CORPORATE GOVERNANCE

6 Traits of Strong Family Businesses

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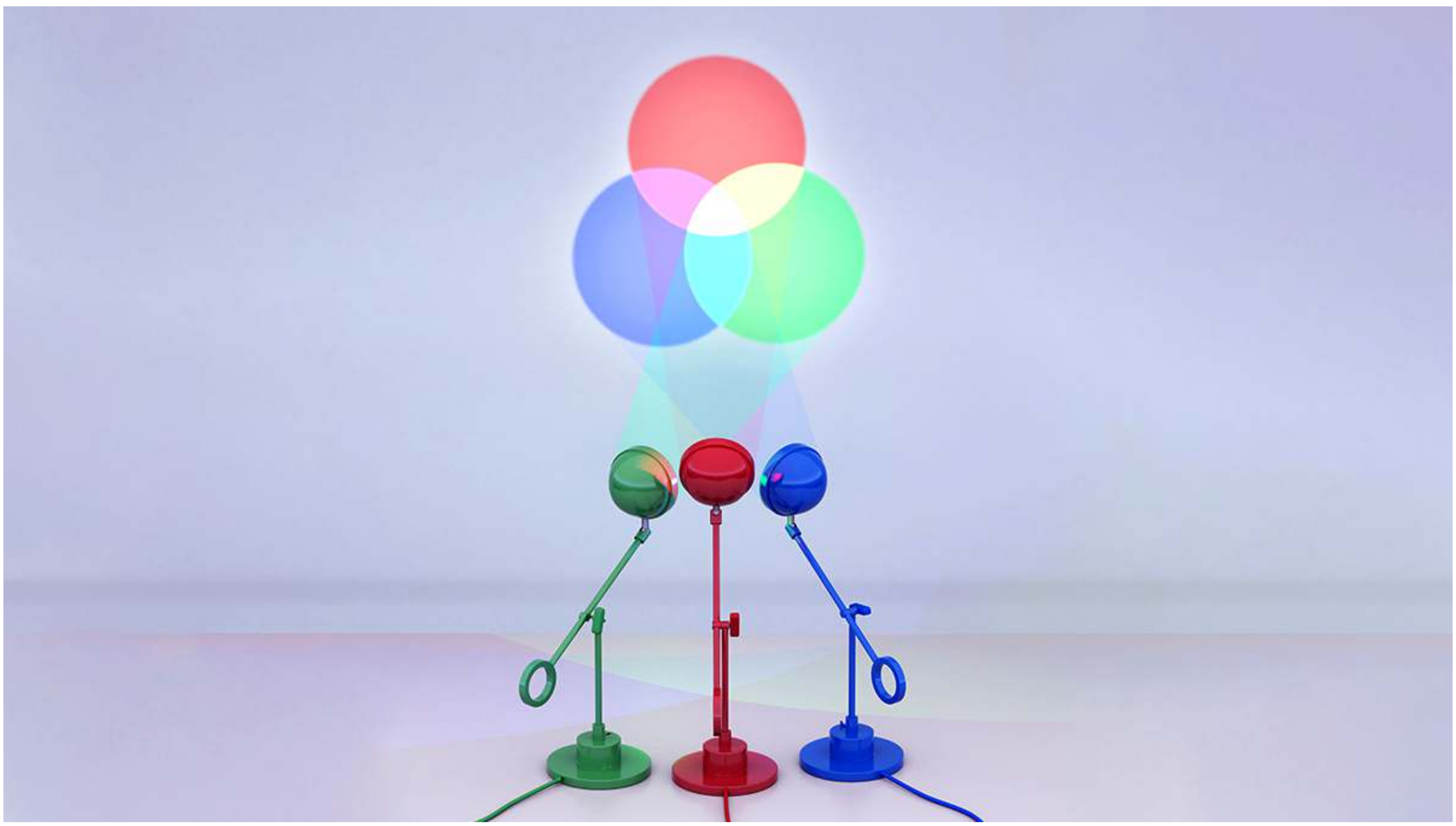

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Family businesses are the cornerstone of most national economies, according to a recent report by Credit Suisse Research. They can create jobs, spur innovation, and drive superior returns.

However, as we highlighted in this 2015 HBR article, such success can only be achieved by following four rules: maintain good governance, identify and develop both family and non-family talent, pursue disciplined succession, and preserve family gravity. We had originally associated the latter with having at least one but up to three family members keeping a strong presence in the firm. But clients kept asking us for more detail. And so, with the Family Business Network International (FBNI), we embarked on a three-year global study to discover what makes up "family gravity."

Our research included interviews with more than 50 executives at 28 leading family businesses across the Americas, Europe, and Asia, a survey of 4,000 FBNI members, which yielded 308 case studies and detailed analysis of 15 family businesses from a wide variety of sectors around the world.

We concluded that "family gravity" is comprised of six elements.

First, families must have a **values system**, which unites members and provides a common framework for building relationships with the business and the community. This gives the organization a moral center that helps sustain it in the face of challenges and difficult decisions and provides a powerful way to differentiate itself in the marketplace.

The **vision for the future** is a clearly defined and communicated vision that guides the family's actions. Such shared vision is particularly important in the current business environment, when ambiguity and complexity can be high and incremental improvements are rarely enough. It allows a business-owning family to set goals and determine priorities.

Families must have clarity on the level of its own **involvement** and how much information-sharing will be necessary to ensure that everyone can carry out his or her responsibilities and be a positive force for the business.

They must also demonstrate **cohesion and interaction**: mutual understanding, respect and support, and a healthy exchange of ideas and discussion of key and delicate issues. This determines how resilient the family will be and how it will respond to change.

Good **family governance** means ensuring that decisions are made and authority exercised in accordance with established and accepted best practices so as to avoid conflict, commit to professionalism and attract and retain superior talent.

Finally, **leadership principles and roles** are clearly defined for all executives of a certain level, whether operating within our outside the company.

We found a strong correlation between these elements and financial success. However, we also found that, among medium to large family businesses, with yearly revenues in excess of $500 million, a full 40% underperformed in at least in three out of the six areas.

So what should they do to remain healthy and viable? The first step is to diagnose where you stand on each dimension. Next, take steps to bolster yourself in the areas where you are weakest.

For example, in establishing a value system, you can begin to identify them, then connect them to the business, then articulate and integrate them. The ultimate goal for vision is to continually incorporate it into the company and individuals' lives. Consider Henkel, founded in 1876 and, as of this writing, one of the largest listed family firms in Germany with revenues of around €20 billion. With 53,000 employees, the consumer and chemical industry company is still majority owned by more than 100 family shareholders. But they are extremely well organized and have a common, unifying understanding of Henkel's future and the role they play in it.

When it comes to cohesion, family businesses should move toward formalized information flow, regular forums, and professional conflict management. At LEGO Group, one of the world's leading toy manufacturers, now in its third generation, with a revenue of €4.8 billion and 15,000 employees, family members have consciously divided their activities among various parts of the business. The basis for this is a strong bond of understanding, respect, and support and fostering one another's growth into new responsibilities.

The right levels of involvement based on expertise and interest should be clarified. Governance, including rules on creating a professional board and hiring both family and non-family roles, should be brought up to industry standards. And leadership principles and roles should be proactively defined. An example comes from the Dabur family business, which was founded in 1884 and is one of India's leading FMCG Companies (and the world's largest Ayurvedic and natural healthcare companies) with revenues of more than $1 billion and a market cap of more than $10 billion. The founding family (now in the fifth generation) has a board balanced with its own members, independent directors and management and was among the first in the country to separate ownership from management in 1998. They also have a family constitution that provides clarity on what roles everyone should play; many continue to be owners, but only a select few help to govern it.

Although most family businesses fail to last through the third generation, some are able to thrive. Why? Mastery of all six family gravity dimensions. They have values and vision, the right involvement, cohesion and interaction, family governance, and clarity on their leadership principles and roles.

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