

# **How To Develop A High-Performing Family-Owned Firm**

**(A Four-Stage *High-Performance* Framework)**

## DOUG VERLEY - PROFILE

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## PREFACE

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This work is derived from a *meta-analysis* of a large body of what I refer to throughout the text as *traditional* strategic theories, models and frameworks. Having developed an interest in the *human element* of business, I went in search of family-firm specific strategic theories, models and frameworks, as it is here that I suspected the *human element* would play itself out in the most profound manner. I discovered that the family-firm area of strategic research is comparatively young and that many of the authorities in the area of strategy have only in the last couple of decades began to turn their attentions to family-firms as a unique class of entity.

Although after much effort, I discovered numerous works on family-firms, I also discovered that this area of research is very fragmented, but perhaps more importantly not a main-stream focus in our business schools. I therefore thought that it may be of value to construct a *reasonably* comprehensive body of work that addresses the various stages that a family-firm may find itself in. It is hoped that this would in the very least direct the thoughts of the family-firm practitioner in a more structured manner.

It would be remiss of me if I did not point out that most of the content in this guide is drawn from the research and works of others, with my intention simply being to compile a concise and user-friendly guide that may be of benefit to you. In the absence of proper referencing I must acknowledge the works of: *JP Kotter, D Ulrich, TG Habbershon and ML Williams, M Poter, W Bridges and S Mitchell, G Hamel and CK Prahalad, R Burr and A Girardi, RS Carlock and JS Ward, D Miller, and KJ Moores and JB Craig.*

I hope your enjoy the guide and I wish you luck in your family-business.

### THE IMPORTANCE OF STRATEGIC CONTEXT

Whilst thinking strategically about your business and formulating your business strategic plan are complex processes, this discipline is so much more complex in the family-firm context.

Undeniably critical to the future success of any business, strategy is a multi-dimensional ‘art-form’ which calls on an extensive understanding of business and all of its many facets. This is made even more challenging when one introduces the complexities of people, so amplified in the family-firm setting.

Successful strategy begins with achieving a clear understanding of ‘*the strategic context*’ the business finds itself in. Amongst other things, the strategic context of the business may be:

- *That the business is in decline;*
- *That the business is in crisis;*
- *That the business is in need of transformation; or*
- *That the business is in need of improved performance*

I describe these as the four stages that the family-owned firm may find itself in, and in each stage I describe suitable strategies which the family-firm owner or manager may apply to move the firm toward recovery, transformation and ultimately high-performance.

Family-owned firms constitute by far the vast majority of firms the world over, accounting for more than half of both Australia’s and America’s employment and Gross Domestic Product, yet little acknowledgement is given to this unique class of entity and little is known about why they experience such a high failure rate, whilst at the same time others experience considerable success that often outstrips their non-family firm counterparts.

This guide provides a useful emphasis on entrepreneurs as individuals and the idea that human beings – with their backgrounds, environments, goals, values and motivations – are the real objects of business. The concepts of the individual and human being are considerably exacerbated when set in the strategic context of family and firm.

Reportedly family-owned firms make up 89% of all firms in the United States, employing 62% of the workforce, and creating almost 80% of all new jobs.

Although family-owned firms share many aspects in common with non-family firms the intermingling of firm relationships with family relationships creates numerous unique organisational characteristics and challenges.

The bulk of research conducted within business schools has largely ignored the family dimension in business, in spite of family-owned firms frequently encountering organisational crises, displaying high rates of failure, and obviously being in need of attention and assistance.

A deeper understanding of why family-owned firms experience crises or in certain circumstances may enjoy considerable success promises improved strategic decision-making abilities and fresh insights into how to successfully implement suitable strategies so that all small-to-medium family-owned firms may benefit.

There is no concise, measurable and agreed upon definition of a family-firm, and experts in the field use many different criteria to distinguish these firms. Of the 27.2 million family-owned firms in the United States, sole proprietors comprise the large majority at 17.9 million, with only 5.5 million classified as corporations. Approximately 42% of all employees work for companies employing less than 500 employees, 72% of which employ less than 20 employees. Whilst drawing on the lessons learnt from all sizes and types of family-firms, it is this group of small-to-medium family-owned firms, employing less than 500 employees, that this guide plans to benefit, as it is this group that will be most vulnerable to the common vagrancies of family-owned firms, namely: the founders' lack of business knowledge and experience as entrepreneur, the demands of early-phase growth and family conflict and poor succession planning, and it is this group that is most likely to experience decline or failure with up to 50% of all family-firms experiencing failure within the first 5 years of starting. It might be fair to suggest that large family-owned firms that comprise approximately 121 of the top 500 privately owned Australian companies have progressed well beyond the founder as entrepreneur and are therefore not the focal point of this guide; however intergenerational succession and other key factors will be addressed.

## **THE SIGNIFICANCE OF STRATEGY IN FAMILY-OWNED FIRMS**

Small firm failure is extremely frequent, with up to 50% of new firms failing within their first five years.

The importance of understanding why small-to-medium firms fail or succeed is crucial to the stability and well-being of the economy, particularly when one considers that family-owned firms in the U.S. account for 89% of all firms, employ 82 million people or 56% of the work force and contribute 64% of GDP or \$5.9 trillion annually.

In Australia approximately 67% of all companies are family-owned, contributing approximately A\$3.6 trillion annually to the national GDP and creating more than half of Australia's employment growth. These figures are staggering but tend to align with worldwide estimates of between 65% to 80% for most western economies.

This is of considerable significance, particularly when one considers the following:

1. Small firms are the essential mechanism by which millions, including women, minorities and immigrants enter the economic mainstream of society;
2. Evidence suggests that small firms are generally more innovative than larger firms in terms of innovations per employee, studies revealing that smaller firms have been responsible for 55% of innovations, and 95% of 'radical' innovations over a ten year period to 1998;
3. Recent studies suggest that small firms lead in offering training and advancement opportunities to workers; and
4. Small firms provide insulation against the effects of recession, with large firms laying-off employees when recessions occur, these employees tending to start small firms or are absorbed into the small firm sector. Between 1987 and 1993 small firms created 5.8 million new jobs in the U.S., while large firms experienced a net loss of 2.3 million jobs.

Of particular concern to any would-be entrepreneur would be the chance of success for the proposed firm, and perhaps of even greater concern to any owner-manager would be how best to avoid corporate decline and failure, and how to get his or her firm back on the road to success.

Throughout history families and firms have always existed in tandem. The necessity of earning a living and supporting a family is often the underlying motivation for starting a family-firm. Among the other motives, *lifestyle* and *wealth creation* goals play an important role in whether a particular family member or members choose to start a firm. At the same time that firms provide an income to the family, the family may serve as a critical supply of resources to the firm - paid and unpaid labour, money, space and equipment.

Family-firms, irrespective of scale of operation, legal form, and industry have been the backbone of corporate life across nations, and the cornerstone of economic development.

Family-firm strategy research has largely failed to establish a clear consensus about what constitutes a family-firm. Few have successfully made the connection between entrepreneurship and the family, with early entrepreneurial research seldom acknowledging the underlying family dynamics of the owning family and its effects on the firm. Conversely, the effects of the firm on the family have been entirely overlooked by most entrepreneurial researchers. Early research has tended to focus on succession, firm governance and related structures, and performance, but has failed to identify those important variables and their interrelationships that clearly distinguished family-firms from non-family firms.

#### **DEFINING A FAMILY-OWNED AND CONTROLLED FIRM**

One of the most popular descriptions of the family-firm social system is the *meta-system*, comprising three broad subsystem components – Firm, Family and Family Member Owner and/or Manager.

Efforts aimed at finding the sources of distinctiveness in family-firms have been directed towards comparative studies of family and non-family firms. This approach has revealed mixed results with family-firms being different in some regards but not in others.

Very importantly, it is generally accepted that family-firms aim to achieve a combination of both *financial* and *non-financial* goals.

*It is recommended that it is extremely important to gain a clear definition of success as used by the family-firm owner and then to formulate appropriate strategies to achieve those desired outcomes. It is pointless trying to impose aggressive growth strategies on the owner of a family-firm that is more interested in non-financial goals.*

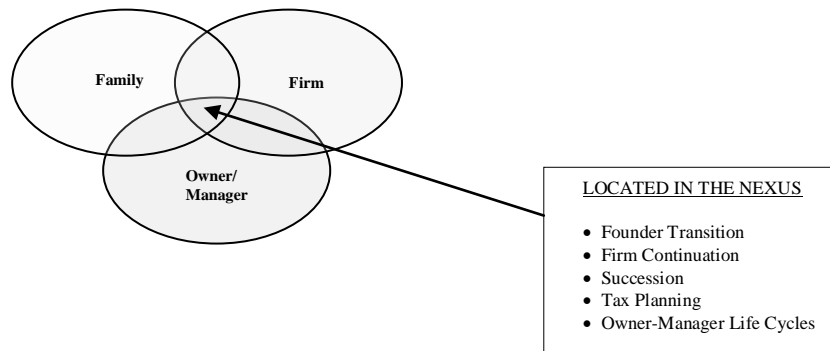
Perhaps the most commonly applied family-firm model is the overlapping three-circles model representing family membership, ownership and managerial roles of internal family-firm stakeholders. It is this overlapping three-circles model which forms the basis to my four-stage high-performance framework for family-firms.

## THE OVERLAPPING THREE-CIRCLES FAMILY-FIRM MODEL

Family-firms are made up of a complex array of systemic factors that impact the formulation of the business strategy and the achievement of targeted performance objectives, which for many years has been portrayed in the three overlapping circles model, as the recognised standard model for picturing the family and firm in an interlinking complex system, as illustrated in *figure 1 below*.

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**Figure 1: Overlapping Three-Circles Model**



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Discussions of strategy and the performance of family-firms frequently refer to the tensions and contradictions that arise between the family system and the firm system. Whether it is the financial decision making patterns of family-firms, their strategic orientation towards market opportunities, or the formulation and implementation of strategy, the tensions between the needs, desires, goals and practices of the family versus the firm are viewed as strategic factors affecting firm performance outcomes.

The overlapping circles model has been used to distinguish the family-firm system as a *distinctly unique strategic entity*, to describe the strategically relevant attributes of each system, to discuss the family-firm's unique strategy making processes, and to explain how each of the subsystems move through stages over time.

Critical strategic management considerations which are peculiar to family-firms are located in the '*nexus*' of the overlapping circles or systems as illustrated *figure 1 above*, these include:

- ***The family-firm founder transitioning from one level of knowledge and capability to the next;***
- ***The successful continuation of the family-firm as it grows and develops from one stage to the next;***
- ***Active and successful succession planning to ensure the intergenerational continuity of the family-firm;***
- ***Effective tax planning for the family and family-firm; and***
- ***Consideration and attention to the owner-manager life cycles.***

The overlapping circles are very useful for describing the complexity associated with the overlapping subsystems of the individual and the organisation, and for identifying the stakeholder perspectives, roles and responsibilities. From a strategic management perspective the overlapping circles model sheds significant light

on the differences between family-firms and non-family firms, however it falls short of being able to explain how these interactions may materially influence family-firm performance outcomes.

The dominant perspective is that the firm is strongly influenced by the family, resulting in constraints on the performance of the family-firm. This dual systems approach emphasises the need to manage the interaction between these two very complex systems in order to develop coping strategies which address the inherent contradictions of each. There are those that stress the equal power of the family and the firm.

***However, it is recommended that the family-firm strategy processes should be an accommodating process that balances the competing and changing needs of the often competing subsystems, family and firm, through time.***

It is important to note that when using the this approach, strategy formulation for the family-firm will be significantly complicated by the need to focus on a series of *trade-off* decisions to manage the overlap between family and firm and their sometimes conflicting objectives.

## **DIFFERENT TYPES OF FAMILY-FIRMS**

Family-firms are not a homogenous group, differing in regard to their ownership and management structures, and the extent to which family objectives dominate. This has far-reaching implications for how a generalised approach is adopted in *thinking of, strategising for and managing family-firms*. It is also important to explore the link between the type of family-firm and its performance goals.

This may best be described in terms of the theory of '*family life-style goals*' and '*family-firm financial goals*'. The theory of family life-style goals does not assume financial goals or economic rationality, and thus may be more applicable to family-firms, particularly small, and especially sole proprietor family-firms. Family life-style goals may encompass pure selfless *altruism*, which is not motivated by financial gain, *altruism* stemming from a loyalty and commitment to family members. Thus in the stereotypical family-firm, the theory of life-style goals would suggest a behaviour that puts the *family first*, a high psychological ownership of the firm and a high level of *altruism*.

Some family-firms do not conform to the theory of life-style goals. For some, the theory of family-firm financial goals is more important. A number of family-firms striving towards the achievement of financial goals may introduce financial control measures such as performance related pay and non-executive directors.

The theory of family-firm financial goals assumes a focus on financial objectives, i.e. the purpose is to serve the financial needs of the firm, i.e. to maximise financial performance.

In considering family-firms and the applicability of either theory or approach there would seemingly appear to be a constant trade-off between the needs of the firm vs. the needs of the family.

Family-firms will exhibit varying degrees of family vs. firm motivation behaviours at differing times and also occurring simultaneously at times. There will also be a differing emphasis on financial and non-financial

objectives, and one may suggest that too will change over time as the firm develops through the various *growth phases and levels of complexity*.

It is very important to note that family-firms may differ to non-familyfirms in their strategic objectives, which may notably include:

- ***The importance of the survival of the family-firm as a going concern;***
- ***The desire for continued independent ownership of the firm and a reluctance to dilute ownership;***
- ***The desire for the transfer of ownership to the next generation;***
- ***The desire to maintaining financial independence; and***
- ***The preference to employ family members.***

As the family-firm ownership progresses from one generation to the next, the structural form of ownership and management will change. Where firms, due to time and growth, are characterised by *increasing complexity* of ownership, shareholdings will become more diverse. Individual shareholders with less control will require extra monitoring to ensure that their interests are secured. This could impact on the *strategic objectives* of the firm and the management structure employed.

Research has found that 73% percent of family-firms exhibited behaviour in-line with the theory of family life-style goals, and 27% in-line with the theory of family-firm financial goals. This suggests *that most family-firms have a bias towards non-financial objectives and serving the needs of the family first*. This may find support in the fact that most family-firms are sole proprietorships or very small, in their early stages of development and survival, with the CEO or head of the firm a family member who will obviously place a greater emphasis on the interests and well-being of the family.

***It is therefore recommended that it is of critical importance when considering and discussing family-firms to realise that success and growth are not universal terms that may be applied to these firms in a generic format, and that in most cases the theory of family-firm financial goals and profit maximisation strategies cannot be applied. It therefore stands to reason that in most instances traditional strategic models, theories and frameworks may not be applicable to the large majority of family-firms.***

## **HOW TO FORMULATING A WINNING STRATEGY IN YOUR FAMILY-FIRM**

In family-firms the interaction between family members plays an influential role in *strategy formulation* and the dynamics in which strategies emerge are deeply rooted in family values and emotions.

The traditional *strategy formulation process* is viewed as sequential steps of strategic analysis, choice and implementation. Contrary to this the strategy formulation processes in family-firms is typically more *informal and unstructured*, where strategic decisions are made in *informal meetings*, including around the kitchen table – *Kitchen table strategy process*, with few participants involved, little influence from external parties, and perhaps more relevant, little use of formal strategic tools such as planning techniques. From this it follows that the

strategy process in family-firms is often characterised as *irrational, unsystematic and non-professional*, where formal channels of communication are seen as something negative.

It is recommended that a formalised approach to strategy-making is necessary for family-firms to thrive and prosper over generations. It is important that the family-firm is viewed as a *special case* of strategic management, requiring a peculiar strategy formulation process that takes the uniqueness of both family and firm into consideration.

It should be noted that the interactions between family and firm have traditionally been regarded as a problem because of the *incompatible logics* of the family system and the firm system, and as an obstruction to the development of the firm.

*Understanding the family-firm and achieving strategic success means acknowledging the interplay and influence of both on the other.* Family values, traditions and ways of thinking, might have a strong influence on the firm, its culture and Long-term prospects. An important characteristic of family-firm strategy is that it is *deeply influenced by family values, goals and relations*, but also that the firm influences the family and its members.

Critical to the formulation of family-firm strategy is the understanding that *family-firm strategy* must be built on the particular dynamics of the family-firm, taking into account, the *micro aspects* of human or family interaction.

*It is Important to acknowledge that strategy is made by human beings, with the forces and activities driving strategic change coming from these humans or family members.*

***It is recommended that strategising in the family-firm must not only acknowledge but must also accentuate the role of the family, the traditions, values and emotions in day-to-day activities and life, as well as the interpretations and interactions of the involved parties.***

***The strategy process in family-firms must emphasize how daily activities shape the ongoing formation, reproduction and transformation of strategic patterns in the family-firm. This will require careful consideration, analysis and interpretation.***

## CHAPTER 2: WHY FAMILY-FIRMS EXPERIENCE DECLINE AND FAILURE

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In order to achieve considerable long-term success or high-performance family-firms must at first successfully navigate from one plane of growth to the next, avoiding decline and failure that plagues so many family firms.

Very little, if any, *traditional strategy* research makes the express connection between the family and the firm as a direct cause of firm decline and failure, citing the most common causes as those in *table 1* below.

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*Table 1: Non Family-Firm Causes of Decline and Failure*

- *Poor management*
- *Inadequate financial control*
- *High cost structures*
- *Poor marketing*
- *Big projects gone wrong*
- *Acquisitions gone wrong*
- *Poor financial policy and management*
- *Changes in market demand*
- *Competition*
- *Government policy*
- *Adverse commodity price movements*
- *Bad luck*
- *Over-diversification*
- *Lack of control*
- *Lack of leadership*
- *Creative accounting*
- *Inability to cope with change*
- *Rapid expansion*
- *Obsolete product*
- *No sense of urgency*
- *Poor cash-flow management*
- *Poor working capital management*
- *Lack of marketing effort*
- *Organisational inertia and confusion*

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Although it may be argued that many of the causes listed in *table 1* above capture some of the dynamics found in the typical family-firm, there would appear to be a lack of acknowledgement of any causes that could be considered peculiar to family-firms.

In his book *The Icarus Paradox*, Miller makes reference to the entrepreneurs skills as the business ‘*Builder*’, required to identify and exploit opportunities faster than competitors, sighting such companies as: Google; Ryan Air; EasyJet; and Vodafone. Miller suggests that these ambitious and sometimes *aggressive* personalities become fixated on their goals and they often make the mistake of:

- *Over expanding;*
- *Over diversifying;*
- *Adopting creative financing;*
- *Becoming ritualistic; and*
- *Ultimately reckless and overburdened.*

Other popular authorities makes reference to a *larger than life CEO* that is lauded by the community and media, and those organisations which suffer a *culture of conflicts*, hiring relatives, contracting with companies owned by relatives, and generally using the company for family and friendly profit. These firms are usually characterised by:

- *One man rule;*
- *Management succession problems;*
- *Inbred bureaucratic management;*
- *Unbalanced top team;*
- *A non-participative Board;*
- *A weak finance executive;*
- *A combined chairman and CEO; and*
- *A lack of management depth.*

However, these causes of firm decline and failure still fall short of acknowledging the complex family-firm mega-system, and how it may be a specific cause of decline and failure.

#### **FAMILY-FIRM SPECIFIC CAUSES OF DECLINE AND FAILURE**

The success of the family-firm depends on the effective management of the *overlap between family and firm*.

A mismatch in the definition of success or goals that different stakeholders strive to achieve for the family-firm could point towards a tenacious source of conflict.

It is argued that *the greatest threat to family-firms* is not out in the marketplace, but within the family-firm itself. The majority of failed family-firms report *considerable stress related to managing family-firm relationships*. Family-firm researchers have uncovered trends that underlie this stress. Some of the key issues that these researchers have highlighted as problematic for family-firms include:

- *Governance structures;*
- *Succession planning;*
- *Under-representation of family members;*
- *Adding outsiders to the system; and*
- *Problems related to conflict and conflict resolution;*

- *Marital Problems;*
- *Poor parental and employee relationships; and*
- *Poor communication.*

The most common causes of decline and failure in family-firms which must be considered at all times and taken into consideration when thinking strategically and formulating your family-firm strategy are:

### **A Too Strong Family Orientation**

A strong family orientation may result in a firm strategy that accommodates the preferences of the founder or other family members, even if that strategy is not sound. For example geographic expansion may be based on the need to create an opportunity for a son wanting to move to a particular city, rather than a thorough analysis of that region. Companies often continue particular products or services, or even the company itself, in honour of the founder, even when it no longer makes sense to do so.

Family-firms also vary in the *resources obtained* by the firm. Thus, whereas some firms might focus on rational choices, such as the most qualified people or best materials for the price, other family-firms may make decisions based on family or historic considerations.

In firms run by cohesive families with a strong family orientation, especially where the firm orientation is weak, family demands may take precedence over firm demands to the extent that assignment of key roles, access to information and decision-making responsibility is given to family even when they may be less qualified to carry out the job, leading to poorer decisions and firm outcomes. This may culminate in the tolerance of low quality work by family members impacting customer satisfaction and the long-term health of the firm.

### **Failed Family Relationships and Family Conflict**

Conflict between family members, or between family members and non-family employees, is a major source of family-firm failure. Family-firms 'not only invite an intensifying stress on the tensions already evident in the family but intrude on the differences that arise from the subjectivity of determining life paths. Five *bad news scenarios* that lead to conflicts in family-firms include:

- *Incompetent family members chosen to run the firm;*
- *Spoiled kid syndrome;*
- *Increased marital conflict;*
- *Entrepreneurial aggression; and*
- *A tendency towards autocratic rule.*

A successful firm may be tied to a family that is tension prone or exhibits failed family relationships. Relationship issues are often central to the success and sustainability of the family-firm, as good relationships

can overcome bad or difficult firm conditions but bad family relationships marred by tension and conflict often have damaging consequences for the family-firm. This is because unlike non-family firms, relationships in the family-firm are tightly linked, wherein the tremors of one or more bad relationships are felt throughout the entire family-firm, impacting all areas of the firm.

Conflict may be described as incompatible wishes, or irreconcilable desires. Three types of conflict may exist, namely:

- **Task – disagreement on what tasks should be accomplished;**
- **Process – disagreement on how to accomplish such tasks; and**
- **Relationship– based on interpersonal incompatibilities about values, attitudes, and so on.**

A neo-Darwinian perspective of the type of relationship forces often to be found in family-firms suggests that, on the one hand the genetic bonds pull people together by ties of affection and dependence; however, at the same time there are inherent conflicts. The parent-child relationship typically involves a pull between the interests of parents seeking to shape and control their offsprings' destiny, and the children seeking to grasp autonomy and resources to enable them to determine their own destiny. Parent-child partnerships are a familiar phenomenon in the family-firm scene, and they may enjoy long periods of stability; but mostly it is an evolving relationship that requires continual mutual adjustment, which may prove difficult to implement.

Siblings are also often locked into a conflicting relationship of love and rivalry, which often plays itself out in the family-firm setting, particularly around succession.

### **Poor Succession Planning**

One of the most common reasons for failure is failed succession. Often seniors fail to, or are reluctant to, withdraw and successors, who may be growing impatient for leadership, are not adequately mentored. This problem is pronounced when the age gap between father and son is modest; the parent not being ready to let go and the child becoming increasingly impatient for an opportunity to lead and take responsibility. This situation is further complicated in the case of self-made entrepreneurs, a group who are said to find it most troublesome to create reciprocal mentorship-style relationships, owing to their autonomous personality styles.

Succession is often complicated when there is more than one heir to an estate and the firm becomes a point of contention, sometimes leading to conflict and the demise of the firm. It should be noted that family-firm complexity increases with each succeeding generation, with less than 30% of firms making it to the second generation.

Due to their long tenures, family-firm founders and CEOs possess considerable *on-the-job knowledge* related to the firm. The performance of the next generation is largely dependent on the effectiveness with which this knowledge and social networks are transferred across generations. Therefore the absorptive capacity of the recipient and the nature of the relationship between the source and the recipient are critically important. It therefore stands to reason that the level of preparedness of the next generation and its relationships with the

senior generation will have a significant influence on the next generation's performance in the family-firm. A supportive relationship and mutual respect enables the smooth transition of knowledge, social capital, and networks across generations, with the contrary obviously holding true.

It should be understood that potential family successors provide a rich emotional reservoir to be drawn on for the future benefit of the firm, and if done astutely their attributes and emotional capital can make a difference between the future success, or failure of a family-firm.

Succession problems have been described as one of the main factors that tend to weaken family companies, whether because of the psychological profile of a powerful leader, the dynamic relationship between father and son, the loss of leadership, or lack of planning.

*It is recommended that despite the central position of firm leaders, given their emotional involvement with the next generation and their parenting rationalities, leaders may not be in the best position to accurately assess either the list of desirable successor attributes or the extent to which members of the next generation possess them. Furthermore, the human resource pool of the owning family may be limited or eventually outstripped by the demands of a growing firm, requiring the sometimes tough decision to look outside the firm and family for potential successors.*

### **The Death of the Business Leader**

The death of the founder is reportedly the catalyst for the downfall in 78 percent of family-firm failures. It is often seen that when the founder lives to retirement it is sometimes difficult for that founder to turn over the reign of leadership, leaving the family-firm in crisis at death.

### **An Inappropriate Organisational Structure**

*Organisational structure* is a common cause of decline and failure in family-firms given the need of the entrepreneurial founder and family to maintain close control over the firm. This leads to an overly centralised structure with power and decision making vesting in a few family members. Work flow and the smoothness of tasks are impacted, being often difficult to detect until things go wrong. *Role conflict and role stress* may provide evidence of poor structure. Signs of coordination problems may include slow or inaccurate fulfilment of customer orders or work slipping through the cracks. Information flow and the decision-making responsibilities are often aspects of effective work-flow. Information may also flow differently as a result of the family dynamics, passing outside the formal chain of command and with the possible consequence, for example, that one or more senior non-family managers may be left out of the loop.

The differentiation between family and firm mainly involves economic relations and human resource policies regarding family members. Applying special human resource criteria to family members would ultimately prejudice the company.

### **An Increase in the Complexity**

An increase in the number of shareholders leads to differences regarding *objectives and values*, making it *difficult to build a dominant coalition* capable of effectively leading the company and navigating difficult times. This leads to the general loss of confidence of the various players. The extension of family equity implies a loss of shareholder commitment to the company, and an eventual loss of entrepreneurial capacity and potential decline and failure of the firm. The energy absorbed by the firm and family systems to keep working increases as the firm grows. Hence, the growth in family complexity can lead to family-firms losing competitiveness or *closing in on themselves*.

As the family-firm develops its growing complexity may present the family with an ever increasing challenge, a challenge that may outstrip their collective ability to cope and manage such complexity. Such complexity may include processes, products, markets, internationalisation, technology, financing, regulation and the like.

***It is therefore recommended that it is vitally important that as the firm grows and becomes more complex that the family develops additional communication channels, so that it can maintain the necessary cohesion and ability to adapt to such change and manage the firm successfully.***

### **Difficulty in Attracting Superior Skills**

In comparison to employees in non-family firms, family-firm employees need to manage *dramatically complex dynamics* even for performing simple transactions, thus explaining why so many individuals may prefer to not work for family-firms, thus making it extremely difficult for some, if not most, family-firms to attract superior skills to ensure their continued success.

### **Altruism**

Altruism presents a potentially very damaging risk to family-firms. The extent of self-control exhibited by far-sighted founders differentiates them from those suffering from short-sighted *myopic altruism*. Myopic altruists are unable to resist the need to satisfy the immediate gratification of each and every family member in favour of the long-term good of the firm, thus violating rules of procedural and distributive justice, leading to their being perceived as unjust by family and non-family members which, in turn leads to conflict and a lack of commitment to the firm. Furthermore, altruism may lead to adverse selection and entrenchment in family-firms of family members that are not suitably qualified for the needs or challenges of the position.

Moreover family members may engage in shirking or free-loading behaviours to the detriment of firm performance due to a lack of enthusiasm or commitment or a feeling of entitlement.

### **Long CEO Tenures**

Family-firm founding leaders have been recognised as having a significant influence on cultures, values and performance of their firms. As compared to non-familyfirms, the tenures of family-firm leaders have been found

to be far longer, on average up to three times longer than their non-family counterparts. These long tenures have been attributed to these founder CEOs facing higher cognitive costs and psychological barriers to exit. Whilst some remain energetic and rejuvenated throughout their tenure others are reported as experiencing loneliness and boredom in their positions, resulting in the gradual decline of the family-firm, and yet they won't relinquish their position and control.

### **The Spouse: *Tensions and Attributes***

Tensions that occur between spouses often centre on resources such as the allocation of finances, the distribution of time across the family and firm, or the energy and commitment provided to either the family or firm. Firm and family finances are linked within the family-owned firm, especially in the early stages of the firm. Owing to the economic bonds of marriage, a spouse becomes a critical stakeholder in the family-firm. In addition entrepreneurs often consult with and are influenced subtly by their spouses, with around one in seven family-firms considering themselves to be co-led by the spouse.

Regardless of the spouse's degree of direct involvement or participation in the firm, spousal attributes, such as commitment, enthusiasm and support permeate family relationships and can affect firm performance by influencing the entrepreneur's attitudes, resources and motivation towards the firm. The nature of the marital relationship may adversely affect the health and achievements of the family-firm and in the most extreme case, *divorce* may spell disaster for a perfectly healthy and successful firm.

### **Intermingling of Finances**

Two-thirds of family-firms intermingle household and firm finances, indicating that those finances are inextricably intertwined. The intermingling of family-firm finances leads to the inability to capture the interchanges in the financial records of either the family or the firm. The lack of such data, while confusing for the family's financial picture, may be catastrophic to the firm. Simply put the firm may not know if it is making a profit and growing or if it is performing poorly, and has entered decline.

### **Power and Status: *One-Man Rule***

Power and status, or one-man rule, in the family-firm context is amplified as often the dominant CEO is also the family figure head, exercising complete unchallenged control over the complete meta-system.

### **Misallocation of Money and Other Scarce Resources**

Money can create a source of conflict and misunderstanding, especially between passive owners and family members working within the same family-firm, with the former often expecting some form of dividend for their shares while the latter often see greater need to keep funds reinvested in the firm to assure long-term survival and growth.

This misallocation of often scarce and valuable resources often takes place, with the ‘squeaky wheel’ that complains the loudest getting the required resources. Often family-firms apply informal budgeting processes and controls, this phenomenon being accentuated by the family-firm assigning a family member – even one not thoroughly trained for the position – as treasurer or bookkeeper, in order to keep a close eye on the family’s assets.

### **A Focus on Business Objectives as Lifestyle**

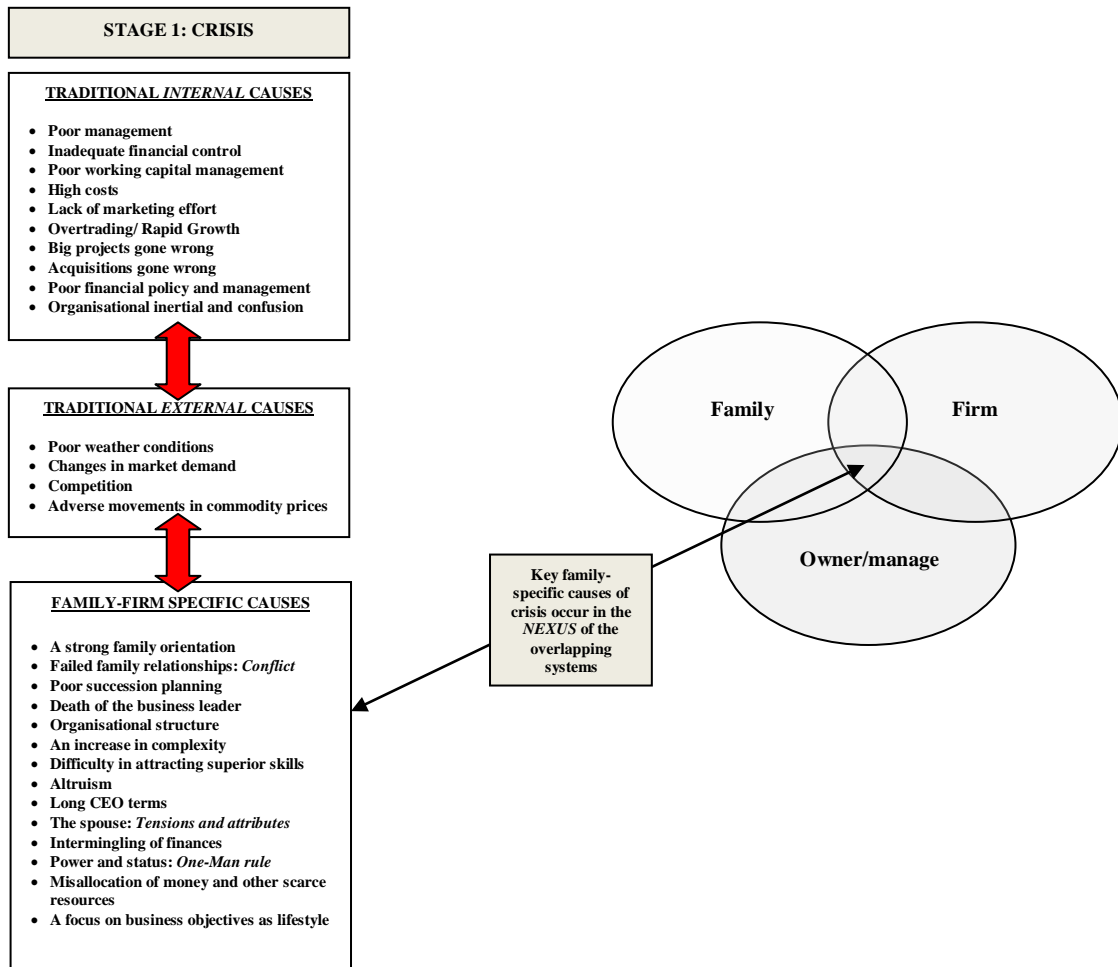
Family-firms that do not focus on wealth creation or financial goals in the long term may struggle to compete, threatening their continued existence. Also, family-firm performance may suffer because founder-owners focus on maintaining or enhancing their lifestyle.

Critical to a family-firm’s success and survival is its ability to balance and integrate the demands or needs of the family and firm, and often the disparate needs of family members. Families who can balance the family and firm systems create a positive environment where the family thrives and the firm performs well. However, it is not a simple task to balance the objectives of both the family and the firm, especially when the orientation towards both is high.

### **STAGE ONE OF THE HIGH-PERFORMANCE FRAMEWORK**

At this stage we may conclude that there are a number of both, generic or traditional causes of business crisis and failure as well as a number that are peculiar to family-firms that find their origins in the extremely complex nature of the family-firm overlapping mega-system. By combining these traditional family-firm specific causes of decline and crises I present the first stage of the *four-stage high-performance framework* which clearly sets out a comprehensive list of causes of decline and failure that all family-firm owners and managers should be acutely aware of at all times, and should constantly consider in the strategic thinking and planning process. Stage one of the four-stage high-performance framework is presented in *figure 2* below.

Figure 2: Stage 1 of the Four-Stage High-Performance Framework - Crisis: Reasons for Decline and Failure



## CHAPTER 3: HOW TO TURN YOUR FAMILY-FIRM AROUND AND GET IT BACK TO GOOD HEALTH

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As illustrated, family-firm crises can be attributed to many causes: *internal traditional causes*, *external traditional causes*, and *family-specific causes*.

If we assume the cause of crisis to be family-firm specific, i.e. the death of founder or family conflict, or to be due to considerable external causes, i.e. a sudden change in legislation or a dramatic economic event, for example the recently experienced Global Financial Crisis, what *turnaround strategies* would the family-firm initiate, and how?

Popular theorists make recommendations that are in practice often not possible, or at best in appropriate. For example some make the recommendation to change the CEO and other senior management, which in most family-firms would be both not possible and often inappropriate due to the unique cause of crisis. It may also be said that in most family-owned firms the founder-CEO is the custodian of considerable *on-the-job knowledge and networks* necessary to the achievement of a successful turnaround, even when the causes are more traditional in nature.

**Table 2** below sets out a summary of the *traditional turnaround strategies* and recommendations as provided by leaders in this area of study.

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**Table 2: Recommended Traditional Turnaround Strategies**

- *Stabilise the crisis*
  - *Change the CEO and other management*
  - *Achieve stakeholder support*
  - *Achieve strategic focus*
  - *Implement organisational change*
  - *Implement critical process improvements*
  - *Restructure finances*
  - *Stop the bleeding*
  - *Adopt a cash management policy*
  - *Accumulate data*
  - *Determine who is going to play*
  - *Assess manufacturing capabilities*
  - *Create a playbook (business plan)*
  - *Set realistic goals*
  - *Create an idea generating process*
  - *Create a war-chest (Cash)*
  - *Show demonstrable progress*
  - *Assemble a turnaround team*
  - *Develop a survival plan*
    - *Gain information*
    - *Select a survival retreat*
  - *Develop a resurrection plan*
    - *Gain information*
    - *Analysis the business*
    - *Assess profit contributions*
    - *Consider the options*
  - *Reduce overheads*
  - *Manage payables*
  - *Manage receivables*
  - *Downsize if necessary*
-

*As a starting point it is recommended that immediate attention be paid to stabilising the firm, achieving stakeholder support, achieving a rapid strategic focus and implementing organisational change.*

### **Stabilise the Crisis**

It is recommended that in most turnaround situations crisis management will have to commence immediately, and is preceded by a worsening cash position or management that is out of control. The need is for *rapid action* and the approach requires very *strong top-down control*.

### **Achieving Stakeholder Support**

Troubled companies typically suffer from poor relationships with their key stakeholders. Often these poor relationships can be largely attributable to poor or ineffective communication with key stakeholders.

In a turnaround it is necessary to decide: *What to communicate, How to communicate, and to whom and where.*

### **Achieve Rapid Strategic focus**

Substantially under-performing companies often *do not have a well-conceived and communicated strategic plan*, and generally face one or more serious strategic problems.

The lack of a formally documented and clearly articulated strategic plan results in confusion across the firm, and the lack of a common set of goals and a clear direction. It is recommended that the family-firm revisit and where necessary redefine the strategic goals and objectives of the firm in turnaround.

### **Implement Organisational Change**

People problems are usually among the most visible signs of a troubled company. This may be attributed to:

- *A confused organisational structure;*
- *A paralysed middle management;*
- *Resistance to change;*
- *A Lack of key skills and capabilities; and to*
- *Demoralised staff.*

As the causes of family-firm crises resides in the area of overlap between the family and firm systems - *the nexus*, so too are the catalysts for bringing about the required change and averting a crisis in family-firms located here. It is at this overlap that the resources and supportive relationships will be found that are required to successfully manoeuvre through such crisis.

As family relationship issues are so central to the stability and success of family-firms and so often the cause of decline or crisis it is essential to establish the *stability and emotional capital* to provide the fuel required to effect a successful turnaround. The survival of the firm is dependent on family and non-family firm members

developing support mechanisms aimed at mending family relationships, stabilising the company and moving it towards recovery.

*It is recommended that families adopt the conflict management strategies of collaboration, compromise and accommodation in the family-firm, with collaboration strategies performing most favourably, providing positive outcomes on both family and firm dimensions.*

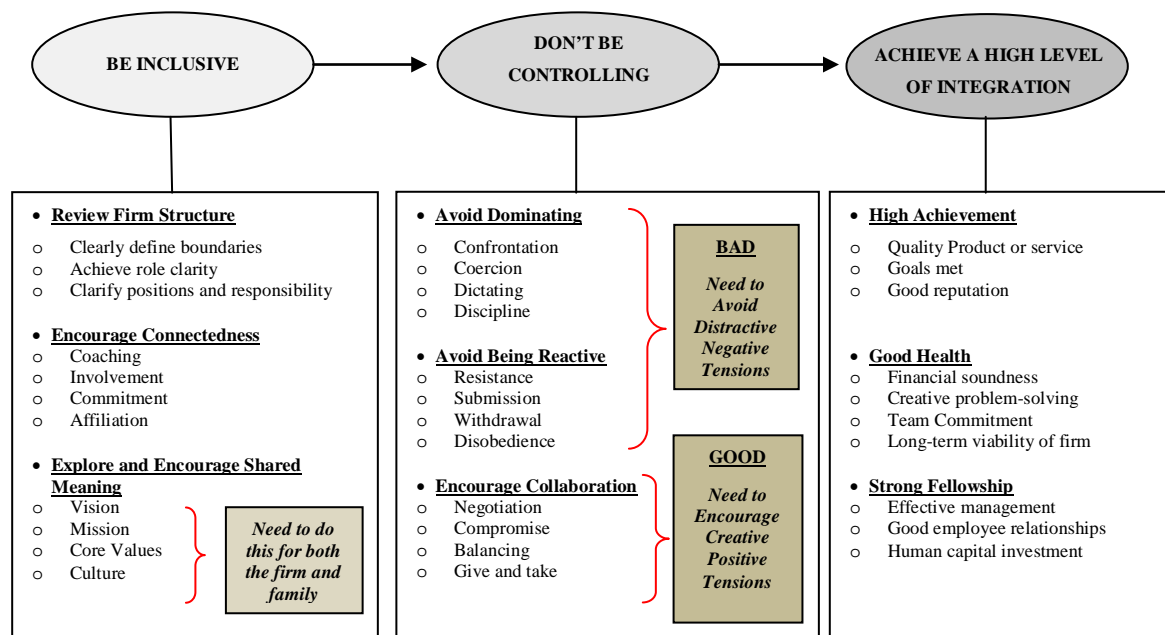
It is extremely important that the family capture their clear *strategic intent* both for the family and for the firm. This may be referred to as the vision for the family and the vision for the firm. There must be congruence in both and the family must have the ability and the desire to sustain both over time.

*It is recommended that in decline or crises it is important to create a sense of urgency and to form a guiding coalition. Besides providing an extremely committed coalition, family can also provide financial resources, emotional support, knowledge and physical assistance in helping the family-firm to survive. Therefore in times of crisis the heads of the family-firm would be well advised to turn to the family guiding coalition.*

In times of crisis family-firm leaders should strive to achieve a high level of inclusion by all members in the family-firm and avoid be overly controlling and autocratic.

This is best illustrated in **figure 3** below which provides a means to examine more precisely the *resources and interpersonal interactions* that may occur during crisis and change in a family-firm.

**Figure 3: Resources and Interpersonal Interactions During Family-Firm Crisis and Change**



A sense of inclusion in the family-firm by all family members and the manner in which control is exercised has an important and far reaching impact of the level of family-firm success achieved.

***It is therefore recommended that the family-firm leaders be inclusive and exercise a collaborative management and leadership style, making all feel valued in the family-firm.***

The inclusion dimension is therefore not just about structure. It is not just about who is part of the family-firm, but it is also about how and to what extent family members are connected to the family-firm, and the degree to which there is shared meaning among family-firm members. It is recommended that during times of crisis that the organisational structure, role clarity, and clarity of positions and responsibilities be reassessed and reconstructed within the family-firm to manoeuvre through any crisis or change successfully. If the subcategories of inclusion are not reconstructed or alternatively cannot be reconstructed to respond to such crisis or change, further conflict and stress will result, affecting the firm and its ability to recover from such crisis.

Included in the inclusion dimension is the need for the family to also consider the shared meaning of the family system over and above that of the firm system. As the fundamental cause of most crises in family-firms is deeply rooted in family dynamics and often conflict, it is imperative to pull together as a family, to resolve any family conflicts and to establish the shared meaning and purpose of the family first.

The control dimension reflects the responses to crisis or change among the family-firm members. Control refers to interactions that concern influence and power that people hold during times of crisis. The responses during the crisis process include tensions resulting from the disruption. Those tensions may either be creative positive tensions or distracting negative tensions as indicated. Creative positive tensions, for example collaboration, project the current reality within the firm toward the vision that family-firm members hold for the firm. These creative positive tensions create energy, excitement and enthusiasm that motivate the family members to engage in behaviours and actions that address the firm issues and lead to success. Distracting negative tensions, for example domination or reaction, focus the family members' energies and emotions on the conflict or cause of the crisis and not on how to solve the company's problems, preventing the company from recovering from such crisis.

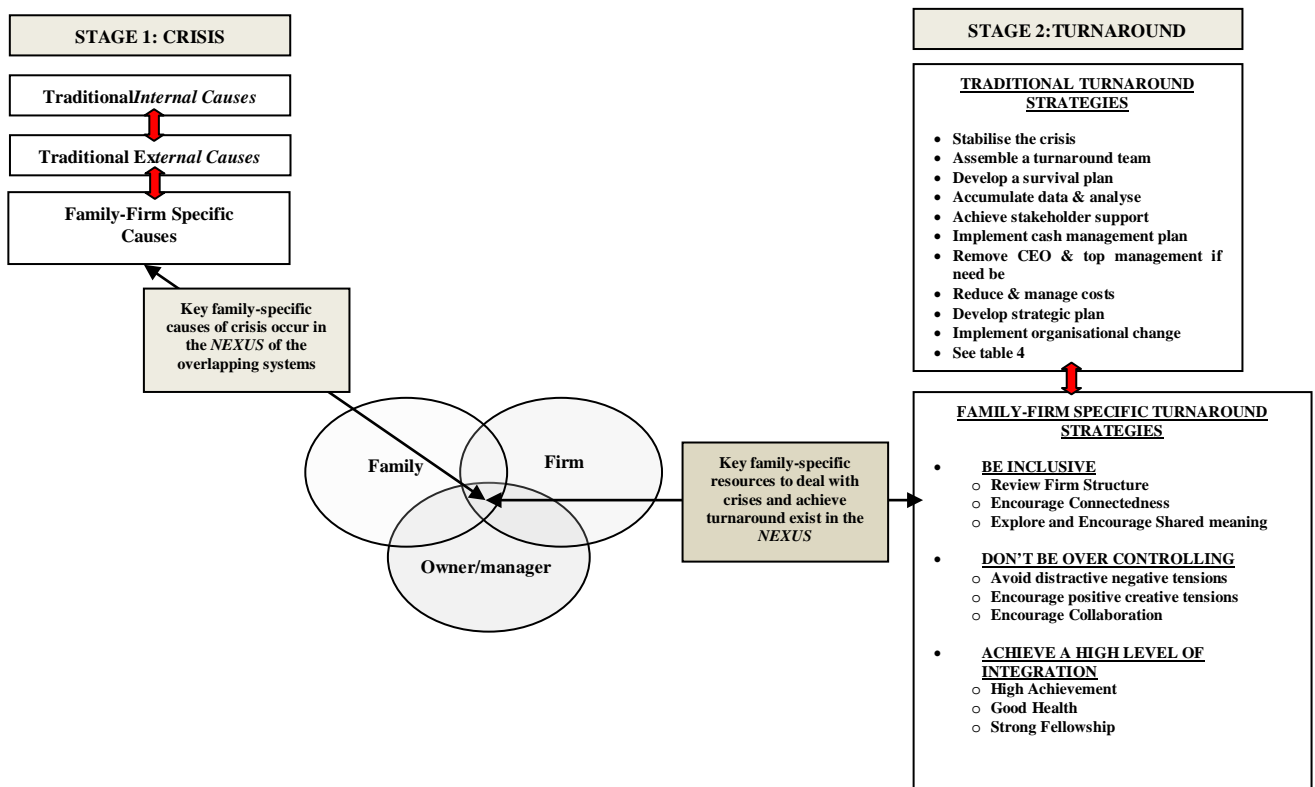
***It is therefore recommended that in order for the firm to emerge from crisis and move towards success, i.e. the integration dimension, defined as high achievement, good health and strong fellowship, family-firm leaders must revisit and reconstruct the inclusion dimension components in a way that minimises the level of distractive negative tensions, and maximises the level of creative positive tensions. Again it is recommended that in most cases this would require the intervention of an external party or parties to successfully facilitate such process as existing inclusion and control dynamics will most likely be deeply embedded in the family and family-firm culture, difficult to identify and challenging to address.***

## STAGE TWO OF THE HIGH-PERFORMANCE FRAMEWORK

It is difficult to deny that family-firms are both unique and subject to numerous additional potential causes of crisis. However, it is also evident that family-firms have additional resources at their disposal to deal with such crises.

There are a number of both traditional and family-firm specific strategies that may be applied to achieve a family-firm *strategic turnaround*. By combining these strategies and recommendations, the second stage of the *four-stage high-performance framework* may be derived, providing a more comprehensive list of step-by-step turnaround strategies which the family-firm may take into consideration when trying to deal with a crisis and achieve strategic turnaround, as illustrated in *figure 4* below.

*Figure 4: Stage 2 of the Four-Stage High-Performance Framework: Turnaround Strategies for Family-Firms*



As companies progress from one phase to the next in their natural life cycle, or as the environment within which they operate changes, they need to transform themselves if they are to survive, prosper and ultimately develop into high-performers.

The family-firm founder is central to the *transformation process* in most family-firms and by his/her very nature is reluctant to let go, share power or embrace change. A significant amount of the *traditional* theory focuses on the *why* and *how* to lead the company and employees through a process of transformation, with limited focus on successfully encouraging company leadership to embrace change and *how* to guide and assist leadership through this very difficult process. Experience suggests that family-firm leaders are uncomfortable with the subject of succession, possibly as it addresses the realities of their own mortality and the need to let go of what has often been their life's work.

The challenge of initiating and embracing change and transformation is often exacerbated in the family-firm system as the *business leader is most often also the family leader* and thus as change permeates through both sub-systems, this can be a considerably disenfranchising and difficult experience for the business and family leader.

It is important to acknowledge that organisations must also have the courage to change. Even if the present is great, the future is just around the corner. Organisations must bring-in *new blood* at all levels, encouraging them to *challenge the conventional wisdom* and way of doing things.

In order for the family-firm to achieve successful transformation it is important to differentiate between *transformation* or change and *transition*. *Transition* is the state that change puts people into, with *change* being external: policies; practices; or structure, *transition* is internal or the *psychological reorientation* that people have to go through when change takes place, and before change can be successful.

Transition requires that people undergo three separate processes, all of which are extremely challenging:

- ***Saying goodbye***– The first requirement is that people have to let go of the way that things, and worse themselves, used to be. One can well imagine how difficult this must be for the typical family-firm founder and leader, having to now relinquish the past so that the firm may move forward;
- ***Shifting into neutral***– That space between the old and the new, no-man's land. This space could be extremely disconcerting for the entrepreneur family-firm founder and leader who has grown used to the old ways, often centred around his idiosyncrasies and way of doing things, now having to adapt to new ways of working with others, communicating, planning, reporting and taking decisions; and
- ***Moving forward***– The new beginning requires that people behave in a new way and that in the case of the family-firm founder and leader can be extremely unsettling as it puts one's sense of value and competence at risk, particularly when this person is the leader of both the family and firm subsystems.

Often business leaders themselves need help in making this transition, which can be achieved by:

- *Getting the leader concerned to succinctly describe the change and why it must happen;*
- *Planning the details of the change carefully and assigning responsibility to someone for each detail, agreeing timelines for implementation;*
- *Understanding who is going to have to let go of what and implementing steps to help people respectfully let go of the past, whilst being understanding and accepting of the difficulties faced in letting go;*
- *Constantly communicating the purpose or why the change is necessary, the picture or what the goal is, the plan of how to get there, and what everyone needs to do to get there; and*
- *Helping launch the new beginning by articulating the new attitudes and behaviours required to make such change work.*

In his book *Leading Change*, JP Kotter provides his eight steps to achieving transformation, which I share with you here as a useful guide.

### **Establishing a Level of Urgency**

Typically discussion around the need to change comes easily, however the enormity of the task, especially the first step, is usually significantly underestimated.

No matter what the situation, the work towards successful transformation and change will require great cooperation, initiative and a willingness to make sacrifices on the part of many people.

Establishing a level of urgency is crucial to gaining the critically important cooperation of others, sometimes many others, and doing all that it takes to overcome complacency. Understandably, some crises, for example the death of the business founder and leader, will naturally cause a significant level of urgency, the challenge will then be to achieve a level of urgency around *what to focus on first*, and how to successfully move forward.

### **Creating a Team Focus**

Although business transformations are often associated with one highly visible individual, it is dangerous to believe that the kind of leadership that is so critical to any change can come from a single larger-than-life person.

No one person is every capable of:

- *Developing the vision;*
- *Communicating it to large numbers of people;*
- *Eliminating all the key obstacles;*
- *Generating Short-term wins;*
- *Leading and managing dozens of change projects; and*
- *Anchoring new approaches deep in the organisation's culture.*

A team approach which enjoys the right composition, level of trust and shared objectives is essential to achieving a successful transformation.

### **Develop a Vision and a Strategy**

The vision provides a picture of the future with some implicit or explicit commentary on why people should strive to create that future.

It is suggested that in a transformation process, a good vision serves three important purposes: Firstly, it clarifies the general direction for change; secondly, it motivates people to take action in the right direction; and third, it helps coordinate the actions of different people.

Clarifying the direction of change is important as more often than not people disagree on direction, becoming confused, or at times wondering if change is in fact necessary.

### **Communicating the Change Vision**

The real power of the vision is only released when most of those involved in the business enjoy a common understanding of its goals and direction. The shared sense of a desirable future can help motivate and coordinate the kinds of actions that result in successful transformation. This is an area where business leaders make mistakes all the time, particularly in larger and more complex organisations, failing to gain the required understanding and commitment to the new direction. Keep the message simple and use multiple methods of communication on a regular and ongoing basis.

### **Empowering Employees for Broad-Based Action**

Often environmental forces beyond our control require that companies change, with such occurrences sometimes being potentially catastrophic for a family-firm, such as the death of its founder and leader, or a considerable family conflict which may end in divorce. This problem is amplified over time as the family-firm grows and becomes more complex in nature, with multiple 2<sup>nd</sup> or 3<sup>rd</sup> generation shareholders.

Major transformation will only happen if many people assist and feel empowered to do so, otherwise generally they will not help in the transformation efforts. Empowering people to assist in the transformation efforts entails:

- *Removing structural barriers;*
- *Providing the necessary training and information;*
- *Aligning the systems to the desired vision;and*
- *Removing troublesome and obstructive people.*

### **Generate Short-Term Wins**

Major transformation takes time, often considerable time, which becomes discouraging to most who want to see that their efforts are paying off. Conducting a transformation effort without being able to demonstrate serious

short-term wins becomes demoralising, energy-sapping and can be extremely risky to the future of the transformation effort.

A conscious effort should be made to generate and communicate short-term wins which should be:

- *Visible;*
- *Unambiguous; and*
- *Clearly related to the change effort.*

It will be these short-term wins that feed upon themselves and give the greater transformation effort momentum.

### **Consolidate Gains and Produce More Change**

Don't celebrate victory too early at the risk of losing valuable transformation momentum. Use the credibility gained in short-term wins to push forward and attack bigger change projects, bringing additional people in to help with the effort where necessary.

### **Anchoring New Approaches in the Culture**

Anchoring transformation comes at the end of the process, after evidence of success and after considerable communication and ongoing support. Along the way a change in culture may require that certain people have to leave the organisation and new people must be introduced. Promotions and rewards must be aligned with the transformation objectives otherwise the old culture may reassert itself.

### **THE FAMILY-FIRM BALANCED SCORECARD (BSC)**

As previously discussed, families that work together face many challenges, with many of the problems and friction in family-firms being attributable to the overlap of the family and firm systems. The family-firm is usually seen from either the firm perspective or from the family perspective, or as two conflicting systems. The transformation of a family-firm may be defined as moving from this conflicting system to a system of kinship, which embodies a pattern of appropriate conduct, coherent, embellished and well-articulated actions towards the best interests of both the family and the firm. In this system of kinship, the glue that holds the family and firm together is cooperation and unity, it's the emotional bonding and affectionate ties that develop between and among the members, as well as a sense of responsibility and loyalty to the group as a complete family-firm system.

In an effort to move or transform the family-firm, strategic planning and strategy formulation must be seen as the key way in which family and firm goals can be integrated. To successfully achieve this I suggest the use of the

Balanced Scorecard (BSC) framework as adapted by KJ Moores and JB Craig in their work entitled, '*A balanced Scorecard Approach to Strategy in Family Businesses*' for application in your family-firm.

The BSC can be adapted to the family-firm context as a measurement and management, as well as a communication tool, that is easily interpretable by those involved in the family-firm. This approach addresses a far too often overlooked area of the family-firm system, namely '*how the goals of both the family and the firm can be concurrently addressed*'. As the family-firm morphs into a larger, and an increasingly complex firm over time, strategy and the strategy process becomes increasingly important as strategic decisions affect, involve and need to be communicated to, an increasingly diverse and larger group of family and non-family stakeholders. This process of *professionalisation* will take place naturally over time as the firm enjoys more success and growth, and as the firm passes from one generation of ownership to the next.

The BSC links the measurement of *financial* and *non-financial* indicators to firm strategy. Originally developed as a performance measurement tool, the BSC has evolved into an organising framework, an operating system, and a strategic management system. An exclusive reliance on financial measures in a management system is both insufficient and as previously pointed out potentially inappropriate for family-firms due to their nature of subjective goals and objectives. The BSC measures and reports on both *lag indicators*, or those reflecting the outcome of past actions, and *lead indicators*, or those measures of future financial performance. Lead indicators would include:

- *Revenue mix;*
- *Depth of relationships with key stakeholders;*
- *Customer satisfaction;*
- *New products developed;*
- *Diversification; and*
- *Future contractual commitments.*

The BSC also addresses the measurement and management of tangible versus intangible assets. *Tangible assets* would include:

- *Plant and equipment, and*
- *Property and inventory,*

Whilst *intangible assets* would include:

- *Skills and knowledge of the workforce;*
- *Information technology;*
- *Customer relationships;*
- *Innovative products and services;*
- *High quality and responsive operating processes; and*
- *The organisational climate that encourages innovation and improvement.*

## **The BSC Framework's Four Perspectives**

At the core of the BSC is the necessity to review:

- *The mission statement;*
- *Why the company exists;*
- *The core values; and*
- *What the company believes in.*

A strategic vision can then be developed. The vision creates a clear picture of the company's overall goal and the strategy identifies the path intended to reach that destination. The BSC typically provides a framework for organising strategic objectives and monitoring performance in four perspectives:

- *Financial;*
- *Customer;*
- *Internal firm processes; and*
- *Learning and growth.*

However, as previously mentioned, performance in the family-firm context is most often measured as value creation, defined in subjective terms as free time, flexibility, family employment and self-control, rather than the more objective measure of financial wealth creation.

The BSC can then be used to accomplish four important management processes:

- *Translating the vision – objectives and measures;*
- *Communicating and linking – by bringing understanding to employees relating to critical objectives and how they will be measured;*
- *Firm planning – helps firms integrate plans by using objectives to set targets, and*
- *Feedback and learning - tests the viability of overall strategy. As such the BSC benefits shareholders, management, employees and other stakeholders.*

As one initiates the transformation process by applying the BSC approach, it is imperative that the main causes of crisis are addressed at the outset. Referring to stage 1 of this guide – Crisis: reasons for decline and failure, one should address the management and leadership style of the dominant family-firm leader, in particular where this is autocratic (one man rule) and non-inclusive. One must also seek to diffuse family conflict by being considerate and inclusive of the views and needs of the complex number and configuration of stakeholders in the family and firm systems, as illustrated in stage 2 – Turnaround strategies for family-firms.

This starting point in this process of family-firm transformation or *professionalisation* is firstly, the exact identification of the firm's numerous *stakeholders* and then the clarification of their expectations. It cannot be emphasised enough that the stakeholder dimension in family-firms is extremely complex, considerably more so than in non-family firms. Family-firms have to consider all of the traditional non-family firm stakeholders as well as others including:

- *The spouse;*
- *Employed family;*
- *Unemployed family with an interest in the firm;*
- *Non-family employees; and*
- *Potential successors and heirs.*

Referring to *figure 4* above the intention is clearly to remove any *distractive tensions* and establish productive *creative tensions* working towards a common *shared meaning* and sense of purpose for both the firm and the family.

Having achieved a high level of *inclusion*, as illustrated in *figure 3* above, senior family members and non-family managers may now use the shared and articulated vision for the family-firm as a *basis to their strategic planning*, with the purpose being to identify a strategic plan for the company in accordance with the expectations of the family-firm stakeholders. Subsequently, each firm manager may now develop objectives, measures and targets within the BSC framework for their area of responsibility.

### **The Family Core-Essence Statement**

Whereas vision and mission statements at the centre of the BSC framework are effectively management tools, in family-firms, there is a need to identify the '*core essence*' of the family and therefore the family-firm. The *core essence statement* encapsulates the values that serve as the foundation for the vision and mission of the firm. The *core essence statement* should be established earlier in the professionalisation process, ahead of the firm vision and mission. Emanating from the core essence statement, the firm's vision and mission will be based on the family and firm's *values*.

### **The Financial Perspective**

When considering the *financial perspective*, family-firms have been found to have a *longer-term perspective* rather than short-term financial goals, this influencing strategic decisions taken. Family-firm success has typically not been tied to, or established from, the same performance measures as non-family firms, this being sighted as a key reason why family-firms perform better than their non-family counter parts over time.

The *financial perspective* objectives should be divided into:

- *Return;*
- *Growth; and*
- *Sustainability.*

### **The Customer Perspective**

The *customer perspective* requires that the firm differentiate itself from competitors via a unique mix of product, price, service relationships, and image that the company does or can offer. The customer perspective is core to the family-firm's strategy, and *competitive advantage* can be found in the *unique family elements* of the firm. This uniqueness may include such strategic assets as the *family name and reputation* as the brand and the considerable on-the-job knowledge and networks that the firm built up over many years of family-member long tenures.

### **The Internal Processes Perspective**

The *internal processes perspective* captures the critical firm activities that will determine the means by which the company will achieve the *differentiated value proposition* and the *productivity improvements* for the financial objectives. These are captured by:

- *Spurring innovation to develop new products and services and to penetrate new markets and customer segments;*
- *Increasing customer value by expanding and deepening customer relationships with existing customers;*
- *Achieving operating excellence by improving supply chain management;*
- *Internal processes, asset utilisation, resource capacity management; and*
- *Becoming a good corporate citizen.*

Managers of family-firms should adopt management systems which are adequate for the demands of their external and internal environments, as well as their firm's stage of development, with management systems and structures dynamically evolving as the firm grows and matures.

### **The Innovation and Learning Perspective**

Regarding the *innovation and learning perspective* family-firms have been shown to place substantial importance upon innovation practices and strategy. Successful family-firms have been found to manage and adjust their innovation strategy well, committing to long-term investment. Like innovation, continual learning in the family-firm is crucial to not only its survival but its growth and transformation. Family-firms often enjoy considerable on-the-job knowledge and '*strategic insight*' due to their extended tenure, passion for and commitment to their family-firm.

It may be suggested that the family-firm divides its *innovation and learning* objectives into:

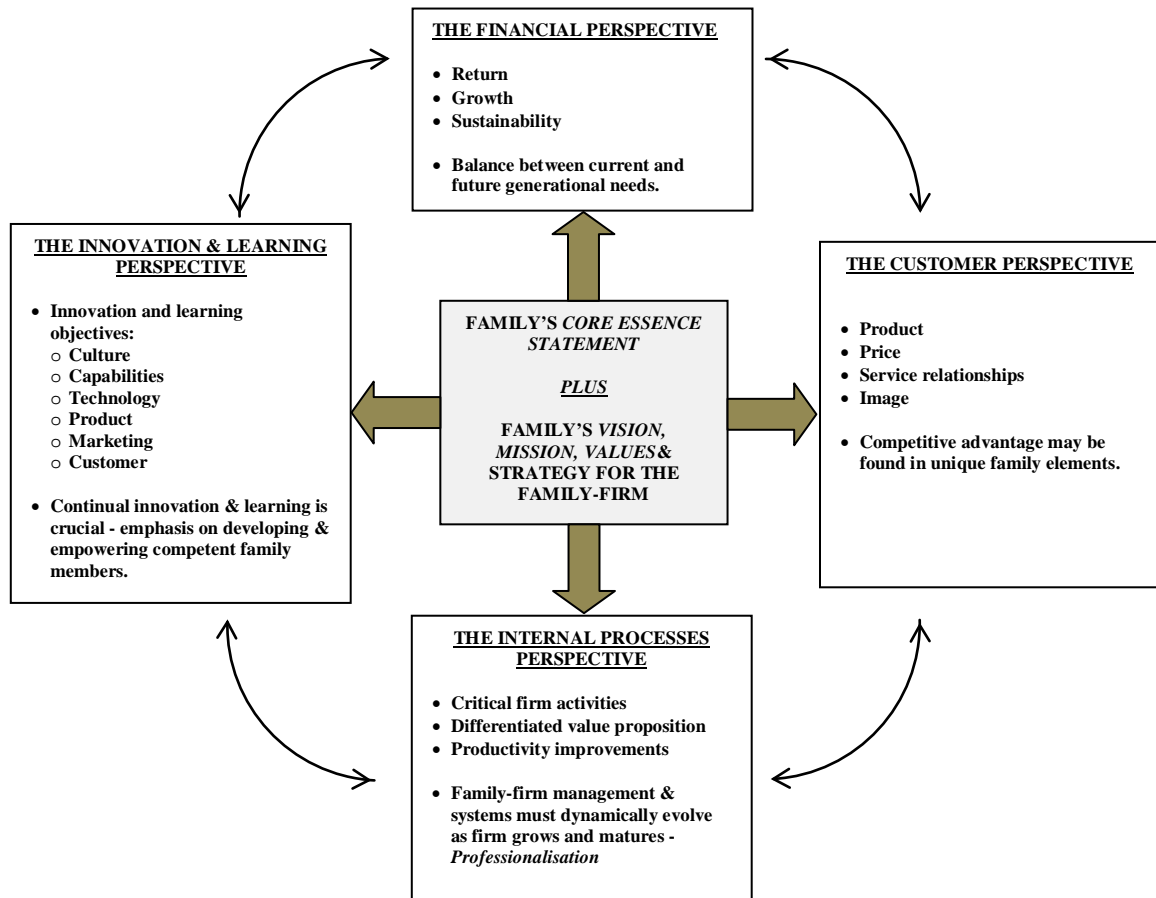
- *Culture;*
- *Capabilities;*
- *Technology;*
- *Product;*
- *Marketing; and*
- *Customer.*

Particular attention should be paid to developing and empowering competent family members to fill the needs of the growing family-firm. This will require a considerable commitment on the part of the family-firm founder and leader, with a particular focus on the *inclusion, control and integration* dimensions of the Model discussed in *figure 3* above.

By following this approach and applying the BSC framework as adapted for family-owned firms, management should be able to adhere to the *strategic* direction and expectations that the family members have agreed upon, and management should be able to document and assess progress against an agreed strategic plan and agreed family and firm strategic objectives. This will provide two crucial outcomes in the context of the family-firm. Firstly, it will enable management to ensure that both the family and firm systems are integrated and aligned, and secondly, that they are able to identify areas that are of potential concern or perhaps still need to be addressed.

I illustrate the adapted BSC framework in *figure 5* below.

Figure 5: The Balanced Scorecard: As Adapted for Family-Firms



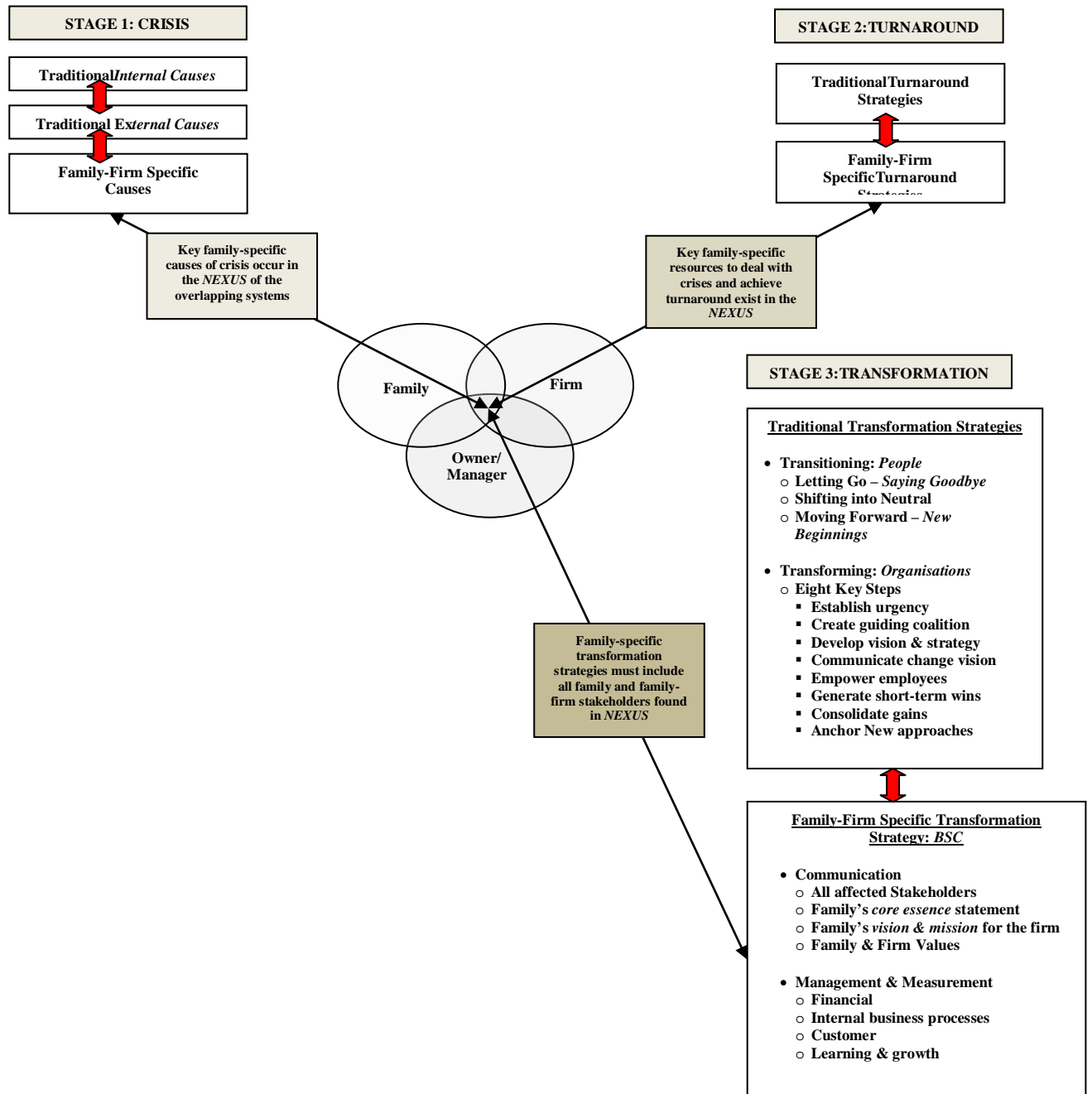
### **STAGE THREE OF THE HIGH-PERFORMANCE FRAMEWORK**

There are a number of *traditional strategymodels*, theories and frameworks which address the question of how to transform a firm, however there is little mention of the need to integrate the family-firm and the family systems to achieve successful and sustainable transformation.

I have combined what I have found to be some of the most relevant traditional strategic theories with the *family-firm specific* adaption of the Balanced Scorecard. I believe that this combination will provide any family-firm owner with a comprehensive tool to successfully and sustainably transform their family-firm, whilst constructively meeting the needs, and addressing the concerns of the family system.

I now offer the third stage of the four-stage high-performance framework: *Transformation Strategies for Family-Firms*, as illustrated in the **figure 6** below

Figure 6: Stage 3 of the Four-Stage High-Performance Framework: Transformation Strategies for Family-Firms



## CHAPTER 5: HOW TO ACHIEVE HIGH-PERFORMANCE AND INTERGENERATIONAL WEALTH CREATION IN YOUR FAMILY-FIRM

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Strategy entails devising a high-level plan to move an organisation from one set of circumstances to another over time. This may be defined as high-performance or *intergenerational wealth creation*, where firm performance may be defined as being derived from the sum of:

$$P = \text{Individual Attributes and Skills} \times \text{The level of Motivation and Effort Applied} \times \text{Individual Style(Leadership)} \times \text{The Organisation's Attributes.}$$

As previously discussed, it is extremely important that you obtain a clear understanding of the firm's *strategic context and that you are constantly thinking strategically* about the organisation, its environment, stakeholders, strategic choice, strategic process and most importantly, strategy implementation.

It must be remembered that high-performance can only be borne out of a deeply felt sense of purpose, that dream that energises the company toward the achievement of its objectives, and a compelling strategic intent.

When striving to achieve high-performance it is recommended that *the job of the strategist is to understand and cope with competition. Often, however, managers define competition too narrowly.* It should be remembered that competition for profits goes beyond established industry rivals to include four other competitive forces as well:

- Customers;
- Suppliers;
- Potential new industry entrants; and
- Substitute products or services.

Understanding your industry structure and the drivers of competition and profitability is important, and whilst a myriad of factors can influence an industry's profitability in the short-term it is *the industry structure that will set the profitability* for the longer-term. The first questions you should ask yourself are:

- what business am I in? and
- Is this a good business to be in?

An intimate knowledge of the industry forces in play, and a healthy industry structure that offers the opportunity of sustainable profitability should be a prerequisite to any company, how to achieve high-performance even within a healthy industry remains a challenge that manages to elude the vast majority of small-to-medium family-owned firms.

Secondly it is critical to note that it is the '*emotional and intellectual energy of every employee*' that will 'Fuel the journey of your family-firm to high-performance'.

When sighting such examples as Honda, Sony, Hitachi, Komatsu and Wal-Mart, all of which are family-firms, it would be correct to suggest that, '*Starting resource positions are a very poor predictor of future industry leadership*', the point being that as a family-firm you should direct your attention to how to make more of limited resources you have at your disposal and be more *resourceful*, with resourcefulness being derived from a deeply felt sense of purpose and a broadly shared dream that all people in the firm subscribe to. This should go further '*than a simple war-cry*', and should be viewed as the heart of the organisation.

Of profound importance is the realisation that the traditional view of strategy focuses on the concept of *strategic fit* between existing resources and emerging opportunities, whilst the concept of strategic intent creates, by design, a substantial *mis-fit* between resources and aspirations, and therefore the need to achieve strategic stretch.

People and teams will strive towards a clearly defined and articulated purpose and set of strategic objectives. The challenge for family-firm leadership is to develop such a purpose or vision, to distil it and to communicate it in easy to understand terms that are both actionable and inspiring.

Family-firm leaders must realise that '*The people process is more important than either the strategy or operations processes*'. After all, it's the people of an organisation who make judgments about how markets are changing, create strategies based on those judgements, and translate the strategies into operational realities. To put it simply and starkly: '*If you don't get the people process right, you will never fulfil the potential of your firm*'. This point brings me onto the importance of people and the need for superior capability and intellectual capital in the strategic process. To put it very bluntly family firms in particular should aim to employ the very best people they can, that display the key attributes which may be defined as comprising intellectual capital. These attributes may be defined as:

IC = Competence  $\times$  Commitment  $\times$  Self-Control (Autonomy).

Intellectual capital is widely defined as the knowledge, information, intellectual property and experience that can be put to use to create wealth and it is this intellectual capital and the ability to transform it into skilled action that will provide the firm with its competitive advantage. It is the future earnings potential from a combination of human capital; being brains, skills and insights, and the organisation's structural capital (Organisational attributes), consisting of an organisation's strategies, processes and policies.

Of particular interest in the context of family-firms are the concepts of affective commitment, and organisational attributes.

Affective commitment is described as loyalty to the organisation, demonstrated by emotional attachment and identification with organisational goals, this type of commitment therefore reflecting the willingness of people to provide discretionary effort.

Organisational attributes can be described as organisational processes, systems, culture, values and management philosophy.

*It is recommended that commitment may be gained by engaging employees' emotional energy and affording employees' a high level of autonomy and self-regulation or self-control.*

*Therefore Family-firms must ensure that they employ only competent employees on merit that display the required attributes of competence, and that they engage and commit to the strategic intent of the organisation.*

Family-firms should not:

- *Fall into the trap of altruism;*
- *Employ incompetent family members;*
- *Tolerate free-loading;*
- *Utilise inadequate or inappropriate processes and systems; and*
- *Encourage a culture too dependent on, and controlled by, the founder and leader.*

Conversely, family-firms can derive considerable competitive advantage through affective commitment as families often have a deep emotional connection with the family-firm and via positive altruism will go to considerable lengths to make it succeed. Furthermore, family-firms are renowned for their rich and caring cultures, committed to long-term *substantive missions*, which are defined by the family's values.

## **A UNIFIED SYSTEMS PERFORMANCE MODEL FOR FAMILY-FIRMS**

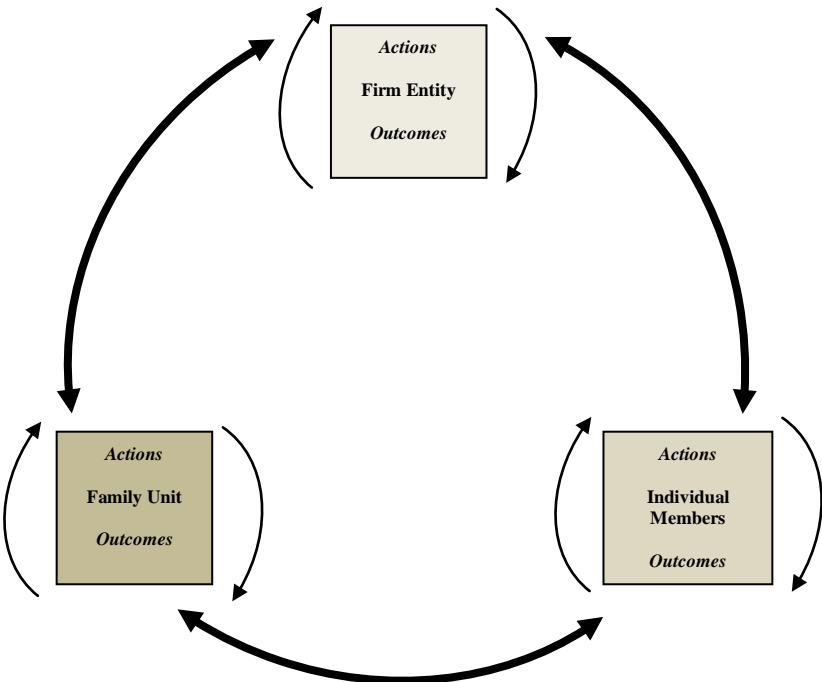
Achieving strategic competitiveness is generally difficult; however these difficulties are made more difficult when firms lack a clear understanding of what influences their performance. Understanding what elements result in firm performance allows managers to organise resources and capabilities and to make the requisite strategic choices to pursue future opportunities. Family-firm literature generally emphasises improving family relationships without a strong strategic management focus on firm performance. Attempts to delineate between the performance requirements of family-firms and non-family firms have left family and management confused at best. More often the response has been to discount, ignore, or isolate the family factors from the firm and to resort to traditional strategy models, theories and frameworks for the firm. The end result is that these managers fail to account for major systemic influences that impact their performance outcomes. In short they do not have an adequate performance model.

In their work entitled, '*A Unified Systems Perspective of Family-Firms' Performance*', TG Habbershon and MC Williams provide a refreshing perspective on the family-firm meta-system. Their unified system model of family-firm performance focuses on how the parts of the system interact to generate a peculiar set of circumstances that lead to the performance outcomes of the family-firm.

This requires a discipline for seeing wholes, interrelationships rather than things, patterns of change rather than static snapshots. The system can be defined as a whole that cannot be divided into independent parts. It therefore stands to reason that a social system model must show how the systematic influences, in this case the family, the firm and the individual members in the family-firm, interact to produce the performance of the whole system – The family-firm, as is illustrated in *figure 7* below.

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**Figure 7: Family-firm Unified Systems Model**



Differing to the overlapping circles model, the unified systems model shows the feedback process with the continuous influence exerted by each subsystem on the other, i.e. the family on the firm, rather than picturing degrees of subsystem overlap and isolated or static points of influence as in the overlapping circles model.

It is therefore very important to understand how the events in one part of the meta-system, i.e. the family, firm or individual family members, are ultimately a cause and effect in the other subsystem components.

It is impossible to think of or speak of one part of the meta-system, i.e. the firm, in isolation of the family and its respective members or to think that in the strategic process one can bracket off the firm and deal with it as if the family does not exist.

As previously mentioned this meta-system or combination of family, firm and individuals may have as its objective, value creation or wealth creation, with value creation being an extremely subjective concept that may

encapsulate lifestyle, free time, employment for all family members or similar values, unrelated to the creation of intergenerational wealth. I reiterate that for the purposes of this guide I have chosen to define the high-performance or success of the family-firm as intergenerational wealth creation, in line with an objective financial orientation. These wealth creation families are referred to as enterprising families and the meta-system as the enterprising-family system.

By focusing on the enterprising-family-firm we can now more clearly define what it may be that potentially influences the achievement of high-performance and intergenerational wealth creation.

In the enterprising family system, a vision for the firm forged by the family members as outlined in the preceding family-firm Balanced Scorecard discussion, directs the activities of the family unit, firm entity, and individual family members so as to pursue the maximum potential wealth for the current and future generations of the family.

High-performance, or intergenerational wealth creation, can only take place if management consistently produces an above average return on capital employed (ROCE). Generating above average returns is achieved only when a firm enjoys a strategic advantage and successfully exploits that advantage over other firms. Conversely, firms that do not have a competitive advantage or are in an unattractive industry will earn only average returns at best, and enjoy little more than strategic parity.

The question must therefore be, "Can, and if so, how can an enterprising-family firm cultivate distinctive family-based resources and capabilities which hold the potential to create unique family-firm competitive advantage? As long as these distinctive resources and capabilities can be developed in ways that lead to distinctive competitive advantage, the results will be above-average rates of return, intergenerational wealth creation and the achievement of high-performance.

It may be assumed that each family-firm is a collection of peculiar resources and capabilities that differentiate it and its ability to produce high-performance over time. Broadly speaking, resources refer to all of a firm's asset and organisational attributes, including intellectual capital, knowledge and other attributes controlled by them.

Research has shown that resources and capabilities create chains of interactions that are directly and indirectly linked to firm performance, competitive advantage, and firm wealth creation.

Identifying these systemic links in the resource and capability chain is an important step in understanding how a firm may achieve high-performance outcomes. Due to the systemic interaction of the family unit, firm entity, and individual family members, family-firms are not only unusually complex but also potentially rich in intangible resources and capabilities. Many of the potential strategic advantages associated with family-firms are found in the:

- *Unique family-firm resources;*
- *Peculiar organisational processes;*
- *Behavioural and social phenomena; and*
- *Leadership and strategy making capability.*

These systemic influences can be linked to family-firm performance outcomes.

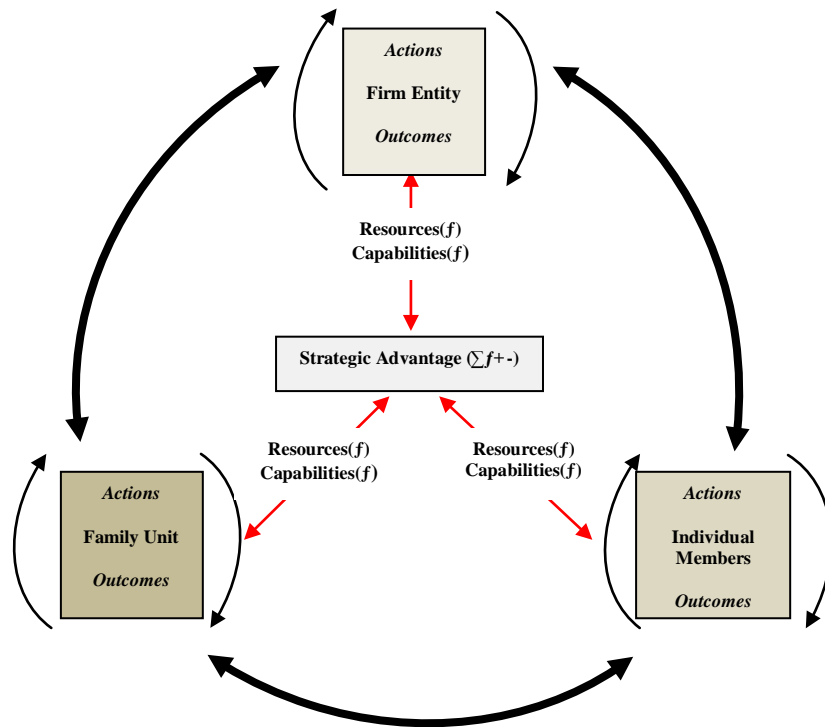
## The family-factor in high-performing family-firms

The *systemic influences* generated by the interaction of the family unit, the firm entity, and the individual family members, create a peculiar pool of resources and capabilities. These resources and capabilities have deeply embedded defining characteristics that may be referred to as the *family-factor* that presents itself as resources( $f$ ) and capabilities( $f$ ), as illustrated in **Figure 8** below. These systemic resources( $f$ ) and capabilities( $f$ ) can become inputs into the meta-system performance model and are key to a particular family-firm's *growth strategy*.

Any of the resources and capabilities that could be associated with a given family-firm might have either a *positive family factor* ( $f+$ ) or a *negative family factor* ( $f-$ ) influence. Positive ( $f$ ) factors hold the potential to provide a competitive advantage to the family-firm, whilst negative ( $f$ ) factors hold the potential to constrain and negatively impact the performance of the family-firm. Family-firms may have a unique potential for trust( $f+-$ ), strength of relationships( $f+-$ ), cost of capital( $f+-$ ), HR policies( $f+-$ ), leadership development( $f+-$ ), alliance building strategies( $f+-$ ), decision making( $f+-$ ), dependability( $f+-$ ), flexibility( $f+-$ ), work ethic( $f+-$ ), understanding( $f+-$ ), forgiveness( $f+-$ ), loyalty ( $f+-$ ), and sacrifice( $f+-$ ).

The family-factor of a firm can thus be referred to as *the sum of all* the resources( $f$ ) and capabilities( $f$ ) ( $\sum f+-$ ) in a given firm. This bundle of resources and capabilities potentially differentiates the family-firm, providing it with a unique source of competitive advantage which results in high-performance, or conversely it may be the source of its disadvantage, holding the potential to put the family-firm into crisis, via conflict, poor relationships or lack of trust.

The defining function of a high-performing family-firm must therefore be the commitment and ability of the family to generate distinctive competitive advantage via the unique family-factor influences it may enjoy, as illustrated in **figure 8** below.



As fundamental to the application of any growth strategy, the *unified systems performance model* requires that enterprising family-firm leaders must be *meta-system leaders*. They need to intentionally manage the interaction of the family unit, firm entity, and the individual family members as an important source of resource and capabilities. Meta-system family-firm leaders must identify and describe both the *positive* and *negative* (*f*) factor influences and deliberately either link them to the achievement of specific competitive advantage and positive performance outcomes for the family-firm, or work to overcome the potential negative impact of the negative (*f*) factors in the strategies they apply.

Studies have shown that the most successful large family-firms all, to varying degrees, demonstrated a common set of driving priorities or passions which in turn give rise to a set of remarkable policies and practices. To summarise what makes a family-firm achieve high-performance I provide you with the following list of driving priorities or passions that you may choose to refer to:

- *Commit enduringly and passionately to a substantive mission – do something important exceptionally well;*
- *Invested deeply and for the long run in the core competencies needed to attain that mission;*
- *Strive to ensure the corporate health and continuity of the family-firm, exercising careful stewardship over resources and encouraging long executive apprenticeships and tenures;*

- *Avoid the temptation for short-term tactics and quarterly earnings;*
- *To realise your mission insist on building a cohesive, clan-like team;*
- *Embrace strong values that rally people around what is important, socialise staff to assure that these values will prevail;*
- *Often pamper employees to elicit loyalty, initiative, and collaboration;*
- *Avoid bureaucratic rules and financial incentives as inducements;*
- *Cherish enduring open-ended, mutually beneficial relationships with business partners, customers, and the larger society;*
- *Act independently – quickly and in original ways. Empower your top team and encourage free and open communication. Make decisions and empower and encourage your top team to make decisions.*

#### STAGE FOUR OF THE *HIGH-PERFORMANCE* FRAMEWORK

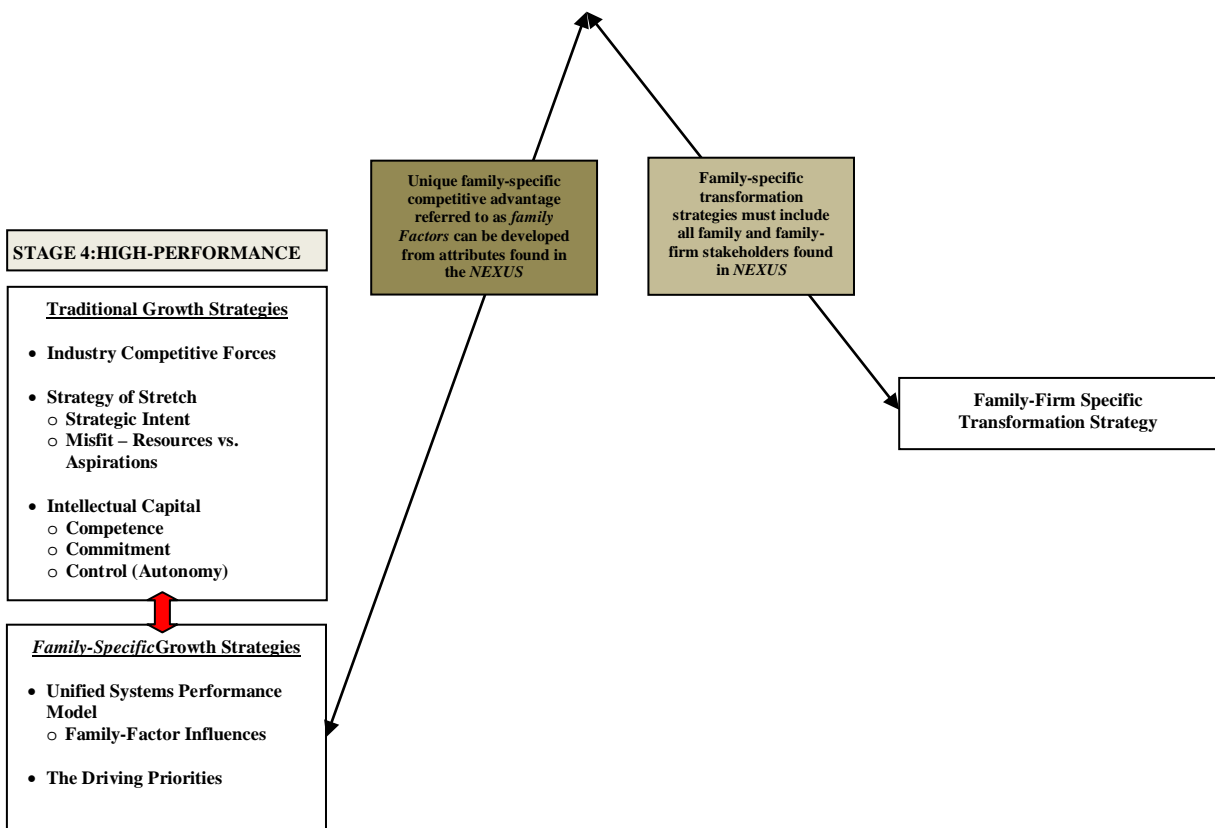
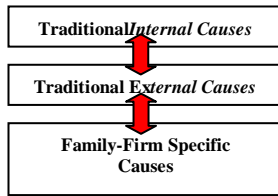
In the knowledge and acute awareness of the intricacies and interdependencies of the family-firm meta-system the strategist can now apply the traditional models, theories and frameworks in search of ways to overcome negative family factors and in search of ways to maximise the potential benefit of positive family factors.

The fourth stage of the four-stage *High-Performance* framework: *Family-Firms Achieving High-Performance*, as illustrated in the *figure 9* below.

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**Figure 9: Stage 4 of the Four-Stage High-Performance Framework: Growth Strategies for Family-Firms**






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**CHAPTER 6: CONCLUSION - THE FOUR-STAGE HIGH-PERFORMANCE FRAMEWORK AND RECOMMENDATIONS FOR PRACTICAL STRATEGIC APPLICATION**

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By combining each of the four stages of this research I now construct the four-stage High-Performance framework as illustrated in *figure 10* below.

The high-performance framework clearly sets out each of the four stages – *Crisis, Turnaround, Transformation and Success*, articulating the strategies that this research suggests can be applied in each stage. The High-Performance Framework illustrates a logical process from crisis to high-performance, indicating an association or linkage between the relevant strategies that can be applied.

From a practical perspective the High-Performance Framework offers academics, advisors and family-firm leaders and managers an easy-to-use frame of reference which clearly and succinctly draws attention to popular and extremely effective traditional models, theories and frameworks, whilst very importantly drawing attention to the little known *family-specific* models, theories and frameworks.

The uniqueness in the High-Performance Framework is that it is derived from an all-encompassing meta-analysis of both traditional and *family-specific* models, theories and framework, which have been distilled into a practical application tool. My research suggests that both traditional and *family-specific* theorists have tended to focus on specific areas of research and not the complete spectrum, as this guide and High-Performance Framework attempts to do.

What this guide does not do is to detract from the use of traditional applications, instead it invites an in-depth study and use of the *family-specific* applications into an already established strategic process in the hope that better and sustainable *family-firm* outcomes will be achieved.

In the most practical of terms the family-firm practitioner should:

- *Carefully assess the current key strategic issues the company is facing;*
- *Develop a very clear understanding of the over-lapping meta-system family-firm dynamics in play;*
- *Identify as many positive and negative family factors as possible and their potential positive or negative influence;*
- *Formulate an appropriate strategy drawing on the traditional and family-specific applications presented in the four-stage High-Performance Framework;*
- *Implement the strategy as articulated in stage three of the High-Performance Framework; and*
- *Continually monitor and apply the traditional and family-specific applications in the most appropriate stage of the High-Performance Framework.*

It is envisioned that given the nature of business lifecycles that the practitioner will constantly be in one of the four stages of the High-Performance Framework, attempting to get to the next. The fundamental premise to the four-stage High-Performance Framework is the immense importance of achieving *strategic context* and understanding the complexity of the strategic variables and forces influencing potential performance outcomes present in the extremely complex family-firm overlapping meta-system.

Figure 10: The Four-Stage High-Performance Framework

