The World of Family Business

Indian School of Business
MBA Students

October 2009
Family Businesses

Who Are They?

How Do They Perform?

How Do They Think?

What Difference Do They Make?
Family Business Quiz

1. Family businesses represent what percentage of western economies?
   a) 95%
   b) 65%
   c) 55%
   d) 25%
Family Business Quiz

1. Family businesses represent what percentage of western economies?
   
a) 95% Firms
b) 65% Employment
c) 55% GDP
d) 25% Public Markets Cap
“Shirt Sleeves to Shirt Sleeves”

Padre Bodeguero  
Hijo Millonario  
Nieto Pordioçero  

富  不  過  三  代

Pai Rico  
Filho Nobre  
Neto Pobre  

La première génération la crée  
La deuxième la développe  
La troisième la tue

Förvärva  
Ärva  
Fördärva  
Erwerben  
Vererben  
Verderben

“The children of the children are indifferent.”
- Shakespeare

“Generations pass while some trees stand, and old families last not three oaks.”
- Sir Thomas Browne, *Hydriatophia*, 1658
I must study politics and war that my sons may have liberty to study mathematics and philosophy, geography, natural history, naval architecture, navigation, commerce and agriculture in order to give their children a right to study painting, poetry, music, architecture, statuary, tapestry and porcelain.

John Adams
Paris, 1778

Let us now return and explain the genesis of the democratical man. An oligarchical father has a son whom he brings up on narrow and parsimonious principles. The young man tastes the honey of drones, and sedition is engendered within his soul. A struggle ensues, the unnecessary desires prevail and the young man becomes an impartial devotee of pleasure in all its forms and consequently a follower of democracy.

Plato
Family Business Quiz

2. Which is the Greatest Family Business Challenge?

- a. Next Generation Competence
- b. Letting Go
- c. Sibling Rivalry
- d. Scattering Interests Among Cousins
- e. Death Taxes
- f. Changing Business Conditions
Family Business Quiz

2. Which is the Greatest Family Business Challenge?

a. Next Generation Competence
b. Letting Go
c. Sibling Rivalry
d. Scattering Interests Among Cousins
e. Death Taxes
f. Changing Business Conditions
Inheriting the business from you makes me a born businessman, right, Dad?
Honey, Quick! He just said his first words!!!
2. Which is the Greatest Family Business Challenge?

   a. Next Generation Competence
   b. Letting Go
   c. Sibling Rivalry
   d. Scattering Interests Among Cousins
   e. Death Taxes
   f. Changing Business Conditions
FOR YOUR 60TH BIRTHDAY, SON,
I'VE DECIDED TO GIVE YOU THE COMPANY

EH??

GAB'S.
Which is the Greatest Family Business Challenge?

a. Next Generation Competence
b. Letting Go
c. Sibling Rivalry
d. Scattering Interests Among Cousins
e. Death Taxes
f. Changing Business Conditions
"It's OK, Mom. We're just having a proxy fight."
GO ON, KIDS, LET FATE DECIDE WHO WILL TAKE OVER.

IF I'D KNOWN I'D NEVER HAVE BOtherED GETTING THREE MBAs...

GABS.
Who says your brother’s the most logical choice as the next president?
2. Which is the Greatest Family Business Challenge?

a. Next Generation Competence
b. Letting Go
c. Sibling Rivalry
d. Scattering Interests Among Cousins
e. Death Taxes
f. Changing Business Conditions
Hagar the Horrible

We need medical attention, Dr. Zook!
You sure do! Were you ambushed by Attila the Hun?

No—we just returned from a family reunion!
Which is the Greatest Family Business Challenge?

- a. Next Generation Competence
- b. Letting Go
- c. Sibling Rivalry
- d. Scattering Interests Among Cousins
- e. Death Taxes
- f. Changing Business Conditions
The trick is to stop thinking of it as your money.
Family Business Quiz

2. Which is the Greatest Family Business Challenge?

a. Next Generation Competence
b. Letting Go
c. Sibling Rivalry
d. Scattering Interests Among Cousins
e. Death Taxes
f. Changing Business Conditions
The Fundamental Dilemma

Family

Business
Five Principles of Success

1. Respect for the Challenge
2. Understanding of the Differences
3. Communicating
4. Planning
5. Commitment
Family

Management

Ownership
Five Principles of Success

1. Respect for the Challenge
2. Understanding of the Differences
3. Communicating
4. Planning
5. Commitment
Family Business Quiz

3. Research has shown that all but which one of the following helps family businesses continue and prosper?

a. Independent Board of Directors
b. Regular Family Meetings
c. Family Constitution
d. Work Experience Outside the Family Business
e. Use of a Family Business Consultant
Family Business Quiz

4. Family business profitability relative to non-family business profitability is on average

a. More profitable?

b. About the same?

c. Less profitable?
Family Firms are More Profitable

Ward: 26% vs 21% ROIC (5 years)

Anderson-Reeb: 5 – 10% S&P 500 (10 years)

Morgan Stanley: +16%/yr vs. MSCI & 18.5% ROE vs. 14.1% ROE (5 years)

Pitcairn US: 30% Premium MV/BV (20 years)

Denison-Ward: Culture of 200 companies

FB 1000: +35% ROIC (2006)
BEST OF THE BEST

A NEWSWEEK study shows family firms outrunning their rivals on all six of the leading stock indexes in Europe, and ranks the top 10 companies.

The Family Factor

A Thomson Financial study for NEWSWEEK compared family firms with rivals on the six major indexes in Europe, and ranked the top family company stocks, with surprising results.

April 12, 2004, p. 42

CHARTING A HOT BUSINESS MODEL
Companies with a big family shareholder outperformed on six key indexes.

- Family stocks
- Nonfamily stocks

1993 03 93 03 94 03 93 03 93 03 93 03
FRANCE GERMANY ITALY SPAIN SWITZERLAND UNITED KINGDOM
...and Continue

FBs: 20% → 50 years

S&P 500: 15% > 40 years

McKinsey 1000: 14% > 37 years

FB 1000: 30% > 100 years
Family Business Quiz

5. Which is the oldest family business?

a) Hoshi Hotel (Japan)
b) Clinton Devon Estate (England)
c) Antinori Wine (Italy)
d) Cordoniu Wine (Spain)
e) Hugel & Fils Wine (France)
f) Ulefos Saw Mills (Norway)
The Reasons?

- Purpose
- Strategy (2/3)
  - Long-Term
  - Unconventional
  - Quality
- Culture (1/3)
  - Personal Values
  - Time Orientation
  - Prudence & Frugality
- Adaptability
How Do We Think About?

- Investing in People
- Inverting in R&D
- Investing in New Products
- Investing in New Markets
- Investing in Alliances
Some Survey Results

• “Only 1% of corporate directors reported that they had never encountered the dilemma between maximizing the stock price and acting in the long-term interest of the firm.”

  Lorsch & MacIver, HBS

• “Stock market’s attention to quarterly earnings has contributed to a decline in long-term investment... and competitive edge.”

  82% of 100 USA CEOs

• “78% of CFOs would give up economic value in exchange for smooth earnings.”
  – 80% would reduce R&D to meet targets
  – 41% would reduce +NPV investments
## Our Survey Results

<table>
<thead>
<tr>
<th>Statement</th>
<th>NFB</th>
<th>FB</th>
</tr>
</thead>
<tbody>
<tr>
<td>I believe my company under invests in the future (CEOs)</td>
<td>43%</td>
<td>8%</td>
</tr>
<tr>
<td>Our planning horizons are getting shorter</td>
<td>84%</td>
<td>59%</td>
</tr>
<tr>
<td>There is no doubt in my mind who will control this company in five years</td>
<td>40%</td>
<td>82%</td>
</tr>
<tr>
<td>If I see a near-term problem I shift my focus to it to the detriment of long-term initiatives</td>
<td>74%</td>
<td>47%</td>
</tr>
<tr>
<td>The future will be better than the past</td>
<td>68%</td>
<td>90%</td>
</tr>
<tr>
<td>In our company we actively promote the past</td>
<td>21%</td>
<td>75%</td>
</tr>
</tbody>
</table>
Why? Values?

Culture is a system of informal, unwritten, yet powerful norms, derived from shared values that influence behavior.
Corporate Culture & Profitability

Adaptability

Involvement

Mission

Consistency

Dan Denison, IMD
Distinct Family Business Culture

Adaptability
Flexible

Mission
Stable

Involvement

Consistency
Internal

External

Source: Denison
Stronger Culture

• Tenure and Stability
• History
• Different Values
**Values**

<table>
<thead>
<tr>
<th>Innovation</th>
<th>Courage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Empowerment</td>
<td>Dignity</td>
</tr>
<tr>
<td>Performance</td>
<td>Reputation</td>
</tr>
<tr>
<td>Teamwork</td>
<td>Fairness</td>
</tr>
<tr>
<td>Change</td>
<td>Open-mindedness</td>
</tr>
<tr>
<td>Leadership</td>
<td>Authenticity</td>
</tr>
<tr>
<td>Efficiency</td>
<td>Hard Work</td>
</tr>
<tr>
<td>Profitability</td>
<td>Stewardship</td>
</tr>
<tr>
<td>Quality</td>
<td>Dependability</td>
</tr>
<tr>
<td>Communication</td>
<td>Empathy</td>
</tr>
<tr>
<td>Creativity</td>
<td>Curiosity</td>
</tr>
<tr>
<td>Learning</td>
<td>Humility</td>
</tr>
<tr>
<td>Continuous Improvement</td>
<td>Discipline</td>
</tr>
<tr>
<td>Entrepreneurship</td>
<td>Prudence</td>
</tr>
<tr>
<td>Excellence</td>
<td>Sincerity</td>
</tr>
<tr>
<td>Customer Service</td>
<td>Do The Right Thing</td>
</tr>
</tbody>
</table>
Most Common Core Values

**Mutual respect:** Empathy, tolerance, golden rule, compassion, trust, generosity, cherish individuality

**Stewardship:** Perseverance, long-term, determination, tenacity, persistence, hard work, legacy

**Integrity:** Do-the-right-thing, honorable, trustworthy, reputation

**Personal responsibility:** Independent thinking, reliability, freedom

**Fun:** Enthusiasm, passion, celebration
Different Values

and

Different Beliefs

Past / Present / Future

Nature of Humankind: Good / Neutral / Bad

Individuality v. Collectivity
Company Time Orientation

Family Firms

<table>
<thead>
<tr>
<th>Past</th>
<th>Present</th>
<th>Future</th>
</tr>
</thead>
<tbody>
<tr>
<td>+</td>
<td>—</td>
<td>+</td>
</tr>
</tbody>
</table>

Non-Family Firms

<table>
<thead>
<tr>
<th>Past</th>
<th>Present</th>
<th>Future</th>
</tr>
</thead>
<tbody>
<tr>
<td>—</td>
<td>+</td>
<td>—</td>
</tr>
</tbody>
</table>
Best Places to Work

- Founder Businesses 34%
- Family Businesses 26%
- Partnerships 16%
- Non-Profits 12%
- Associations/Co-Ops/ESOPs 4%
- Widely-Held 8%
Century of Success

“Control is the ability to absorb and adapt.”

Confucious

• Resilience
  – Slack Resources
  – Ownership Commitment

• ProActive AdaptAbility
  – Sensing Fronts
  – Testing Fronts

• Continuity
  – Sensibility
  – Tenacity
## The Family Business Paradigm

<table>
<thead>
<tr>
<th>For the Family Firm</th>
<th>For the Non-Family Firm</th>
</tr>
</thead>
<tbody>
<tr>
<td>The purpose is continuity</td>
<td>The purpose is maximizing near-term share price</td>
</tr>
<tr>
<td>The goal is to preserve the assets and reputation of the owning family</td>
<td>The goal is to meet institutional investor expectations</td>
</tr>
<tr>
<td>The fundamental belief is that the first priority is to protect downside risk</td>
<td>The fundamental belief is that more risk promises more return</td>
</tr>
<tr>
<td>The strategic orientation is adaptation</td>
<td>The strategic orientation is constant growth</td>
</tr>
<tr>
<td>The management focus is continuous incremental improvement</td>
<td>The management focus is transformation</td>
</tr>
<tr>
<td>The most important stakeholders are customers and employees</td>
<td>The most important stakeholders are shareholders and management</td>
</tr>
<tr>
<td>The business is seen as a social institution</td>
<td>The business is seen as a disposable asset</td>
</tr>
<tr>
<td>Leadership is stewardship</td>
<td>Leadership is personal charisma</td>
</tr>
</tbody>
</table>
“Continuity is the fundamental value of a family business.”

G. Agnelli, 2001

“All decisions are made in the context of the long-term preservation of the family name, honor and traditions.”

Wallenberg
“I am not in favor of mega-mergers which are counterproductive to create what this industry is about, which is innovation.”

Franz Humer, CEO Roche

“Being a family business is an asset. The employees know there is a Marriott family and that provides stability and continuity in its management.

We’re not constantly shifting chief executive officers around like other companies.

When a CEO is shifted the company gets a new set of values and ideas and that creates confusion and instability.”

Bill Marriott
“We are fearful when others are greedy, and greedy when others are fearful.”

Warren Buffett

“We answer to a higher authority than the stock market – that higher authority being family values.”

Levi Strauss
Special Topics for Family Businesses in India

• How fast to grow?
• Corporate financial structure
• Beware of generic strategy
• Separating ownership and management
• One family and one business
• Building good boards
• Evolving to strategic philanthropy