# Turning to Family Firms for

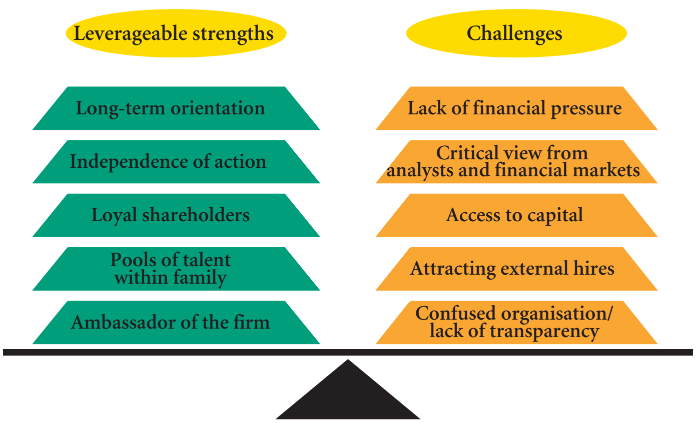
**After decades of silence and discretion, family firms are attracting the interest of researchers and media alike. The market capitalisation collapse of renown public giants -and dozens of other highly praised companies- has triggered a renewed interest in these family-owned companies who seem to transcend the centuries, survive storms and grow ever stronger. This begs the question: how do they do it? In an attempt to pinpoint their characteristic strengths, we asked ourselves: could any of these learnings apply to other types of companies? By the same token we also asked: are there any red flags which family firms should be paying attention to?**

At Bain we continuously accumulate experience with all types of company ownership: publicly traded companies, private equity funds, state owned companies, privately held companies, partnerships and family firms. We acknowledge that none of these tend to think, function or act in at all the same way. Based on our experience and research, we attempted to extract the core learnings from each category of companies. The case of family firms seemed particularly timely.

## WHAT IS A FAMILY FIRM?

This question may seem trivial, but it is trickier than it appears. Philips, Michelin, Nestlé, Heineken, Siemens or Ford and over 25% of the world's largest companies still boast the patrimonial name of their founder, yet not all of them qualify as "family firms". We commonly define family firms as companies where family members hold a significant portion of the shares.

Based on what we've observed, it is also essential to qualify the role played by family in the management of the company. Some family firms have a totally independent management, such as Interbrew, others are essentially family led such as C&A. The extent of family involvement in two key aspects -ownership and management- has profound ramifications; these constitute the potential strengths, but also the challenges, of family firms.




Some Specificities of Family Firms

*"The belief shared by most family firms -regardless of risk- is that the long-term matters more than the short-term"*

## OWNERSHIP

The most characteristic trait spanning all family firms is long-term orientation. While the stock market typically focuses on earnings and growth -exerting relentless pressure on most publicly traded firms- family shareholders usually focus on maintaining and bolstering their heritage. One could say they are balance sheet driven, rather than profit and loss driven.

In difficult times, family firms display greater resilience than publicly traded companies, mainly in their ability to tough out the storm and sit tight, in anticipation of better times. In highly cyclical businesses, such as trading of commodities, the ability to adopt this kind of behaviour can be critical.

**Attitude to Risk**
Family firms' attitude towards risk varies widely, from gutsy entrepreneur to ultra conservative bondholder. However, the belief shared by most family firms -regardless of how risk averse they are- is that the long-term matters more than the short-term. In the current state of affairs, one wonders whether capital markets could reward companies displaying such long-term perspective.

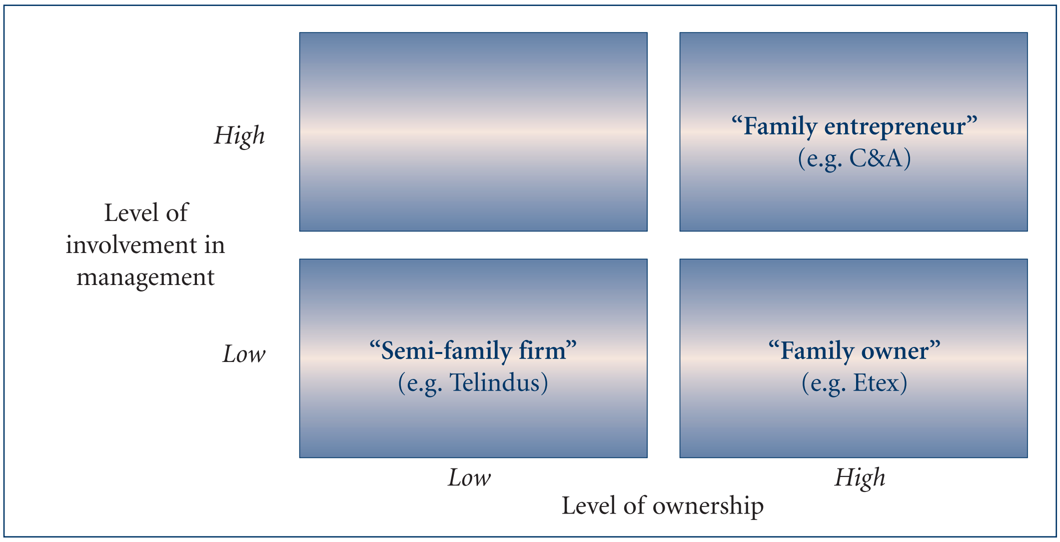
**Capital Control**
Access to capital is frequently an issue. The desire to maintain full control is often strong, and the fear of opening up the firm's capital, which could ultimately expose too many details on profits including how much the family actually makes, can lead to curtailing the growth of promising businesses. Possibly even compromising future industry leadership and survival.

**Shareholder Yardstick**
Possibly one of the biggest advantages of being publicly quoted is the free service rendered by all types of analysts scrutinising the company's share prices, market, competitors, customers, even employees and capabilities. The daily quotation becomes a permanent -albeit external- dashboard or, at the very least, a predictor of future business performance. The absence of such a yardstick often leads public opinion to the conclusion that family firms are under-performing. Recent studies have proven this perception wrong.

**Freedom and Independence**
The flip side of this argument, and another valuable characteristic of family ownership, is independence of action. Family firms cautiously consider the trends driving the stock market -e-enablement, convergence and the like- but rarely feel pressured to please the market. Along the same lines, fast decision making remains perhaps the greatest, most distinctive asset of family firms. The CEO of a family firm can fly in the morning, visit a company, acquire it in the afternoon, and discuss the next acquisition the following day.

# Inspiration

## MANAGEMENT MYTHS AND REALITY




Role of Family

We will not delve into succession issues, which many have extensively studied and documented. In our view, the bottom line is that family members can contribute immensely to their company's growth, provided a number of factors are defined and respected.

**Explicit Rules of the Game**
Family firms tend to suffer from the difficulty of attracting talent, a problem that isn't generally their fault. The main reason behind this: non-family members joining the firm fear they will not enjoy equal access to management information, broad enough job responsibilities, or chances for promotion. In response to these concerns, many family-owned firms go out of their way to show that this is not the case. They realise that, more than any other type of firm, they must explicitly state and live by an HR policy that will make people development a core value, and create attractive career tracks and compensation. As a subset of this policy, it is essential that family firms recognise that, while family members may be offered key positions, there should be no compromise on the specific competencies required for the job.

**Leveraging the Family Members' Potential**
Management talent is not 100% inherited. Still, it can largely be acquired, through appropriate career tracks. Family members bring with them a tremendous amount of experience, often acquired by osmosis through childhood exposure to the trade. At the same time, few people within the organisation dare play a mentor role with long-standing family members (given their existing or future power), such as telling them the truth when required. Family members bring a unique set of talents or skills to their job, from the high IQ scholars who land strategic development positions, to street fighters with no university degree who become inspiring leaders when well advised. Finally, families must make it a real point of honour not to assign incompetent family members to key positions.

*"The inspiration generated by prominent family members still running the company represents a huge asset"*

**Ambassador of the Firm**
Employees, customers, unions, potential partners, all value direct contact with family members. The latter carry the roots of the company, its fundamental values, plus some real decision power, or at least access to the top. The inspiration generated by prominent family members still running the company represents a huge asset. The symbolic personification of leadership and authority can be leveraged for the benefit of the company.

**Clear Organisation and Respect**
For a variety of reasons, the organisational structures of family firms are not always transparent. In many cases, when family members overextend the scope of their job or bypass hierarchy, no one stops them. Over time, such behaviour can weaken or even jeopardise the company's structure, and demotivate some of the stronger individuals. More than anyone else, family managers must demonstrate the greatest respect for the overall organisation and its processes.

**Financial Transparency**
Finally, in some family businesses we encountered, a culture of keeping secrets -sometimes stemming from the need to remain discrete about the family or company wealth, sometimes in an attempt to protect the company from risky publicity- led to a lack of financial transparency for management. Which in turn led to late detection of underperformance and/or missed opportunities for improvements, or anxiety from the banks in difficult times. Lack of financial transparency also makes it difficult to establish dialogue and trust when discussing alliances with other parties.

**The Best of all Worlds**
When all is said and done, today's companies could learn from the behaviour of family firms. And the lessons are refreshingly straightforward. The value of cautious common sense versus succumbing to market or shareholder pressure. The value of remaining focussed on the long-term, rather than confronting decisions with a survivor's mindset or, worse yet, adopting the latest trend without visualising future implications. In today's economic climate, family firms seem to have a lot going for them. And if they pay vigilant attention to their corporate governance issues, they could well outlive us all.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