north-eastern part of the American continent extends to issues of business risks and longer-term perspective on strategy (Lamoreaux 1986:653). Nevertheless, business groups will remain the dominant form of organising in the region. Reforms in the private sector will need to take their dominance into account as they "will continue to be important vehicles for the sustained future growth of this region." (Chang 2003: 414)

Once business groups sort out the best form of financing for their web of businesses, where and how to invest the capital they receive is a strategic challenge. The best way to conceptualise the investment strategy of a business group is akin to an investor who has different assets in different sectors but the assets are major vertically-integrated businesses or companies across a variety of industries. Depending on the level and appetite for risk - as in any investment portfolio - a wide variety of assets are present across different industries. For large business groups in Asia, they behave like a diversified investment portfolio with the holding company acting like the fund manager and the bank at the core. Similarly with a business group, several companies that it owns may be classified as the aggressive/high growth entity, the conservative asset or the diversified business. The following figure is the owning family/holding company perspective of the business group. The figure shows the business group as an investment portfolio with different businesses classified according to the level of risk appetite and growth strategy:

<insert Figure 3 here>

For professional managers working in these companies they must have a sense of awareness of the investment strategy of the owning family/holding company so their sense of purpose in the business is tempered by this knowledge. A well-diversified portfolio spreads the assets and the risks and business groups generally take such an approach with companies under their umbrella.

The Economic Implications of Business Group Dominance

The implications for the dominance of business groups and the political economy perspective behind their ownership complexity are considerable. A volatile political environment influences business groups to organise in a form that can operate in a perceived absence of institutional order and an economic environment with endemic corruption. As business group theories in Table 2 mention, the volatility of the political environment ensures that this form of organising is the best way to do business in an uncertain political environment, and more essentially against the bulwark of a predatory state.

According to Dyer and Mortensen:

> "Hostile environments create a situation where individual entrepreneurs face significant moral dilemmas. They can either comply with the law, thus forfeiting the success of their businesses and their own economic well-being, or they can attempt to work within the context of a corrupt system in order to survive. Most choose survival." (2005: 253)

This was the case for Philippine and Indonesian business groups under the Marcos and Soeharto dictatorships respectively. How to manage the political risk in a predatory, crony capitalist state required major manoeuvrings that blurred the line between business and politics. Galang (2011) provides a useful insight into the different ways the private sector responds to corruption in its business environment with strategic activities to mitigate its debilitating impact. For one Filipino business group, mitigating this political risk included having a major foreign investor in its companies as it would be to Marcos' detriment to seriously offend another foreign government if he decided to expropriate the assets of a foreigner whose political masters were bigger and mightier - economically, politically and militarily - than an archipelago on the western coast of the Pacific.

Managing political risk in this way has been applied before in corporate history with varying degrees of success. In Mitterrand France, the presidential decree of nationalising strategic sectors and companies was met with fear, loathing and futile acceptance. Making overtures to a foreign investor to mitigate government expropriation is not an uncommon business strategy. Indeed one French bank invited the "U.S. Treasury to threaten France with retaliation if the takeover went through. The Treasury refused."[14][15] Unintended consequences arise when the lines between political and business risks intersect.

[14] Byron, C. (1981). France's Private Banks Go Public, Time Magazine, September 28 http://www.time.com/time/printout/0,8816,953148,00.html

[15] This 1980s strategy had ramifications for another business twenty years on. For the French cosmetics company L'Oreal - in anticipation of the Mitterrand regime - invited the Swiss multinational Nestlè to take an ownership stake in the company in 1974. This fear proved to be unfounded as Mitterrand did not seize the

As Schneider points out, the degree of political intimacy a business group has with the government of the day can readily determine its ability to strategise and operate in the future (2010: 662). Indeed, the complexity of family business group ownership complements the opacity of political strategies to rein in the financial strength of the former, or to bring the oligarchic private sector under the rule of the state. However, the strength of business affiliated business group transactions can also be the source of its weakness. In an era that emphasises transparency, the related party transactions of business groups must ensure it can withstand such scrutiny. Financial markets readily punish business groups which have less than transparent business arrangements as owners of India's Satyam Group[16] and the aforementioned Parmalat Group discovered. Kim argued that Korea's chaebols are a reflection of its domestic market being weak with insufficient competition (2004: 31).

For politically well-connected groups such as Indonesia's Salim Group and the Philippines' Lucio Tan Group of Companies, both have survived their respective country's transition – albeit weak transition - to democracies. Indeed, the introduction of corporate governance reforms to these family business groups has proven to be a conundrum. The professionalisation of these business groups has meant the improvement in their standards of behaviour and codes of conduct. Professionalised business groups operate ensure family members who are appointed as potential successors to the family business undertake their education in Western business schools. However, their expectation and standards of behaviour from the state are not similarly reflected in their public sector regulatory counterparts.

More specifically, the family-owned business groups are affected by doubts and conflicts that are present in other family-owned businesses and business families. Interfamily disputes are common and succession is the Achilles heel of any successful family-owned business group. For the owners of Samsung, the Lee family's disputes were unmasked with filial conflict[17] echoing the Ambani brothers and their inheritance of Reliance Industries.[18]

Finally, what does the business group structure in the region mean for our understanding of China's economic development? While the strong arm of the state under the Communist party is still ever

company nor viewed the fashion sector as strategic enough. See The Economist (2009) In pursuit of beauty, January 22nd http://www.economist.com/businessfinance/PrinterFriendly.cfm?story_id=12995773

[16] Leahy, J. (2009) $1Bn fraud at India IT Group, Financial Times, http://www.ft.com/cms/s/0/32ea8364-dc85-11dd-a2a9-000077b07658.html

[17] AFP (2012) Brother sues Samsung boss – for $580M, Sydney Morning Herald, 15 February http://www.smh.com.au/technology/technology-news/brother-sues-samsung-boss---for-580-million-20120215-1t4pr.html accessed 15 February 2012

[18] Sharma R. & Bhattacharya, P. (2009) Ambanis exchange accusations as Reliance rift grows, Wall Street Journal, 9th August http://online.wsj.com/article/SB124966875030315041.html accessed 23 April 2012

present with its purges and censorship, the “princelings”[19] or children of revolutionaries have been adept in exercising their privileged position and are acutely transforming and evolving the structure of state-owned and state-run businesses to the domain of family business ownership. In particular, one princeling-general[20], Ren Zhengfei, has managed to transform Huawei into a global telecommunications enterprise with inauspicious undertones,[21] yet its structure of having insiders on the board, its perception as a ‘national champion” and government-backed financing makes it not too dissimilar from the growth of other business groups in the region.

It remains to be seen to what extent the party’s leadership will allow the transformation of state enterprises to well-connected family-owned enterprises like the rest of the region as this is the first generation of founder-entrepreneurs. The business interests of these princeling families are interconnected with the economic development of China. How they are run and governed will set the tone and value of Chinese enterprises as they expand in the future. Professionalisation will be a challenge and like other family-owned business groups, succession issues will prevail. Whether the concentration of power and capital in a select group of oligarchical groups are healthy for the state is something future research can look at and it will be in the succeeding generations that we will able to see more clarity

Understanding the weaknesses and strengths of business families rely closely on business relationships, their interactions and culture provide a window into how the region economically develops and how ruling families will still rule the private sector of the region in the foreseeable future. The business groups of region may not be taking the path of Chandlerian development where family-based capitalism transforms into managerial capitalism. Indeed the maturation of Asian’s family-owned business group to generational ownership has more in common with European family-owned business groups than American conglomerates with widely dispersed ownership.

A strong private sector requires a strong public sector so that the latter has the capacity to regulate and resources to apply laws. A regulator that is not politicised and that can make robust independent decisions will give more confidence to the majority of private sector participants. This, perhaps, is one of the major differences between business groups that operate in developing countries, and companies operating in developed countries: the robust, regulatory state.

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[19] Editorial (2012) China: Fall of a princeling, The Guardian, 12th April http://www.guardian.co.uk/commentisfree/2012/apr/12/china-fall-of-princeling?newsfeed=true accessed 23 April 2012

[20] Bo Zhiyue (2006) Princeling-Generals in China: Breaking the Two Career Barriers, Issues and Studies, 42 (1): 195-232; Huawei (2012) Corporate Governance Report http://www.huawei.com/en/about-huawei/corporate-info/annual-report/annual-report-2010/corporate-governance-report/index.htm acccessed 23 April 2012

[21] Hartcher, P. (2012) Why ASIO won’t get online with Huawei, Sydney Morning Herald, 10th April http://www.smh.com.au/opinion/politics/why-asio-wont-get-online-with-huawei-20120409-1wl2y.html acccessed 23 April 2012

This conundrum was pointed out by the Ayala business group CEO and how the weak public sector in his country is proving to be a challenge to operate in an ethical business manner:

> "We have long decided to meet what we believe are global ethical and governance standards so that we can succeed in a world where those standards are set. But in emerging markets, where institutional foundations need strengthening, those ethical standards can, ironically, be a competitive disadvantage. Others can take advantage of the system's malleability, if only in the short term…As a group, we try to keep business and politics separate, which is not particularly easy to do in a country like the Philippines."[22]

The precepts of transparency and accountability have no force if government regulators fail to ensure all companies disclose the required information. But as the above statement shows, where there is an imperfect market, exacting information is unreliable and hard to verify. This resonates with the market failure theory and institutional theory of business group formation. A business group can never be a replacement for a strong state. They are an adequate stop-gap during a long period of transition. However, business groups represent the private sector and there are profound limitations on how effective these entities can operate. Business groups are not an adequate replacement for civil society organisations though they may contribute to civil society's functioning. They are not a replacement for government because their goals are different and their motivations are largely based on that of their family owners.

Business groups can effectively contribute to their country's economic development if there is public sector leadership that will promote less unsavoury ethical behaviour. Reciprocally, undermining the institutions of the state for short-term private gain leads to long-term weaknesses and instability and the market power of business groups should not be an excuse for weakening the imprimatur of a democratic state and its promotion to create a less oligarchical society.

Conclusions

This article examined the development of business groups under the state-led industrial development policies of countries in the region, theoretical underpinnings of Asian business groups, their dominance and how they operate in the region. It also looked at the highly concentrated ownership of these groups and the complex ownership structure of their companies. The importance of banks in the financing of investments remains critical in countries with weak regulatory institutions and underdeveloped capital markets. The private sector of the region is highly concentrated in its ownership and control and is reflective of an oligarchic private sector. Business groups dominate the economic life of their countries as they provide strong institutions in an otherwise poor institutional

[22] Gibson, K. (2002) A case for the family-owned conglomerate, McKinsey Quarterly http://mkqpreview2.qdweb.net/Governance/Leadership/A_case_for_the_family-owned_conglomerate_1238

and regulatory environment due, in some cases, to the perception of a weak state. However, the pervasive influence of business groups is often associated with an ambivalence which can undermine the development of more rigorous, objective ethical and governance standards, and the independent institutions that will uphold and enforce these standards. By their size and scope they also influence the political life of the country but equally, their strategies and structure are also influenced by current political trends. Business groups will remain the dominant form of private sector organising in the region; explaining their behaviour will provide better understanding for their enduring existence.

Tables and Figures

Table 1: Theoretical Perspectives on Business Group Development

Agency Theory	This looks at the organisational microcosm of interacting relationships within an organisation. Primarily, this looks at the relationship between the principals (the financial ones such as shareholders) and agents (executives and managers). This is the most prominent theory used in corporate governance despite its flaws.
Institutional theory	Institutional theory asserts that highly diversified business groups (BG) create value by compensating for a nation's inefficient capital, labour, and product markets
Market failure theory	Market failure theory, concurring with institutional theory, argues that external markets can fail due to inefficient market mechanisms, legal impediments, and lack of trust
Transaction cost theory	Transaction cost theory argues that internal business transactions lower transaction costs because they avoid costs associated with contracts, negotiations, and contract enforcements.
Resource based theory	Resource-based theory asserts that BG-affiliated companies have opportunities to acquire and accumulate valuable resources, such as industry entry skills, trained employees, managerial skills, export-related skills, and others, giving them resource advantage over non-affiliated companies .
Social capital theory	Social capital theory proposes that intra-firm networks such as BG companies are social capital that can facilitate value creation.
Principal-Principal Agency Theory	Principal-principal agency theory argues that because BGs are owned and managed by founder families, agency problems are minimised between professional managers and shareholders. The institutional environment is underdeveloped and the framework close to non-existent. Boards are rubber stamps of the owner.

Table 2: Concentration of Family Control in East Asian Corporations (Claessens et al 2000: 108)

Country	**Average No. of Firms per Family**	**% of total value of listed corporate assets that families control (1996)**				**% of GDP**
		Top 1 family	**Top 5 families**	**Top 10 families**	**Top 15 families**	**Top 15 families**
Hong Kong	2.36	6.5	26.2	32.1	34.4	84.2
Indonesia	4.09	16.6	40.7	57.7	61.7	21.5
Japan	1.04	0.5	1.8	2.4	2.8	2.1
Malaysia	1.97	7.4	17.3	24.8	28.3	76.2
Philippines	2.68	17.1	42.8	52.5	55.1	46.7
Singapore	1.26	6.4	19.5	26.6	29.9	48.3
South Korea	2.07	11.4	29.7	36.8	38.4	12.9
Taiwan	1.17	4.0	14.5	18.4	20.1	17.0
Thailand	1.68	9.4	32.2	46.2	53.3	39.3

Figure 1: Relationship between Institutional Reform and Ownership Concentration (Claessens 2003: 28)

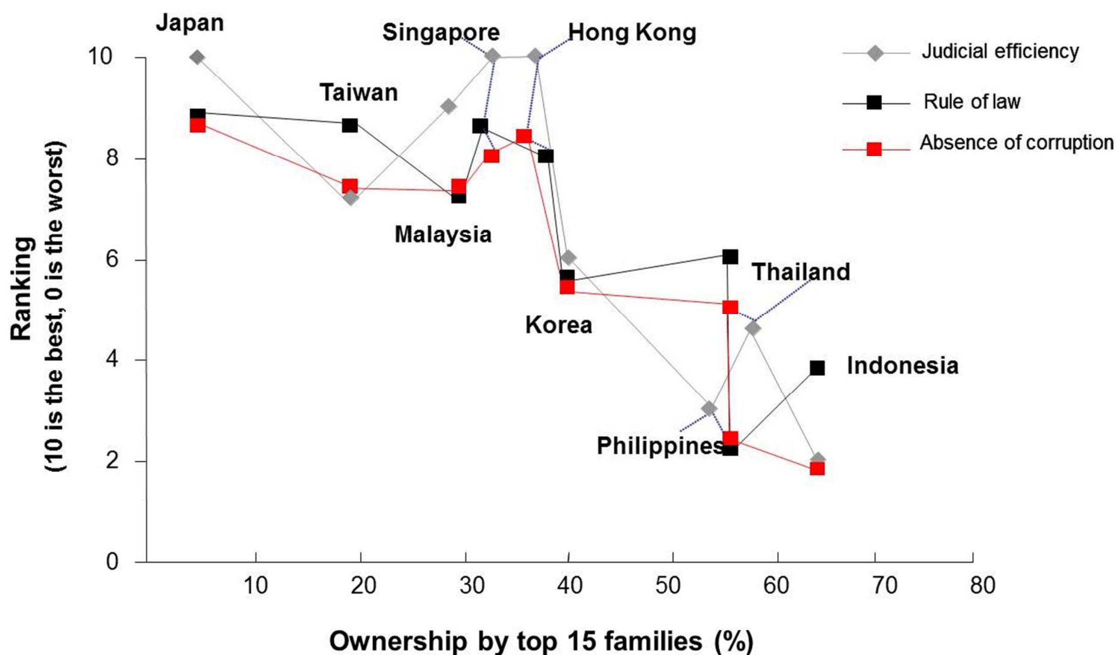


Figure 2: Listed and Unlisted Subsidiaries of Two Filipino Business Groups in 2007

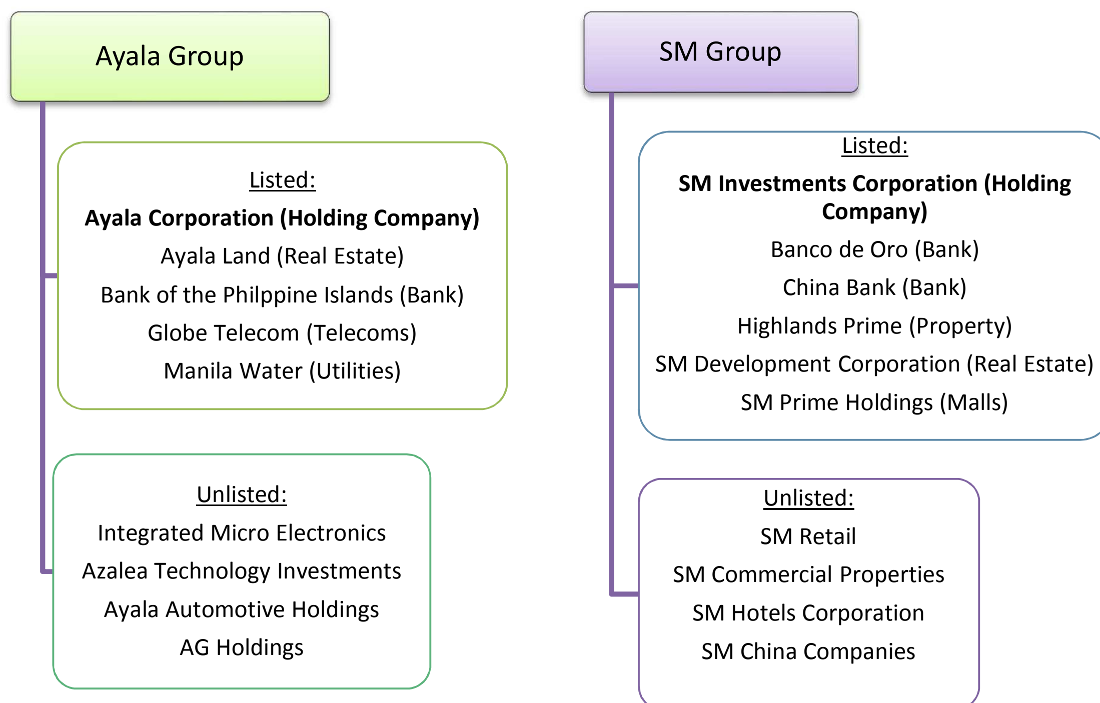
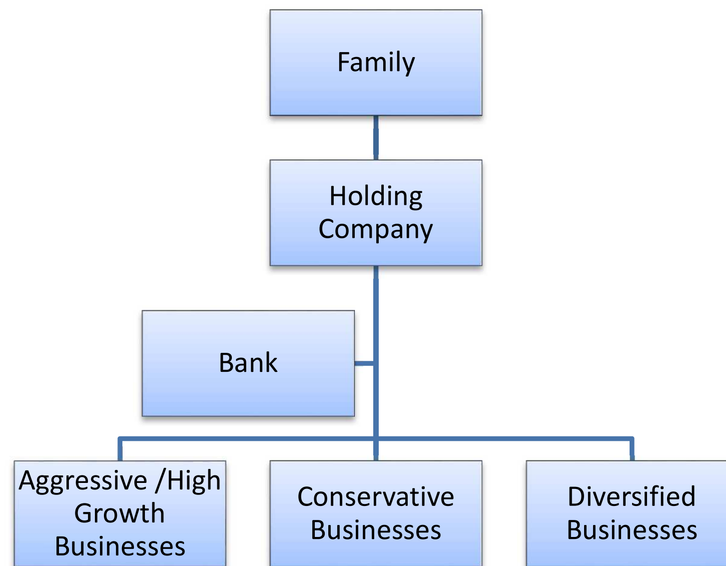


Figure 3: Business Group as an Investment Portfolio



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The Pivotal Role and Pervasive Influence of Business Groups in East Asia

Abstract

The role, power and dominance that business families play in economic development in East Asia require thorough consideration. This paper seeks to explain the pivotal role family-owned East Asian business groups have in contributing to economic development in the region and their dominance of the private sector. By their size and scope the pervasive influence of business groups in the East Asian region can be interpreted to be detrimental to the development of more rigorous, objective ethical and governance standards, and weaken the independent institutions that will uphold and enforce these standards. This paper concludes that business groups will remain the authoritative form of private sector organising in the region and suggests various avenues of further research in this area raised by the issues emerging from their sheer dominance.

Keywords: East Asia, business groups, private sector, corporate governance, family business owners, economic development

Introduction

Concentration of ownership in the East Asian private sector is manifested in the corporate form known as the business group. Family-owned business groups, also known as family-owned conglomerates, dominate the private sector landscape of the region with exemplars being the Japanese pre-war *zaibatsus* (Miyajima and Kawamoto 2010), post-war *keiretsus* (Lincoln & Shimotani) Korean *chaebols* (Chung 2005) and Taiwanese *guanxigiye* (Amsden 2001: 236). Their size, scale and scope mean that, aside from government, they are the most influential and economically important institutions in these countries. Business groups are "collections of firms bound together in some formal and/or informal ways, characterised by an 'intermediate' level of binding…they are the outcome of investments by a single family or small number of allied families who, once having acquired the component companies, keep them together as a coherent group among which personnel and resources may be shifted as needed. Yet the individual companies continue to keep some separate identity." (Granovetter 2001: 69-70). In other words, they are "legally independent companies [that] utilise the collaborative arrangements to enhance their collective economic welfare."(Colpan & Hikino 2010: 17)

The paper poses the following question: Why does the family-owned business group form persist throughout the East Asian private sector?

In seeking to answer the above question, this paper is structured as follows. Firstly, a short history of prominent business groups in the region is examined and in some cases, how state-led development policies of the region and how they established and affected business groups are also summarised. As this is but a sliver of the plentiful state-development policy literature of the region, the paper seeks to limit the discussion to the interaction of the state with business groups and provide it in its historical context of the region. Secondly, the theoretical perspective of business groups is developed and to show how they differ from the Western organising of corporate governance. Thirdly, the structure of business groups is explained and why they dominate the region thus due to institutional environment weaknesses is explored. The structure of groups, especially for largely conglomerates, is largely helped by having their owned and controlled bank at the centre of the group. Tying all this together from the macro to the micro environment, the paper looks at the economic implications of the dominance of business groups in the region and also proposes future research in the area especially with the emergence of China's own business groups. Finally, the paper concludes by summarising why it is important for business groups need to be studied in order to understand the role they play in the region.

Origins of East Asian Business Groups

The origins of business groups in the region can be pinpointed to different catalysing events and upheavals in East Asian history such as colonialism, war, post-war colonialism and independence. Some business groups emerged from 19th century trading houses established by British, Dutch, Japanese and Spanish colonialists. In the 20th century, some business groups emerged in the wake of political destabilisation in 20th century China with the post-Chinese civil war and Chinese Cultural Revolution era catalysing the exodus of entrepreneurs throughout the region with the emergence of ethnic-Chinese owned business groups. Lastly, the rise of Japanese foreign investment (encouraged by its government) in the latter half of the 20th century under the 'flying geese' model (UNCTAD 1993) also favoured investment in by-now well-established family-owned business groups in the region as the Japanese *keiretsu* form attracted like with like. (Bello 1992; Hart-Landsberg & Burkett 1998)

The emergence of business groups in the following selected Asian countries is briefly mentioned:

Hong Kong

As a former British colony, some of today's Hong Kong business groups descended from the 19th century trading houses established by British colonialists to conduct trade with a weakened imperial China after the Opium War. Business groups that exist today from this period include the privately-owned Swire Group[1] while another (albeit listed) counterpart, the Keswick family-controlled Jardine Matheson Holdings[2] was the subject of a historical novel "Noble House" by James Clavell as a testament to the influence the family wielded on the island. What catalysed these historically British groups' expansion was their consolidation of capital in Hong Kong after the emergence of the Communist Party in China as a political force with mainland interests divested or expropriated. As one of Clavell's characters commented, Hong Kong was like a small village where everyone knew each other and the *taipan* was the most important personality on the island.

British-ruled Hong Kong was perceived as a stable location and became one of the first places for the mainland Chinese entrepreneurial class to immigrate to in the wake of Japanese colonialism, World War Two and increasingly, the unknown force of Mao Zedong and his policies. Business groups originating from this period include Li Ka Shing's Cheung Kong Holdings[3]and Lee Shau-Kee's Henderson Land.[4]

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[1] Swire Group (2012) About Swire – Our Story http://www.swire.com/eng/about/story.htm accessed 14 June 2012
[2] Four members of the Keswick family currently sit on the board of directors of Jardines http://www.jardines.com/the-group/directors.html (accessed 14th June 2012)
[3] Cheung Kong Holdings (2012) Chairman's Profile http://www.ckh.com.hk/eng/about/about_chairman.htm accessed 14th June 2012
[4] Henderson Land (2012) About the Group http://www.hld.com/en/about/profile.shtml accessed 14th June 2012

These Hong Kong groups formed a bridge between the West and to post-Cultural Revolution China as the latter emerged from the shadows of Mao. These businesses were able to maximise the opportunities that presented the island due to their long historical and political ties with successive mainland Chinese governments as it transitioned to a more open economy. For Hong Kong groups, the value of their 'old friends' relationships with the mainland are testament to their resilience and political savviness as expropriation did not occur after the handover of the island to China in 1997.

Lastly, an important distinction that can be made between these British and Chinese business groups is the former have had their family business operation for several generations with a formalised succession structure, while the latter groups are still controlled by their founder-owner entrepreneurs and facing succession issues as they transition to a multi-generational group.

Indonesia

The origins of today's Indonesian business groups were an outcome of the nationalisation of Dutch properties in the 1950s after the country's war of independence. President Soeharto's lengthy rule in the latter half of the 20th century allowed the consolidation and expansion of favoured and politically-connected groups.

One such group was the Salim Group which flourished under Soeharto's regime (Sato 1993). Salim Group is the country's biggest conglomerate with "interests in in agriculture, food, automobile manufacturing, building materials industry, chemical, banking and financial services, resorts and hotels, real estate and industrial parks, resources and international trade, distribution and retail, communications and media industry, charitable and public welfare."[5] It was founded by another ethnic Chinese Sudono Salim whose son Anthony now runs the group and navigates through the sometimes murky world of Indonesian politics.[6]According to Sato, the Salim Group is emblematic of favoured business groups under Soeharto's rule:

> "The 'pursuit of market domination' seen consistently throughout the development of the Salim Group can be understood as the manifestation of the group's own power: 'politically affiliated power' and 'conglomerate power'. These two hallmarks of Salim Group have been possible because of Soeharto's rise to power and because of the 'full-set' industrialisation strategy that has been promoted by Soeharto's government. In this era the Salim Group is a symbolic economic actor of Indonesia during the Soeharto era." (1993: 441)

[5] Business Week (2012) Salim Group http://investing.businessweek.com/research/stocks/private/snapshot.asp?privcapId=9682271 accessed 23 April 2012
[6] Saragih, BBT (2012) Chinese tycoons join politics for survival, Jakarta Post, 24th January http://www.thejakartapost.com/news/2012/01/24/chinese-tycoons-join-politics-survival.html accessed 23 April 2012

Indonesia's business landscape is dominated by the interests of the Salim family and peer group. With a government still emerging from Soeharto's long rule, fragile bureaucratic arms prone to influence, and an underdeveloped capital market, the dominance of Indonesian business families will continue in the foreseeable future.

Malaysia

The dismantling of the British colonial empire after World War saw immense structural socio-political changes occurring after the divestment of Malaya. Two new states were created from this former colony with the establishment of Malaysia and the creation of ethnically Chinese-dominant Singapore after the latter was politically ousted from the former. The winds of history also made an impression on the commercial actors in the region with one such group, the conglomerate Kuok Group, able to surf the tide of change.

The Kuok Group has its origins in the early 20th century when Kuok Keng Kang fled an economically depressed mainland China to seek his fortune in the British colony. During the Japanese occupation of Malaya, Kuok's son Robert became an apprentice at Mitsubishi. This exposure to a Japanese diversified conglomerate allowed Robert Kuok to modernise the family business and when his father died in 1949, he inherited the leadership mantle of a group largely comprised of agricultural interests. (Heng 1999: 163) Kuok took advantage of the process of decolonisation in Malaya and diversified into trade, shipping, oil and made most of the retreat by British companies such as Tate and Lyle (Heng 1999: 162) in the sugar trade.

Kuok expanded in the region and formed ventures with other ethnically-Chinese business families in other industrial sectors such as media and property. (Heng 1999: 163)

Privatisation under the rule of Mahathir in the late 20th century led to the evolution of a conglomerate structure and strategy similar to the Japanese form:

> "…the typical conglomerate was inclined to adopt a familiar strategy: deal in property and real estate, build up construction capacity, lobby for infrastructural and utility works, secure a banking or finance arm or a brokerage licence, buy up plantations, diversify into tourism, and enter newly privatised areas like telecommunications and social services…In effect, they evolved into a privileged league of private oligopolies which benefited from the fragmentation of state monopolies." (Khoo 2000: 219)

Indeed, the close form of ties between a few Malaysian business families and the state have been characterised as either being rentierist, distributional-coalitionist or indeed, cronyist. (Khoo 2000: 222)

South Korea

The nexus of state-led industrial development policies and business group development could not be more exemplified by the experience of South Korea. From its very beginnings, chaebols were inextricably linked to its political masters. The government unequivocally played a pivotal role in their establishment, development and expansion. The chaebol form had its origins under Japanese colonialism and was heavily influenced by the keiretsu structure. When Japanese rule ended, the colonialists' properties were seized with "industrial interests sold far below the market value" (Kim 2004) to favoured participants. This formed the basis of the emergence of the chaebol. As Lim (2003) narrates:

> "In the post-war environment, the Rhee government sold "vested properties" of formerly Japanese-owned industrial properties taken over by the US military government and subsequently transferred to the new Korean government. The Rhee government set the conditions for the sale of these properties so as to preclude competitive bidding and to favour the interim plant managers as well as the politically well-connected....Certainly not everyone who was privileged to pick up an industrial property at a fire-sale price had the entrepreneurial talent to build a business empire. But vested properties provided the initial base for many of the largest chaebol."

Hence, the chaebol emerged out of favourable government policies which also included low interests rates from Korean banks. In a financial coup, in the 1950s, South Korean commercial banks were privatised and the recipients of this process explicitly favoured the chaebols. From Lim again:

> "Using political connections, top industrial capitalists borrowed money from the banks in order to make bids for the ownership of the same banks. When bank privatization was completed in 1957, all major commercial banks were under the control of the industrial capitalists."(2003:42)

By the 1970s, export-oriented government policies were in full-swing which allowed the chaebols to expand with the backing of state banks. This strategy allowed chaebols to internationalise while their financing was being underwritten by the government. However, the South Korean government did impose a measurement of "export performance" which allowed the policymakers to objectively assess whether the expansion of its stable of national champions overseas were successful.(see Lim 2003: 44)

The reciprocal benefit from the private sector in pursuing or aligning itself with the government policies of the day, Amsden notes, led to mutually beneficial progress and successful outcomes. The governments of the region disciplined capital as well as labour. Thus selective relationships and

attachments with certain business groups allowed their progress to occur and their form to continue despite reaching a middle-class type of development.

However, this close nexus between politics and business did unravel and by the time of the 1997 East Asian crisis, the concentration of economic power and the management culture of dynastic dictatorship in the chaebols saw the "too big to fail" (Kim 2004: 12) nature of this private sector form of organising with immediate short-term severe effects for the rest of Korea's economy and society. Questions of legitimacy and financial sustainability hung over the partnership that had underpinned Korean's economy for the latter half of the 20th century: "…much of the '*chaebol* problem' encompassing both moral hazard and corporate governance issues, remained unsolved even as the economic crisis of 1997 approached." (Lim 2003: 49) For other countries and their business groups in the region, the troubles of the Korean chaebol instigated an inward-looking search for reform.

Thailand

Modern enterprise in this country can be traced to close interaction with Chinese entrepreneurs and Western trading houses in the mid-19th Century (Falkus 1989: 120). In the 20th century, these Western (mostly British) properties were nationalised and under military rule, the nationalised enterprises formed alliances with ethnic Chinese-owned industrial interests.

In Pananond's 2004 resource-based view study of a Thai business group owned by the Chansiri Family, Thai Union Frozen Products (Asia's largest canned tuna exporter), the author writes, "large family business groups are likely to stay as a dominant form of firms in Thailand because the business group structure responds effectively to the institutional context of developing economies such as Thailand…[and they] can be best understood as an institutional innovation for internalising the returns that accrue from operations in the imperfect market conditions of less developed countries." Not surprisingly, the familial-based society of Thailand resonates in the business group as "it is an organisational form that has been shaped by the sociological patterns of relationships in that specific society." (2004: 73)

The realisation that these groups dominate a large part of the private sector means foreign investors in the region must interact and form relationships with these groups as they do form a formidable barrier to entry due to: "the information asymmetry between local and foreign firm benefits diversified business groups at the expense of foreign multinationals and domestic non-diversified firms (2004: 74)

Pananond further expounds, "the large and diversified business group does have a rationale for its development and continued existence, especially in Asia and Latin America where the institutional context is often characterised by market imperfections and familial ties and the business group

structure is an appropriate organisational response to the environment in which it develops." (2004: 74)

Indeed, given the sometimes politically unstable environment of Thailand with military interventions occurring when the civil government fails to promote social harmony, it is notable the intersection of political-business ties under the prominent Shinawatra family who owns one of Thailand's largest conglomerates, Shin Corp through its holding company In Touch.[7] More notably it was founded by ethnic Chinese Thaksin Shinawatra who became Prime Minister of the country, was later deposed and whose sister Yingluck was later elected as Prime Minister in 2011.

China

China's Communist Party also became interested in forming business group structures in its 1997 plan albeit with ownership still linked to the party. This was done in large part to consolidate its various industries and partly propelled by nationalistic pride to have Chinese industrial giants enter the Fortune 500. (Amsden 2001: 275). In 2011, 61 Chinese companies had reached the Global Fortune 500 although the ranking system favoured companies that specialised by industry and less by conglomerate structure.[8]A discussion on the Chinese business group form is discussed later in this paper.

Business Group Formation in its Historical Context

In the region, the first wave of business group formation occurred during the colonial era of each respective country. The second wave of business group formation came in the aftermath of the post-Chinese civil war and Chinese cultural revolution era. This second wave had a more profound impact as this saw the emergence of ethnic-Chinese owned business groups especially in Taiwan, Thailand, Malaysia and Indonesia. Forming alliances with ethnic Chinese entrepreneurs became the trademark for much of the region's business groups as they expanded under institutionally weak post-colonial and post-war governments.

This form of picking national winners was hypothesised by Amsden (1995) under the principle of reciprocity. Amsden strongly argues the principle of reciprocity as explaining the basis of the region's industrial and economic development as opposed to its peers in South America during the same period. The government expected benefits from subsidies being given to selected "winners" or "supporters" of its industrial policy programs by tracking and ensuring performance standards were met.

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[7] In Touch Company (2012) Corporate website http://www.intouchcompany.com/index_en.asp accessed 23 April 2012

[8] CNN Fortune (2011) Global 500 By Location: China http://money.cnn.com/magazines/fortune/global500/2011/countries/China.html accessed 23 April 2012

The politically-connected, diversified business group was a success for an export-oriented industrial policy that fostered economic development and allowed some countries to lift their citizens out of poverty. However, the reliance on such opaque forms of private sector organising with unpredictable political ties (such as those that occurred under the crony capitalism regime of Indonesia and Philippines) provoked questions of viability and acceptance of whether this form of organising in the hands of a few, arguably, oligarchical families is best for long-term economic industrial development.

Theoretical Perspectives of Business Group Development

As the previous sections looked at the macro view of the business group largely through the lens of historical policies and institutional environment, this section seeks to explain the theoretical views behind their continued existence and endurance especially with regards to their governance structures.

The use of agency theory to explain the corporate governance of private sector companies is well-established.(Berle & Means 1993; Achilan & Demsetz 1972; Demsetz 1983; Fama & Jensen 1983; Jensen & Meckling 1976; Boyd & Hoskisson 2010) The application of agency theory is commonly represented in studies of corporate America and Anglophone countries where research primarily looks at the relationship between principal and agent – mainly the financial principals (such as shareholders with their representatives on the board of directors), and the managerial agents (that of executives and managers).(Mace 1971; Lorsch & MacIver 1989; Clarke 2004) The challenges in agency theory's applicability have become more obvious with its widespread use in the last quarter of a century to explain control – or lack thereof – and costs in principal-agent relationships. Given major American listed corporations have widely-dispersed ownership and generally do not have a dominant owner-manager, this ownership composition does not hold in other parts of the world especially in Asia. In countries where family-owned and family-managed corporations dominate, the premise of agency theory disappears as there is unity in strategic decisions: "Clan control implies goal congruence between people, and therefore the reduced need to monitor behaviour or outcomes."(Eisenhardt 1989:64)

Nevertheless studies of corporate governance have expanded internationally, consequently broadening the theory's scope and audience. Despite the anomaly of agency theory's application, there is persistence in its use in studies where ownership and control is one and the same (see Schulze et al 2001). Tsai et al applied an agency theory perspective to the CEO tenure of two different groups of Taiwanese firms: one family-owned, the other non-family-owned and found that family control serves as the crucial monitoring factor that is generally absent in widely-dispersed ownership corporate forms (2006: 26). Dharwadkar et al looked at the failure of privatisation in emerging economies from an agency theory perspective. The weak corporate governance structures within companies and lack of recognition of property rights in the external environment of most emerging economies resulted with an agency problem unique to developing economies - that of expropriation due to "the weak

governance context when large or majority owners assume control of the firm and deprive minority owners the right to appropriate returns on their investments."(2000: 660) Young et al (2008) supported the principal-principal problem of owner vs. owner value expropriation to differentiate this from the traditional Western agency problem of owner vs. agent. Agency theory remains a powerful and influential theory to study corporate governance. However it is problematic to apply this theory in countries where firms have high ownership concentration and how it explains the phenomenon of business groups.

The East Asian model is characterised by family control and high ownership concentration.(Claessens et al 2000) Control and ownership is not separated. Most large firms are family-owned, and are usually not listed or partially listed on the stock exchange. Stock exchanges are relatively new and underdeveloped. Control is through pyramid structures and cross-holdings. There is a long-term focus on wealth-building. In comparison to other models, firm and financial information is less publicly available. A small number of families control the economy and government officials directly participate in the control of the sector, suggesting the existence of crony capitalism. Countries belonging to this model include Hong Kong, Indonesia, Malaysia, Singapore, South Korea and Thailand. The Philippines definitively falls under this model.

Other theoretical perspectives provide a more compelling reason why business groups should exist, evolve and are the common form of private sector organising in the region. Explaining business group development is a source of rigorous debate. A variety of theories proffer different perspectives to their enduring existence. Millar et al (2005) posit the relationship-based nature of corporate governance in the region in the absence of institutional transparency, while Khanna and Yafeh propose a triangular perspective on business group development: the structure of the group depends on the extent of horizontal diversification, vertical integration and financial involvement; the control depends on family involvement and degree of pyramidal ownership; and the relationship of the business group with the state.(2010: 578) On a more macroeconomic vein, Chung looked at different theories such as institutional failure, transaction cost, resource-based and social capital to provide perspectives on business group development in Japan and Korea (Chung 2005) while Young et al (2008) supplemented this with their principal-principal agency perspective. The following table summarises their theoretical perspectives:

<insert Table 1 here>

For the most part, except for agency theory, the theoretical perspectives on business group development show how important the external, political environment is in determining business group development as the establishment of business groups in the wake of historical crises expounded earlier in this paper explained. Indeed, "[t]he nature of institutional country effects in which business groups are embedded…shapes the governance of business groups and their member firms."(Boyd &

Hoskisson 2010: 691) They "internalise functions for which no external market or supporting institution exists."(Colpan et al 2010: 7) Another perspective of Table 1 is shown in the following figure that shows the concentration of ownership of business groups in the following Asian countries has an inverse relationship with the level of institutional and regulatory development in these states.[9]

<insert Figure 1 here>

The more concentrated the ownership - and indeed the wealth - the less progress there is in institutional reforms in the areas of judicial efficiency, the rule of law and absence of corruption. The top 15 family-owned business groups in the more developed countries of the region such as Hong Kong, Japan and South Korea control less than half of the total value of listed corporate assets as opposed to their counterparts in the less developed countries. Higher business group concentration is a strong indication of the instability of the political and institutional environment for the size of business groups allows them to withstand the vagaries of uncertainty. This has strong implications for studies of other business groups around the world especially for family-owned business groups in the erstwhile politically turbulent Latin America and Middle East regions. Strong public sector institutions allow the private sector to do what they do best: allocate goods and services efficiently. Weak public sector institutions distort the groups' ability and capacity, with rent-seeking, revenue collection avoidance[10] and political influencing flourishing as a way to protect their family owners' interest.

The institutional perspective sees business groups as filling in the voids due to inefficiencies in a country's capital, labour and product markets. The market failure perspective supports this notion of business groups as filling in the institutional voids. The lack of trust in the political environment means the ability to transact commercially and with confidence with well-connected and well-established (albeit complex) entities supports to overcome this impediment. As a result, the market failure theory endorses the transaction costs theory which states business groups are more economically efficient in such a prevailing environment. In addition, the resource-based and social capital theory of business groups lends support to the efficiency and value creation argument.

[9] p.28 in Claessens, S. (2003) Corporate Governance and Development http://www.ifc.org/ifcext/cgf.nsf/AttachmentsByTitle/Focus_1_CG_and_Development/$FILE/Focus_1_Corp_Governance_and_Development.pdf accessed 20 June 2011

[10] The fall in revenue collection is indicative of a loss in trust and confidence in the government executive and/or public sector as related in the following situation in Central America:
"Álvaro Uribe, Colombia's stern former president, who made his country safer and also implemented a similar transfer programme, has become the hottest conference speaker in Central America. Businessmen in Guatemala last October loudly applauded his message about security; but when he exhorted them to pay their taxes, he was met with silence. Even in Costa Rica, "Tax evasion is the national sport," says Ofelia Taitelbaum, the ombudsman." http://www.economist.com/node/18558254?story_id=18558254 accessed 28 April 2011

Underpinning the principal-principal agency perspective is the realisation that the institutional framework is grossly underdeveloped, corrupted, lacking and non-existent in some countries. There exists little trust in the public or regulatory arms of the state as regulators remain vulnerable to politicisation and face undue influence or corruption by certain interests. However, at the same time this reinforces the perception that corporate governance in the business groups and their boards are heavily influenced by the owning and controlling shareholders and remain mere "rubber stamps" of the dominant owner/s. (Young et al 2008)

Therefore, the agency problems present in Anglo-American countries rarely exist in Asian companies. It is also worth noting, in studies of business groups in developing economies, their relationship with the state is fundamental. It is this relationship that determines why the other non-agency theories provide a more useful explanation of this phenomenon. In most Asian countries, the relationship business groups have with the state determines and influences the manner by which these companies operate.

Carney supports this notion by proposing four hypotheses of business group development in Asian business groups: institutional voids, life cycle, state-led industrialisation, and crony capitalism (Carney 2008: 602). Of the four, two are most pertinent in a developing country situation such as in Indonesia and the Philippines: that business groups fill the institutional void (Carney 2008: 598) with the provision of infrastructure which is normally the realm of the state, and the proliferation of crony capitalism in the post-dictatorship era which has allowed the endurance of some business groups. The state played a dysfunctional role in these countries (Granovetter 2001: 97). Yet dysfunctional business-state relationships are far from unidirectional as business groups with enough extraterritorial might and political connections can play a pivotal role in overthrowing the elected government of the day as in the case of the Chile's Allende government (Zeitlin et al 1974) and some Philippine business groups actively supported the removal of Marcos in the dying days of his dictatorship.

For other countries in the region namely Taiwan, South Korea and Japan, they were beneficiaries of state-led industrialisation as their governments were actively interventionist (Fligstein 1996). The relationship between the private sector in those countries and their governments were mutually beneficial (Zhang 2005), united by a common goal towards greater economic development and providing this distinct form of Asian capitalism (Granovetter 2001: 71-73; Whitley 1994). Finally, Carney's hypothesis of business groups as part of the life cycle proposed business group formation and affiliation by entrepreneurs was important in developing countries, but they could also "frustrate continued economic development by inhibiting the entry of new firms into the economy." (Carney 2008: 603)

The Dominance of Business Groups and their Structure

Ownership concentration is a manifestation of economic control[11]. In the ground-breaking study by Claessens, Djankov and Lang (2000) of 2,980 East Asian listed corporations, they found more than two-thirds of firms are controlled by a single shareholder. The table below shows the percentage of concentrated ownership across the region ranging from Japan where only the top 15 families control 2.1% of that country's GDP to Hong Kong where the top 15 families control over four-fifths of that island state's wealth:

<insert Table 2 here>

There is little evidence of any significant changes in the concentration of ownership amongst the leading families in East Asian countries in the last decade even after the 1997 East Asian Crisis and 2008 credit crisis. The 1997 East Asian Crisis and the collapses of Enron and WorldCom heightened the awareness that poorly run and weakly managed business groups in the region need to institute robust controls that promote transparent and accountable decision-making.(Faure 2002; Reed 2002; Trivellato 2002) dHowever, while political discourse improved due to the contagion effect of the crisisd (Derichs & Heberer 2002),apart from notable internal improvements of some Korean chaebols both financial crises - reiteratively - did not lead to fundamental, structural reform of the ownership concentration of Asian business groups

It was also notable that during the crisis of 2008-09, Asian family-owned business groups confidently managed to weather the storm. Indeed, these groups proved resilient in the aftermath of both crises with some opportunistic business groups consolidating their interests in the insurance sector after the bailout of American Insurance Group (AIG) and its divestment of extensive Asian interests in 2009. The owners of these Asian business groups remain solidly family-based.

According to the previously mentioned 2002 World Development Report, there is a link between high concentrated corporate ownership and the efficacy of legal protection in countries. That is, "concentrated ownership tends to substitute for weak legal protections" (2001: 58). This view complements and supports resource dependence theory and the resource based view of the firm in developing countries: where there is an unstable political environment, the conglomerate form is the preferred method of organising. Investors in weak institutional environments also play a premium on firms who are part of conglomerates due to the perception that "concentrated ownership delivers great benefits when those owners in control have appropriate incentives and when owners outside the firm

[11] For different classifications of control of a company, see Berle and Means 1933 and Sales, A. (1979) La Bourgeoisie Industrielle au Quebec, Quebec: Les Presses de L'Universite de Montreal

have more leverage."[12] This was supported by a McKinsey study that showed an average premium of 24% an investor would pay for a well-governed company in the Asia region.[13]

However, the dominance of family-owned business groups means their treatment of minority shareholders can be less than satisfactory and is a pressing corporate governance issue in countries with concentrated ownership. Even where the prevalence of business groups is a private response to weak government institutions, the concentration of wealth in a few people, families or groups is a "formidable barrier to policy reform" and could negatively affect "the evolution of the legal and other institutional frameworks for corporate governance and the manner in which economic activity is conducted."(Claessens et al 2000: 110) Business groups are a form of organising that try to mitigate uncertainty especially where the country has a dominant public sector and government executive. By being part of a business group, transaction costs between affiliated companies are lower and being part of a group may help overcome market failure problems, allows the transfer of managerial talent across businesses, and share other resources between affiliated companies (Kim et al 2004). The might of business groups and conglomerate power also allows competitive advantage over single firms. As business groups dominate industries, being affiliated with a business group allows a company access to the network and resources available within that group. Being part of a business group builds up and consolidates the social capital amongst members.

In terms of structure, business groups in the region that are vertically integrated reflect a great degree of control by owners and Leff saw their structure as substitutes for the imperfections in the capital market.(1978: 661-675). While business groups may be the most *efficient* form in an *inefficient* market, because of their size, domestic business groups have an almost unassailable advantage over new entrants with foreign ownership restrictions in developing economies – in most cases - unilaterally favouring domestic participants. Below is a figure showing the structure of two Filipino business groups with their listed and unlisted companies across different industrial sectors:

<insert Figure 2 here>

In the Philippines, listed business groups tend to be in the mature phase of their life cycle. They privately build up their businesses before utilising the capital market to unlock the market value of their assets. Business groups list one business after another and not at the same time. Therefore, a business group's portfolio has assets that are listed and others that remain private. In the above figure, the Ayala Group has 5 listed and 4 unlisted companies, while the SM Group has 6 listed and 4 unlisted companies. Both Ayala and SM groups are family owned by the Zobel de Ayala and the Sy

[12] World Bank 2001: 58
[13] McKinsey (2002) Global Investor Opinion Survey: Key Findings http://www.mckinsey.com/clientservice/organisationleadership/service/corpgovernance/pdf/globalinvestoropinionsurvey2002.pdf accessed 11th June 2010

Families respectively. As Guillen points out, in sectors where foreign investment is restricted, domestic business groups that have proliferated under such protectionist policies will be reluctant to lose this 'asymmetrical' position. Foreign entrants have little choice but to collaborate with them, thus ensuring the continuation of the status quo of the dominance and entrenchment of business groups. (Guillen 2000: 376)

The strong ambivalence towards the economic power and domination of a few select economic groups have been articulated by Kang et al (1991)'s book on chaebols, which posed the question on whether they were "the locomotive of growth or the personification of avarice" (Lim in Haggard 2003: 50, endnote 1) in South Korea, and more provocatively and recently and by Khanna & Yafeh in their 2007 article entitled *"Business groups: paragons or parasites."*

Perhaps this is a crude dichotomy, but it does highlight the difficult behaviour patterns at opposite ends of the ethical and governance spectrum in Asian business groups. Khanna and Yafeh conclude that both types of business groups exist: business group paragons are the ones who have a good reputation premium and are well known to practice good corporate governance (Carney 2008: 597) while the parasitic business groups rarely observe corporate governance standards and depend largely on the largesse of their political connections (Faccio 2006) and superior contacts to sustain the viability of their companies (Fisman & Khanna 2004: 621). This parasitic view of business groups provide support for Carney's hypothesis that some business groups emerged due to the reciprocal nature of crony capitalism. The common principal-agent problem common in Anglo-American countries are not present in the Asia as most owners are themselves part of management. In most cases, the control of business groups has not been decoupled from the owners. Unlike their widely-owned and -held non-family and listed Anglo-American counterparts, out of control managerial remuneration is less of an issue and a long-term outlook on the group of companies allows a lengthier strategic planning, albeit conservative, process.

The Economic Implications of Business Group Dominance

The implications for the dominance of business groups and the political economy perspective behind their ownership complexity are considerable. A volatile political environment influences business groups to organise in a form that can operate in a perceived absence of institutional order and an economic environment with endemic corruption. As business group theories in Table 2 mention, the volatility of the political environment ensures that this form of organising is the best way to do business in an uncertain political environment, and more essentially against the bulwark of a predatory state.

According to Dyer and Mortensen:

> "Hostile environments create a situation where individual entrepreneurs face significant moral dilemmas. They can either comply with the law, thus forfeiting the success of their businesses and their own economic well-being, or they can attempt to work within the context of a corrupt system in order to survive. Most choose survival." (2005: 253)

This was the case for Philippine and Indonesian business groups under the Marcos and Soeharto dictatorships respectively. How to manage the political risk in a predatory, crony capitalist state required major manoeuvrings that blurred the line between business and politics. Galang (2011) provides a useful insight into the different ways the private sector responds to corruption in its business environment with strategic activities to mitigate its debilitating impact. For one Filipino business group, mitigating this political risk included having a major foreign investor in its companies as it would be to Marcos' detriment to seriously offend another foreign government if he decided to expropriate the assets of a foreigner whose political masters were bigger and mightier - economically, politically and militarily - than an archipelago on the western coast of the Pacific.

Managing political risk in this way has been applied before in corporate history with varying degrees of success. In Mitterrand France, the presidential decree of nationalising strategic sectors and companies was met with fear, loathing and futile acceptance. Making overtures to a foreign investor to mitigate government expropriation is not an uncommon business strategy. Indeed one French bank invited the "U.S. Treasury to threaten France with retaliation if the takeover went through. The Treasury refused."[14][15] Unintended consequences arise when the lines between political and business risks intersect.

As Schneider points out, the degree of political intimacy a business group has with the government of the day can readily determine its ability to strategise and operate in the future (2010: 662). Indeed, the complexity of family business group ownership complements the opacity of political strategies to rein in the financial strength of the former, or to bring the oligarchic private sector under the rule of the state. However, the strength of business affiliated business group transactions can also be the source of its weakness. In an era that emphasises transparency, the related party transactions of business groups must ensure it can withstand such scrutiny. Financial markets readily punish business groups which have less than transparent business arrangements as owners of India's Satyam Group[16] and the

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[14] Byron, C. (1981). France's Private Banks Go Public, Time Magazine, September 28 http://www.time.com/time/printout/0,8816,953148,00.html

[15] This 1980s strategy had ramifications for another business twenty years on. For the French cosmetics company L'Oreal - in anticipation of the Mitterrand regime - invited the Swiss multinational Nestlè to take an ownership stake in the company in 1974. This fear proved to be unfounded as Mitterrand did not seize the company nor viewed the fashion sector as strategic enough. See The Economist (2009) In pursuit of beauty, January 22nd http://www.economist.com/businessfinance/PrinterFriendly.cfm?story_id=12995773

[16] Leahy, J. (2009) $1Bn fraud at India IT Group, Financial Times, http://www.ft.com/cms/s/0/32ea8364-dc85-11dd-a2a9-000077b07658.html

aforementioned Parmalat Group discovered. Kim argued that Korea's chaebols are a reflection of its domestic market being weak with insufficient competition (2004: 31).

For politically well-connected groups such as Indonesia's Salim Group and the Philippines' Lucio Tan Group of Companies, both have survived their respective country's transition – albeit weak transition - to democracies. Indeed, the introduction of corporate governance reforms to these family business groups has proven to be a conundrum. The professionalisation of these business groups has meant the improvement in their standards of behaviour and codes of conduct. Professionalised business groups operate ensure family members who are appointed as potential successors to the family business undertake their education in Western business schools. However, their expectation and standards of behaviour from the state are not similarly reflected in their public sector regulatory counterparts.

More specifically, the family-owned business groups are affected by doubts and conflicts that are present in other family-owned businesses and business families. Indeed, they are not so different to any other family. Interfamily disputes are common and succession is the Achilles heel of any successful family-owned business group. For the owners of Samsung, the Lee family's disputes were unmasked with filial conflict[17] echoing India's Ambani brothers with their inheritance of Reliance Industries.[18]

Finally, what does the business group structure in the region mean for our understanding of China's economic development? While the strong arm of the state under the Communist party is still ever present with its purges and censorship, the "princelings"[19] or children of revolutionaries have been adept in exercising their privileged position and are acutely transforming and evolving the structure of state-owned and state-run businesses to the domain of family business ownership. In particular, one princeling-general[20], Ren Zhengfei, has managed to transform Huawei into a global telecommunications enterprise with inauspicious undertones,[21] yet its structure of having insiders on

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[17] AFP (2012) Brother sues Samsung boss – for $580M, Sydney Morning Herald, 15 February http://www.smh.com.au/technology/technology-news/brother-sues-samsung-boss---for-580-million-20120215-1t4pr.html accessed 15 February 2012

[18] Sharma R. & Bhattacharya, P. (2009) Ambanis exchange accusations as Reliance rift grows, Wall Street Journal, 9th August http://online.wsj.com/article/SB124966875030315041.html accessed 23 April 2012

[19] Editorial (2012) China: Fall of a princeling, The Guardian, 12th April http://www.guardian.co.uk/commentisfree/2012/apr/12/china-fall-of-princeling?newsfeed=true accessed 23 April 2012

[20] Bo Zhiyue (2006) Princeling-Generals in China: Breaking the Two Career Barriers, Issues and Studies, 42 (1): 195-232; Huawei (2012) Corporate Governance Report http://www.huawei.com/en/about-huawei/corporate-info/annual-report/annual-report-2010/corporate-governance-report/index.htm acccessed 23 April 2012

[21] Hartcher, P. (2012) Why ASIO won't get online with Huawei, Sydney Morning Herald, 10th April http://www.smh.com.au/opinion/politics/why-asio-wont-get-online-with-huawei-20120409-1wl2y.html acccessed 23 April 2012

the board, its perception as a ‘national champion” and government-backed financing makes it not too dissimilar from the growth of other business groups in the region.

It remains to be seen to what extent the party’s leadership will allow the transformation of state enterprises to well-connected family-owned enterprises like the rest of the region as this is the first generation of founder-entrepreneurs. The business interests of these princeling families are interconnected with the economic development of China. How they are run and governed will set the tone and value of Chinese enterprises as they expand in the future. Professionalisation will be a challenge and like other family-owned business groups, succession issues will prevail. Whether the concentration of power and capital in a select group of oligarchical groups are healthy for the state is something future research can look at and it will be in the succeeding generations that we will able to see more clarity.

Understanding the weaknesses and strengths of business families provide a window into how the region economically develops and how ruling families will still rule the private sector of the region in the foreseeable future. The business groups of region may not be taking the path of Chandlerian development where family-based capitalism transforms into managerial capitalism. Indeed the maturation of Asia’s family-owned business group to generational ownership has more in common with European family-owned business groups than American conglomerates with their widely dispersed form of ownership.

A strong private sector requires a strong public sector so that the latter has the capacity to regulate and resources to apply laws equally and not haphazardly. A regulator that is not politicised and that can make robust independent decisions will give more confidence to the majority of private sector participants. This, perhaps, is one of the major differences between business groups that operate in developing countries, and companies operating in developed countries: the robust, regulatory state.

This conundrum was pointed out by the Ayala business group CEO and how the weak public sector in his country is proving to be a challenge to operate in an ethical business manner:

> “We have long decided to meet what we believe are global ethical and governance standards so that we can succeed in a world where those standards are set. But in emerging markets, where institutional foundations need strengthening, those ethical standards can, ironically, be a competitive disadvantage. Others can take advantage of the system’s malleability, if only in the short term…As a group, we try to keep business and politics separate, which is not particularly easy to do in a country like the Philippines.”[22]

[22] Gibson, K. (2002) A case for the family-owned conglomerate, McKinsey Quarterly http://mkqpreview2.qdweb.net/Governance/Leadership/A_case_for_the_family-owned_conglomerate_1238

The precepts of transparency and accountability have no force if government regulators fail to ensure all companies disclose the required information. But as the above statement shows, where there is an imperfect market, exacting information is unreliable and hard to verify. This resonates with the market failure theory and institutional theory of business group formation. A business group can never be a replacement for a strong state. They are an adequate stop-gap during a long period of transition. However, business groups represent the private sector and there are profound limitations on how effective these entities can operate. Business groups are not an adequate replacement for civil society organisations though they may contribute to civil society's functioning. They are not a replacement for government because their goals are different and their motivations are largely based on that of their family owners.

Business groups can effectively contribute to their country's economic development if there is public sector leadership that will promote less unsavoury ethical behaviour. Reciprocally, undermining the institutions of the state for short-term private gain leads to long-term weaknesses and instability and the market power of business groups should not be an excuse for weakening the imprimatur of a democratic state and its promotion to create a less oligarchical society.

Conclusions

This article examined the development of business groups under the state-led industrial development policies of countries in the region, theoretical underpinnings of Asian business groups, their dominance and how they operate in the region. It also looked at the highly concentrated ownership of these groups and the complex ownership structure of their companies. The private sector of the region is highly concentrated in its ownership and control. It is ruled by families and is reflective of an oligarchic private sector.

The main reason why business groups dominate the economic life of their countries especially in East Asia is they provide strong institutions – even certainty - in an otherwise poor institutional and regulatory environment due, in some cases, to the perception of a weak state. Not surprisingly, a secure association with a business family provides more certainty and security than with the whimsical maelstroms of politicians (and their interests) whose tenure of power may be short-lived in comparison. Where privatisation of government utilities allowed the emergence of a more diversified group of shareholders as in Australia, this process only allowed the consolidation of financial interests by East Asian groups.

Even in more developed city-states such as Singapore and Hong Kong, business families dominate the economies as government institutions do not have the same professionalised bureaucracy that allows an effective depoliticised public sector to operate independently of elite family interests. For countries who have risen from the shadows of colonialism, the after-effects of European and/or American

colonialism have ironically produced selected families or business elites to own and control so much of the country's private sector capital. Indeed, this paper argues East Asia in the post-colonialism era has produced an environment that has allowed Machiavellian elites to prosper simply because the weak arms of the state have undermined the government's effectiveness in terms of being able to objectively, consistently and effectively implement common commercial rules without fear or favour. Furthermore, this author argues China's ruling party elites have ensured a new generation of dominant business families will emerge in the next generation or so because its government have failed to treat all its citizens (party and non-party members alike) equally with a bias towards party members who are seen as the chosen elites with more opportunities given to this group and the business networks that open to outside investors when they associate with them.

The pervasive influence of business groups is often associated with an ambivalence which can undermine the development of more rigorous, objective ethical and governance standards, and the independent institutions that will uphold and enforce these standards. By their size and scope they also influence the political life of the country but equally, their strategies and structure are also influenced by current political trends. Business groups will remain the dominant form of private sector organising in the region; explaining their behaviour will provide better understanding for their enduring existence. The issues outlined in this paper: their origins, business interests, form, function, influence, relationship with regulatory bodies, pivotal role with state-led development and the emergence of China's business families are areas where future research can shed more light.

Tables and Figures

Table 1: Theoretical Perspectives on Business Group Development

Agency Theory	This looks at the organisational microcosm of interacting relationships within an organisation. Primarily, this looks at the relationship between the principals (the financial ones such as shareholders) and agents (executives and managers). This is the most prominent theory used in corporate governance despite its flaws.
Institutional theory	Institutional theory asserts that highly diversified business groups (BG) create value by compensating for a nation's inefficient capital, labour, and product markets
Market failure theory	Market failure theory, concurring with institutional theory, argues that external markets can fail due to inefficient market mechanisms, legal impediments, and lack of trust
Transaction cost theory	Transaction cost theory argues that internal business transactions lower transaction costs because they avoid costs associated with contracts, negotiations, and contract enforcements.
Resource based theory	Resource-based theory asserts that BG-affiliated companies have opportunities to acquire and accumulate valuable resources, such as industry entry skills, trained employees, managerial skills, export-related skills, and others, giving them resource advantage over non-affiliated companies .
Social capital theory	Social capital theory proposes that intra-firm networks such as BG companies are social capital that can facilitate value creation.
Principal-Principal Agency Theory	Principal-principal agency theory argues that because BGs are owned and managed by founder families, agency problems are minimised between professional managers and shareholders. The institutional environment is underdeveloped and the framework close to non-existent. Boards are rubber stamps of the owner.

Table 2: Concentration of Family Control in East Asian Corporations (Claessens et al 2000: 108)

Country	Average No. of Firms per Family	% of total value of listed corporate assets that families control (1996)				% of GDP
		Top 1 family	Top 5 families	Top 10 families	Top 15 families	Top 15 families
Hong Kong	2.36	6.5	26.2	32.1	34.4	84.2
Indonesia	4.09	16.6	40.7	57.7	61.7	21.5
Japan	1.04	0.5	1.8	2.4	2.8	2.1
Malaysia	1.97	7.4	17.3	24.8	28.3	76.2
Philippines	2.68	17.1	42.8	52.5	55.1	46.7
Singapore	1.26	6.4	19.5	26.6	29.9	48.3
South Korea	2.07	11.4	29.7	36.8	38.4	12.9
Taiwan	1.17	4.0	14.5	18.4	20.1	17.0
Thailand	1.68	9.4	32.2	46.2	53.3	39.3

Figure 1: Relationship between Institutional Reform and Ownership Concentration (Claessens 2003: 28)

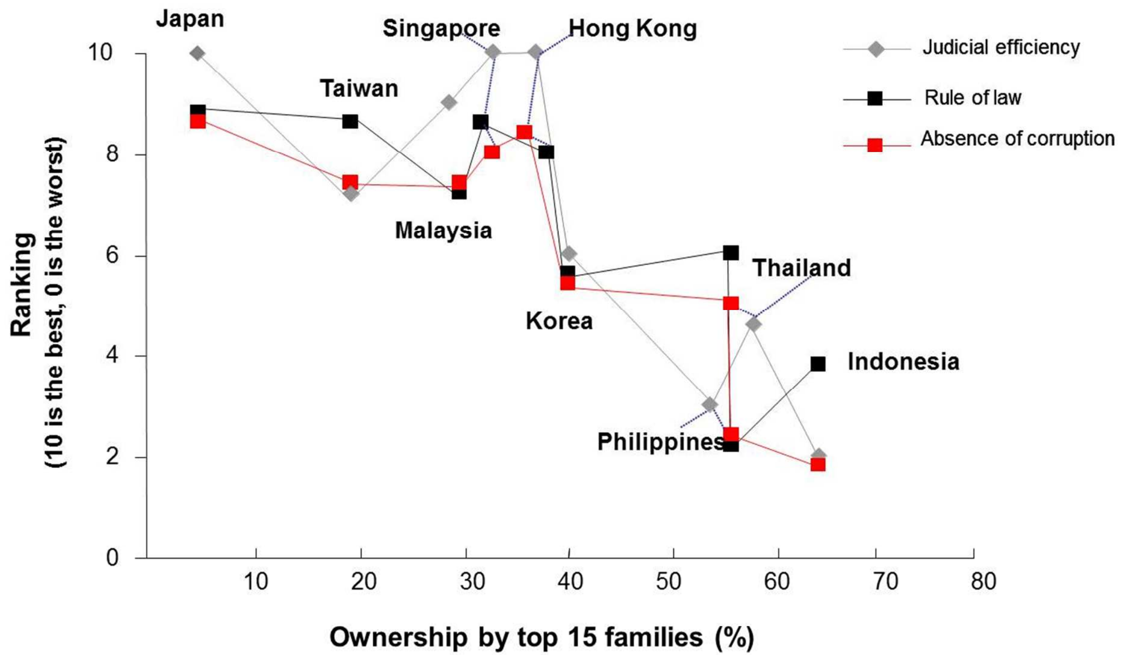
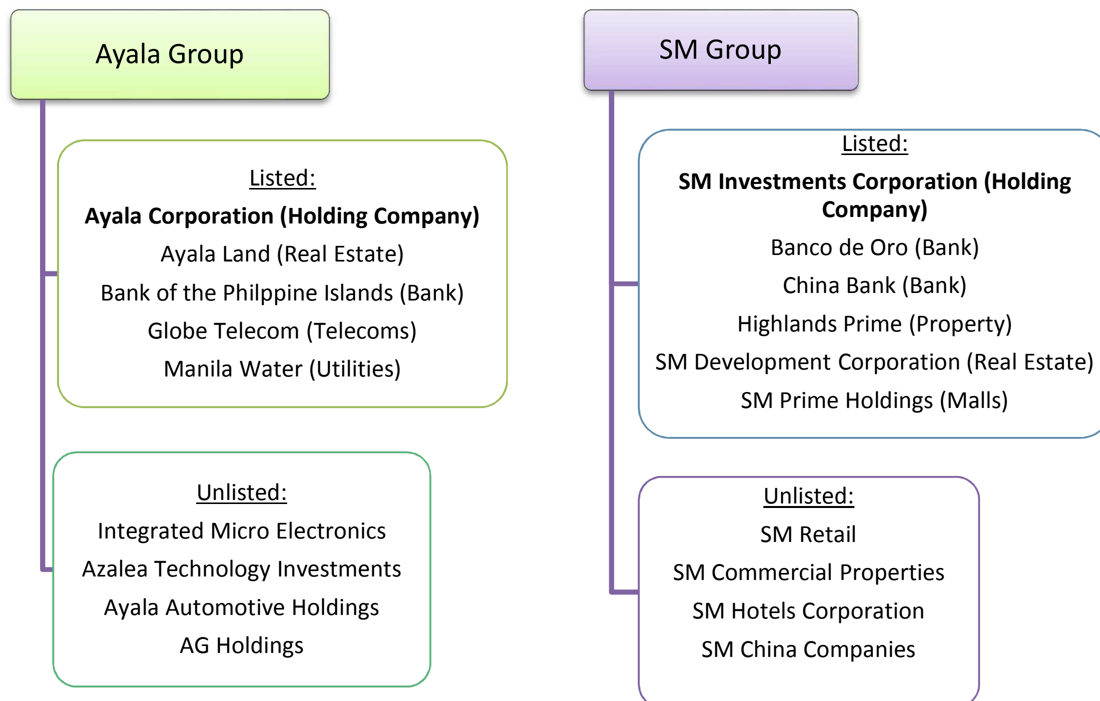


Figure 2: Listed and Unlisted Subsidiaries of Two Filipino Business Groups in 2007



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