

Generation to Generation

The art of stewarding businesses into
institutions

BY IVAN LANSBERG & DEVIN DECIANTIS

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IN light of the many crises—both economic, political and social—that haunt the daily news cycle and introduce terrifying uncertainty and apocalyptic scenario planning into the heart of the executive suite, there is one segment of the corporate landscape that seems to be weathering the storm better than most: family businesses. Credit Suisse recently released a report entitled *Family businesses: Sustaining performance*¹, which profiles how publicly-traded family-run enterprises have outperformed their non-family peers by 8% since the onset of the Global Financial Crisis. Perhaps that isn't surprising, when you consider the names on the list, including Wal-Mart, Samsung, Carrefour, Volkswagen, BMW and L'Oréal. It may also have a lot to do with the role that family dynamics naturally play in stabilizing the governance and expanding the strategic outlook of modern corporate systems. Put simply, families are the first "organizations" we are exposed to. In them, we learn fundamental lessons about the meaning of shared identity; about loyalty and betrayal; about sustainable collaboration and destructive competition.

As far back as Aristotle, the family has been identified as a model for the organization of the state². They are the laboratories where we first experiment with how to relate to those in authority and with those who are our peers and subordinates. Within these systems, we are also exposed to the concepts of legacy and longevity. The familial and social roots of our behavior are so deeply encoded in the DNA of our species that they often drive our relationships with bosses, coworkers' and direct reports in all of the organizational hierarchies to which we belong.

It is hardly coincidental that the metaphor of being "like a family" is so often called forth in high-performing organizational settings to

convey the sense of belonging, commitment, solidarity and loyalty that is essential within the fluid and mobile workforces of the 21st century.

This is readily exemplified by thousands of proud Googlers (and their familial offshoots—Nooglers, Gayglers, and Xooglers³).

High-performing family companies naturally evoke these characteristics in their employees regardless of whether or not they are related to the owners. They achieve this through a variety of strategic initiatives, including their promotion of a compelling longer-term institutional vision beyond the bottom line, their patient deployment of financial and physical capital to achieve this longer-term mission, an intense commitment to stakeholders—sometimes at a short-term cost to shareholders, and their development and retention of the human capital necessary to execute their ambitious strategic plans.

In so doing they are able to create sustained levels of loyalty, engagement, and vitality that allow them to outperform their competitors over time—as Credit Suisse's recent report clearly suggests.

These practices are at the heart of such legendary institutions as Louis Dreyfus, Haniel, C&A, and countless others. While these practices come naturally to family businesses, research and experience suggest that they can also be grafted into the way that non-family businesses are managed with excellent results (e.g. Interface, General Electric, and PepsiCo). In fact, there are two clusters of strategic practices used by high-performing organizations of all types which maps very closely to behaviors that naturally emerge in large family enterprises.

360-degree engagement

First, leaders of successful family companies proactively engage and motivate shareholders to care about the longer-term interests of the firm. These leaders work “upwardly” to help shareholders define their values, shape the company’s culture, and chart the company’s strategic vision. They educate their owners about the significance of the products and services they produce on the lives of their key stakeholders. They treat owners with respect and measure their “ROI” not just against economic parameters of growth and profitability but also against the backdrop of the broader mission of the enterprise and its owners, and its impact on the communities in which they operate.

While this may be harder to accomplish with fragmented, flighty ownership that characterizes modern investment managers—it is certainly not impossible.

Pension funds, endowments and foundations are required to take a longer-term view both by design and by regulatory requirement. Their patience and engagement in governance as share-owners comes in stark contrast to high-frequency traders and certain hedge funds that act more like short-term share-renters with no clear allegiance to the business or the mission. High-performing companies are often successful at fostering a longer-term partnership between owners and operators, as Warren Buffet proves every May at Berkshire Hathaway’s annual meeting in Omaha, Nebraska.

The leadership of long-lasting family companies also actively govern “downwardly” into the organization by promoting a culture that involves and (metaphorically) “adopts” employees into the firms broader “family”—instilling a high level of personal ownership of and commitment to the work of the enterprise. As research by Akerlof and Kranton⁴ suggests, the most important determinant of whether an organization functions well is not monetary incentives but whether workers identify with the organization and their role within it. Feeling more like “insiders”—akin to family membership—increases performance and satisfaction in organizations as diverse as professional

sports teams, the military, and investment banks. This in turn reduces turnover at the top, which, in turn, extends the institutional memory and capacity for longer-range planning among key employees. This contrasts with the more traditional/non-family view that entrenched or tenured professionals are resistant to change and actually impede progress. In fact, it suggests that non-family businesses may be able to better utilize their longest-serving employees in ways that help them to actively manage their culture, preserving and projecting a core set of operational values while still adapting to ever-changing business needs. As John Ward has suggested⁵, long-lasting family companies adopt a “tradition of change”—a synthesis of long-term strategic planning anchored in cultural continuity, with shorter-term tactical adaptation that is keenly responsive to changing circumstances.

The leaders of family companies that have proven themselves to be truly “built to last” also govern “outwardly” into the world by engaging with customers, suppliers and community using a win-win partnership spirit. Precisely because of the commitment and identification that long-lasting family companies are able to stimulate with their owners, the citizenship of the company in the community is regarded as a critical objective deeply embedded in the mission of the enterprise. Benefits include maintaining stable funding relationships, securing priority supply contracts and favorable procurement terms, opportunistic management of receivables and payables, positive government relations, access to exclusive deal flow, and substantial brand loyalty.

Moreover, if the company behaves poorly it reflects both on the company and on the family—the “name-on-the-wall” effect (e.g. the Toyota’s and the Murdoch’s most recently). Family companies built to last place a huge premium on quality and brand reputation, so it is hardly coincidental that so many dominate top quality niches (BMW, New York Times, Patek Philippe, and LVMH, to mention a few).

Finally, the leaders of effective family companies govern “inwardly”—meaning they con-

tinuously monitor the effectiveness of their governing bodies—their boards, their holding companies, their family councils, the trusts through which their ownership is often held. In these systems, getting the governance right is viewed as the key for balancing the conflicting demands and agendas of engaged stakeholders. Effective governance is viewed as critical competitive advantage. This contrasts with publicly-traded companies where boards are fundamentally viewed as policing agents protecting shareholders from self-serving managers, and investments are typically passive and predominantly focused on relative performance. Too few “activist” shareholders are both willing and able to whip an organization into shape while also maintaining a focus on the longer-term success of the enterprise.

Stewardship

The leaders of established family companies (whether they are family members or not) don’t just lead, they steward.

Their mindset is fundamentally “inter-generational”—even though their tenure at the helm is typically longer than their counterparts, they view themselves as transient links in a chain, and view developing a strong bench of successors as imperative. In the most successful family enterprises, the driving assumption is that one generation is simply not enough time to realize the organization’s mission and objectives. These systems do not measure success in years but in decades or more—certainly not in terms of quarterly earnings results. An overwhelming 70% of respondents in the Credit Suisse survey considered a long-term management perspective as one of the most important factors for ensuring their ongoing success.

Making stewardship work requires a clear articulation of the long-term business case to a group of patient investors, and reflects the emerging theme of “capitalism for the long-term” recently popularized by McKinsey’s global managing director⁶. Where publicly-traded companies have traditionally struggled to convince shareholders that a few quarters or years of below-average growth and above-average investment can yield substantial

longer-term economic benefits (Amazon may be the rare exception), family businesses are naturally designed to make these valuable trade-offs in service of their longer term vision.

As good stewards of profit, people and planet, pursuing so-called “double” and “triple” bottom line success has been the cornerstone of some high-performing family businesses for longer than these terms have existed. This is precisely the difference between managing an organization and creating an institution. Enduring family businesses do not exist to only making money today, but are able to adapt to broad societal changes that will continue to be profitable in the more distant future. Rajan Tata specifically describes this type of enlightened institution in a recent issue of the MIT Sloan Management Review—one with a “higher purpose than profits.”⁷ Approaching their strategic and operational mandate as long-term stewards has also allowed high-performing non-family businesses pursue and generate substantial collateral benefits like minimizing their environmental footprint while building brand profile and loyalty (e.g. Interface’s “Mission Zero”), and supporting economic development in their operating communities while generating higher unit sales (e.g. PepsiCo’s “Performance with Purpose”). They realize earlier than most that simple economic growth as a measure of performance is short-sighted and potentially self-defeating in a highly competitive and interdependent world with scarce resources.

The value of family values given the current economic environment, many companies have been forced to shift to short-termism and focus exclusively on economic performance in response to broader industry and macroeconomic trends.

However, companies like Berkshire Hathaway prove annually that this ownership mentality can be grafted onto people that are not family.

In that respect, families and family enterprises provide many valuable lessons for their non-family peers on the performance of human systems, and their executives and policy makers would do well to take notice. ■

Ivan Lansberg is an organizational psychologist based in New York City. He is on the faculty of the Kellogg School of Management where he is Co-Director of Family Enterprise Programs. He is also a founding partner of Lansberg, Gersick & Associates LLC, a research and consulting firm specializing in family enterprise. His latest book *Succeeding Generations*, published by the Harvard Business School Press, is on succession and continuity in family enterprises. He is also one of the authors of *Generation to Generation*, published by HBS. Ivan holds Ph.D., M.A., and B.A. degrees from Columbia University.

Devin DeCiantis is a management consultant based in Boston, specializing in the financial, operational, and strategic aspects of family enterprise. He is an Associate at Lansberg, Gersick & Associates LLC. He holds an M.P.P. from Harvard University and a B.B.A. from York University.

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Notes

1. Credit Suisse Research Institute (September 2012), Family businesses: Sustaining performance, retrieved from https://www.credit-suisse.com/news/en/media_release.jsp?ns=42052.
2. "The first society to be formed is the village.
And the most natural form of the village appears to be that of a colony from the family, composed of the children and grandchildren, who are said to be suckled 'with the same milk'". Aristotle, *Politics*, Book One, Part II, Paragraph 6.
3. Fost, Dan. "Keeping it All in the Google Family."
New York Times, November 12, 2008: SPG6.
4. Akerlof, G. and Kranton, R; "Identity Economics: How our identities shape work, wages and well-being": Princeton University Press, 2010.
5. Aranoff, C. & Ward, J. "Make Change your Family Business Tradition": Palgrave-McMillan, 2011.
6. Barton, D. "Capitalism for the Long Term", Harvard Business Review, March 2011.
7. Tata, R. "When Making Money is Not Enough".
MIT Sloan Management Review, Summer 2013.