What makes family businesses dynamic?

Lessons learned from our Family Business Award of Excellence winners on talent, innovation and growth

Family businesses were meant to be swept aside by the development of capital markets. But the reverse has happened. Today, they are arguably the most sustainable and dynamic business model globally. Their numbers are increasing, not diminishing. What makes them so dynamic?

As the popularity of the family business model grows, more people are asking questions about what sustains them over the generations. How do family businesses continue to grow, create jobs and innovate long after the original entrepreneur has died? What is so special about their business model?

There is no single answer to these questions. Indeed, the dynamism of a family business over multiple generations is often linked to individual factors relating to a specific business, rather than to any commonality of reasons between similar types of business. Nevertheless, we are now in our fourth edition of the *Family Business Yearbook*, and we have interviewed hundreds of successful family businesses and have begun to see some common themes that help to explain their dynamism. These themes are centered on three areas — innovation, growth and talent management — and they will be explored in this essay.

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The magic of innovation

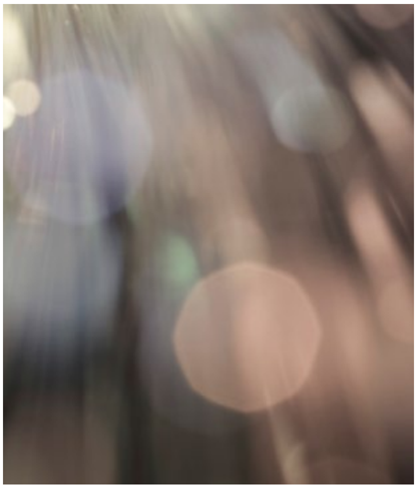
Innovation is that special piece of magic that can make a business prosper. Of course, other factors play an influential role, but ask pretty much any business owner and their ability to innovate comes near the top of their list of what makes them successful. But how do family businesses innovate when many of them have moved on from the initial entrepreneur who set the business up? After all, innovation is usually associated with the latest ideas from a start-up tech company, not businesses that have been around for 50-plus years.

That said, if businesses do not innovate, surely they will end up failing. This leads to a potential paradox — businesses that have been around for 50-plus years look to be just as innovative, if not more so, than tech start-ups. Indeed, innovation is just as much of a factor in successful multigenerational family businesses as it is in any business. But what makes innovation different in a family business? **When asked, they point to some common themes. One of these is the freedom to spend generously on R&D.**

Family businesses often spend at the level that is required in order to push innovation further for the products and services they have been developing for years. **Anton Paar GmbH (see profile page 26),** an Austrian maker of high-precision measuring equipment and a fifth-generation family business, is a good example. The company spends 20% of its annual revenues on R&D. This high level of spend is made possible by being a family business, says its CEO Friedrich Santner. "There are no shareholders taking profits out of the company. Most listed businesses would not be allowed by their shareholders to invest so much of their revenues in R&D," he says.

This is a sentiment shared by **Winsert, Inc. (see profile page 132),** an automotive component maker based in America's Midwest and a second-generation family business. Winsert has grown its R&D department from a one-person office to a newly purpose-built 10,000-square-foot facility with 12 staff. "Innovation is the reason why Winsert has remained world class and relevant," says Trisha Lemery, the company's President and CEO. "It has become our core competency."

Tied up with the freedom to spend on R&D is the ability to take a long-term perspective on their businesses. OK, this is the old nugget that gets pulled out a lot whenever considering the virtues of family businesses. But it can never be said too many times. Rarely do family businesses talk about quarterly innovation targets or one-year targets; instead, they talk about five-year targets and beyond. **They have the luxury of thinking long term when it comes to innovation** — and often, innovation that works needs considerable time to develop.



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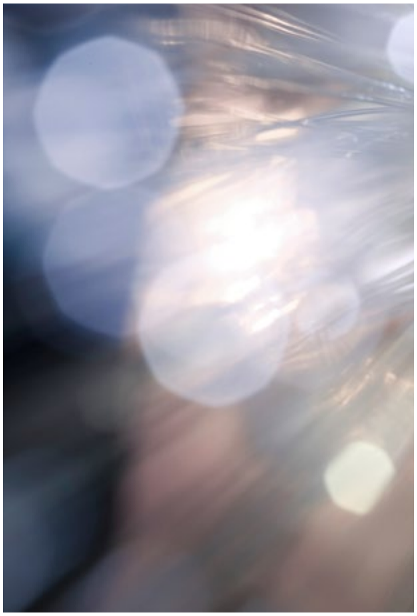
Individualism and innovation

But perhaps it is the individual observations on innovation that are the most interesting — and the most instructive. Here is what Guido Vanherpe, CEO and Member of the Board of Directors of La Lorraine Bakery Group (see profile page 32), says about innovation: "Entrepreneurship and innovation are synonymous. You don't have one without the other." He adds, **"The important thing to know about entrepreneurship in business is not to lose it.** Once you lose it, entrepreneurship is extremely difficult to regain. We have to do everything to keep it." Guido has a very strong belief in organic growth as a driver of entrepreneurship and innovation. **"If acquisitions become the main strategy of growth, they are likely to destroy entrepreneurship."**

Jørgen Mads Clausen, Chairman of the Danish company Danfoss (see profile page 38), thinks innovation is inherently tied up with technology. Danfoss is strong on innovation. Back in the 1930s, it was a pioneer in the development of refrigeration technology — which Jørgen rightly said was the equivalent in technological terms of today's cutting-edge smartphones. Jørgen says that innovation at Danfoss is a bit chicken-and-egg in its interpretation — first you need the technology, then you get the innovation. He also talks about the idea of promoting the concept of the "man on the moon" within the company's culture. This is a way to achieve good innovation, Clausen thinks. Innovation led to the landing on the moon, but how they got there was also due to meticulous planning. This, says Clausen, is good innovation, which can be translated into the products and services that customers want.

For Heinrich Jessen, head of the Singapore-based family business Jebsen & Jessen (SEA) (see profile page 184), innovation means to continue to move up the value chain. Jebsen & Jessen (SEA) is an industrial enterprise spanning manufacturing, engineering and distribution. So it is involved in many sectors, and that's where moving up the value chain and across different sectors makes real sense when it comes to innovation. Australian family business the Manildra Group (see profile page 172) links innovation with export markets. "Through our focus on innovation and sustainability of Australian manufacturing and agricultural industries, we have adopted a truly global outlook," says John Honan, Managing Director of the group. "This constant innovation has been necessary to maintain a competitive edge and to meet the ever-changing demands of the export market."



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Interpretations of growth

Growth is usually the by-product of innovation. Businesses that innovate are more likely to grow. But what does growth mean for family businesses, and does growth mean something different for a family business from what it does for a non-family business? Of course, all businesses need to grow or eventually they will fail. Yet family businesses seldom place as much store on growth as other businesses do. Studies show that family businesses tend to perform better during economic downturns than their non-family counterparts. But, of course, the reverse has also been proven, whereby family businesses perform less well in an economic growth phase compared with non-family businesses.

None of the family businesses interviewed for the *Family Business Yearbook* ever downplay the importance of growth. But nor do they say their objective is growth regardless of the cost. **Rejlers (see profile page 92),** a Swedish engineering consultancy company, believes that — despite being listed on the local stock market — the long term is the most important objective. Stewardship of the business for the next generation is what it is all about. "Even though we are a listed business, we have very much a long-term attitude to growth," says Peter Rejler, CEO of the group. "You must be prepared not to make a big profit every year, even when you're a listed business. You need to make sure the company survives to the next generation as well."

The **LDC Group (see profile page 50),** one of Europe's biggest poultry companies, links growth to its identity. Denis Lambert, Chairman and CEO, has his own motto — "Growth without losing identity!" — which helps to define the values of the company as it strives for growth. **"The company's family character often comes to the fore when it comes to growing the business,"** says Denis. "LDC succeeds by developing its processes — it takes time to observe and learn from the existing processes to build something better."

Family businesses are unique in their ability to oversee growth during difficult times. Recent studies have suggested that family businesses are more likely to survive downturns in economic activity

than their non-family counterparts. Also, they are more likely to retain staff during these difficult times.

Slovenia's **KLS Ljubno (see profile page 80)** is a good example of durability of family businesses. Although well established and successful today, the business has often traded through tough times, when other businesses would probably have given up. "During the economic crisis of the 1990s, our father had to work all the time to get things back on track," says Nataša Strašek, one of the founder's two daughters who work at KLS. "These were difficult times, but we did not complain because we understood even back then what was at stake, and that our father needed the support of the family."

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Managing talent

The third element in the family business dynamic is talent. How do family businesses manage talent over successive generations? How do they avoid the worst aspects of nepotism and reassure talented non-family staff of the benefits of working for them, despite the glass ceiling of family control? All family businesses will tell you that nepotism is bad and they do not practice it. But in reality, it still happens and creates a problem with managing talent in family businesses. Increasingly, good family and corporate governance are viewed as the best means of managing talent at all levels.

This point is illustrated by the experiences of the German family business Dachser (see profile page 56), one of Europe's biggest logistics companies. The family shareholders believe in a very clear division of power between the family and the business, which is clarified by CEO Bernhard Simon's well-known quote: **"Company before family."** And he adds: "The company will last well into the future only if the family itself stands behind the company in the long term. That is why it is so important to create structures, bylaws, contracts and governance rules that maintain the close relationship between continuity of ownership and that of the company." For Dachser, exceptional governance is key to managing talent and business success.

But it is the next generation that will ultimately secure the future of the family business model. And here, there are some interesting developments. One of the most pertinent of these is reverse succession, whereby a next-generation member goes out and sets up a business or career outside of the core family business, and attempts to prove their own entrepreneurial and managerial skills independently. If a next-generation member progresses by setting up a successful business or succeeds in another company, this helps to alleviate any perception of nepotism if they then go on to work at the core family business. And it also helps to reassure the controlling generation that the next generation's skills are up to managing the core business, if and when they join.

There are few better examples of this trend than this year's EY NextGen Club Award winner Christina Suriadjaja (see profile p.). Christina, whose family owns

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a prominent business in the property sector, is the co-founder of **Travelio.com** **(see profile page 223),** an online short-term home rental provider in Indonesia. **"Growing up with unquestionable respect and obedience toward our first-generation patriarch leaders doesn't set an easy stage for the third generation,"** says Christina. "It's even more of a problem for women entrepreneurs like me." But by setting up Travelio.com, Christina has broken down some of those preconceived ideas and has proven her skills to the family. Christina's example is a good way of managing talent within the family.

What constitutes the dynamism of family businesses will preoccupy observers of the sector for many years to come. But the role of innovation, growth and talent — as practiced by all the country winners of the EY Family Business Award of Excellence — is a good place to analyze their dynamism. At the very least, all their stories provide a fascinating insight into what makes family businesses work, and why they are essential for the health of the global economy.

The three themes of innovation and family businesses

Innovation is often specific to individual businesses — what leads to innovation in one business may not necessarily lead to innovation in another. Nevertheless, there are some common themes when it comes to innovation in family businesses:

R&D

Family businesses often say the ability to spend on R&D for their products and services at a non-specified level is crucial for their ability to innovate. Some family businesses spend as much as 20% of their annual revenues on R&D.

Long-term planning

Rarely do members of family businesses talk about quarterly innovation targets or one-year targets; instead, they talk about five-year targets and beyond. They have the luxury of thinking long term when it comes to innovation — and often, innovation that works needs some time to develop.

Decision-making

Family businesses often talk about their ability to act fast when it comes to decision-making — and that helps them to innovate. They are often much less bureaucratic than businesses that have many shareholders. Even family businesses that are publicly listed talk about the need to make and implement decisions quickly. Most say the ease of decision-making helps them to innovate.