

KEEPING IT IN THE FAMILY – AND SUCCESSFUL

Family companies are all around us. The figures speak for themselves. In New Zealand around 220,000 registered businesses, between them generating up to 80% of all employment and 65% of GDP are family operations of one sort or another

Of course, not all family businesses are alike. They span the spectrum from small husband-and-wife enterprises to corporations with instant brand recognition. One-third of the 1000 largest companies in the world are controlled by families but half are traded publicly, half are privately held. Some like News Corporation (media) and BMW (car maker) only have a few members. Others such as Henkel (cleaning, personal and homecare products and adhesives) and Cargill (producer and marketer of food, agricultural, financial and industrial products and services) have dozens of family proprietors. So, whilst there is a danger of ownership being so tight that it shuts out the welcome winds of change, inevitably, more family members will mean a greater potential for disunity.

Family matters are among the least rational aspects of all human behaviour, whereas business success relies to a large extent on cold rationality. How are these behavioural polar opposites reconciled when there is the ever present danger and temptation for families to meddle in management as well as in the boardroom?

There are three essentials; first, good family business requires clarity both of the roles and responsibilities of the owners; second, family unity is essential in determining the company vision and purpose; and third, commitment to the business and management teams.

Highly motivated

The strength of family ownership is not only that it is concentrated; it is also intense and personal. Typically most of the family's wealth is invested in the business. The family is therefore usually highly motivated to be vigilant and to contribute because the wider issue for family-controlled companies is ensuring that the business adapts over the generations.

During the global financial crisis, family businesses generally performed better, according to the KPMG Survey of Family Businesses 2009. "This is because they tend to be more patient with their profit expectations and more conservative from a balance sheet perspective with their investment decisions," says KPMG partner Bill Noye.

Family businesses that survive over the generations make sure they permeate their ethos of ownership with a strong sense of purpose, usually preferring steady long-term growth and performance to avoid risking the family's wealth and control of the business. This tends to shield them from the temptation, which has recently brought many corporations to their knees – of pursuing maximum short-term performance at the expense of long-term company health.

The two dominant success factors are: strong boards and a long-term view coupled with prudent yet dynamic portfolio management. Successful family businesses tend to have strong governance with members of these families avoiding the principal agent issue by participating actively in the work of company boards where their focus is on developing strategy and diligently monitoring performance. The family can also be a true asset to the management team by providing deep industry knowledge, since collectively they have been around the industry for decades. And vice versa.

Independent directors

The benefits of an active board containing independent directors lie in encouraging creative strategic brainstorming and providing objective opinion and a professional forum for resolving complex family issues, for example evaluating and compensating family managers. An effective board will also provide support and expertise for succession planning as well as mentoring next generation leadership. Independent directors should also bring an expanded network of contacts. If best practice is followed and the owners are responsible for designing the board and electing the directors then the foundation for success is laid.

Four goals

To synchronise governance and management, owners should propose the goals in four key areas - growth, risk, liquidity and profitability. The board should then evaluate these for feasibility and consistency. Addressing these four goals forces the owners to grapple with the inevitable trade-offs in expectations.

Thus, to be long-term successful, a family business must meet two intertwined challenges: achieving strong business performance and keeping the family committed to and capable of carrying on as the owner. Family ownership and professional management can provide the best of both worlds, enabling managers to take a long-term view in decision-making, with less pressure to produce quarterly results for investors or to achieve earnings targets. Effective engagement by family members permits a governance system that empowers and trusts management to pursue long-term strategies. Trust in management also reduces the friction of governance and burdensome costs of boardroom regulations.

Reference:

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