The Paradox of Performance in Established Family Businesses

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Enduring family businesses consistently lead with ‘values’ that define their culture …

Bringing the best to everyone we touch.
- Estee Lauder

We do what we say.
- Day & Zimmermann

Sell good merchandise at a reasonable profit, treat your customers like human beings, and they will always come back for more.
- LL Bean

Every day you get our best.
- Wegmans

Be always kind and true.
- Welch Allyn

We are competitive because of our soul.
- Kohler

And both the research and our own practice confirm that …

Sustainability across generations is clearly fed by a sense of **mission** or **purpose**—a rallying theme that provides **glue where difference might otherwise pull the family apart**, and with it, the business.

We also observe that long-lasting family businesses share these features …

- The organization is permeated by a **sense of purpose**. Everyone knows what it is.
- The **economic rationale** for the business *fits* the organization's purpose.
- The family has **weathered ups and downs** in the value of its ownership and in their relationships but has enough belief in the **resilience** of the business to cohere around it.

How do these firms make changes to stay competitive, while holding fast to their founding values?

- We have all witnessed family businesses that have collapsed under the pressure of trying to balance values and performance. Sometimes, one is compromised for the sake of the other.

- Though the firm's leaders may believe the compromise is temporary, and perhaps even unimportant, in fact the very survival of the business can be at stake.

The heavy weight of the past can bring even great family businesses to their knees …

Anheuser Busch:

- Prior to the sale of Anheuser Busch to InBev for $53 billion, the CEO, August Busch IV, faced differences of opinion across the family:

> *"There are members that absolutely want it to stay status quo … others say they want to see some kind of chance to enhance shareholder value."*
>
> —August Busch's uncle Adolphus

Kesmodel, David. "Anheuser CEO Fights for His Legacy." *The Wall Street Journal*, May 27, 2008

Underneath that view was an inability to manage the central family business dilemma

Business Strategy…

- *"Father and son …have been divided on a number of issues, including how to carve out a winning strategy amid tepid sales of major brands like Budweiser and Michelob",* say people close to Anheuser.

…and Relationships.

- August Busch IV said he's still seeking his father's admiration. *"His love and respect will be when I'm ultimately successful,"* he says. …*"I've never had a father-son relationship, Its "purely business."*
- Some say that InBev or another takeover was inevitable as long as CEO August Busch IV opposed expansion outside the US, where AB already was the overwhelmingly dominant player. His dad had been against moving overseas.

Efforts to build a successful strategy were handicapped by a static rather than dynamic view of the family's legacy.

Inadequate attention to the competitive landscape is a form of complacency

Ssangyong Motor Company/Daewoo:

- This month, Daewoo acquired Ssangyong, setting a new precedent for South Korean family-run conglomerates (chaebols). Now highly diversified, Daewoo may focus on fewer industries and sell the rest—either to other chaebols or to foreign companies. Last month, Ssangyong also sold its paper company to Procter & Gamble.
- Until now, the chaebols had easy access to capital and competed for bragging rights by becoming bigger and more diversified—but the result:
  - **Overcapacity and soaring debt**
  - **Disgrace, in relinquishing the empire to a rival family**
  - **Loss of competitive edge in the global economy**

Pollack, Andrew. "Auto Business Sold to Rival In Korea Crisis", *New York Times,* December 9, 2007.

These examples bring us back to our question …

How do successful second, third, and older family businesses—aiming for continuity through independence— **compete well** (achieve profitability and financial strength) while holding themselves to an **uncompromising values standard**?

We talked to successful family business leaders about how they enact ostensibly contradictory goals

When faced with concrete choices, how do leaders from different kinds of businesses, with different kinds of backgrounds, facing different competitive pressures, and with larger numbers of increasingly heterogeneous employees, shareholders, products, and customers:

- **Make and communicate decisions**?
- **Advance their business strategy** such that it creates a unique culture that is also adaptable?
- **Steward family values?**
- **Excel in their markets** against their competition?

We draw on public sources, interviews, and 25 years of client experience

Companies we can identify include:

Business	Kind of Business	Generation
Welch Allyn	Manufacturer of medical diagnostic equipment and therapeutic devices, cardiac defibrillators, patient monitoring systems, and miniature precision lamps.	Fourth Generation
Wegmans	Supermarket chain	Third and Fourth Generations
Disney	Entertainment	Second Generation
Ford	Car, truck and SUV manufacturer	Fifth Generation
LL Bean	Outdoor apparel and equipment manufacturer	Third and Fourth Generations
Kohler	Manufacturer of plumbing fixtures, furniture, tile and stone, and primary and backup power systems. Kohler also develops hospitality and golf destinations.	Third and Fourth Generations
Gilbane	Real estate, construction, and facilities service company	Fourth, Fifth, and Sixth Generations

First, a framework

We begin with the idea of polarities*—the state of having two directly opposite tendencies or opinions.

Family Businesses, in the ideal, have the requisite mindset for polarity management: successful leaders bring both superb rational decision making skills paired with "informed intuition" to reconcile opposing options.

- Hirschhorn, Larry. "Manage Polarities Before They Manage You (Managers at Work)." *Research + Technology Management*. Volume 44, Number 5, September–October 2001, pages 12 – 16.

* Barry Johnson, "Managing Polarities," *Gestalt Review* 6(3):209-219, 2002.

Leaders of long-lived family business think of the issues they confront as dilemmas to manage, not problems to solve …

*"The test of a first rate intelligence is the ability to **hold two opposed ideas in mind at the same time** and still retain the ability to function."*

—F. Scott Fitzgerald

*"The …leadership issue was whether or not you believe in the core values ...and the idea of LL Bean adding value for all of its stakeholders, or you believed that LL Bean was a business like any other, whose sole purpose was to maximize the bottom line. **It wasn't an either/or question**, but a matter of balance between the two points of view. Senior (non family) management and I did not agree on where the balance point was."*

—Leon Gorman, grandson of Leon Leonwood Bean

Managing Dilemmas—an example of working with polarities

- Our client was faced with a **strategy challenge** and many forces to manage as they considered continuity.
- We asked them to take a survey using a CFAR tool* that included 13 choices, seeming "**polarities**" or opposites. For each one, we asked them:
  - To choose a position on the continuum between the two choices that reflects your assessment of the ***present*** situation;
  - To choose a position on the continuum between the two choices that reflects what you would like for the ***future***; and
  - To assess the ***importance*** of this particular issue to the company's future.

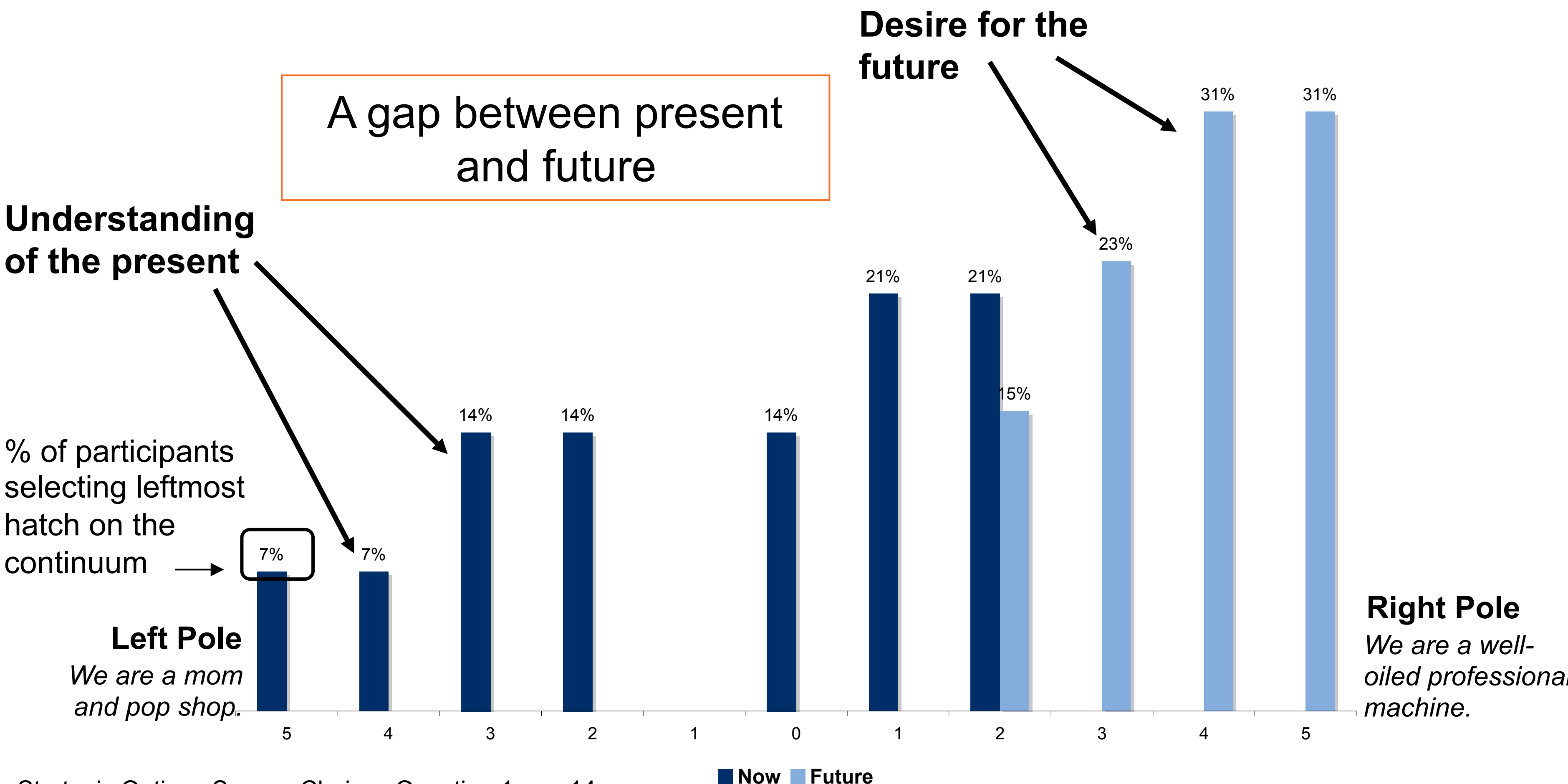
*Strategic Options © 2008 CFAR.

Examples of "polarity" choices included ...

	Left Pole	Right Pole
1	We are a mom and pop shop.	We are a well oiled professional machine.
4	Decision making is tightly held at the top.	Decision making is shared among members of the top team.
5	The family bears all of the risk and reward.	The management shares in the risk and reward.
6	Our identities are very tied to the side of the business we work on.	Our identities are tied to the business as a whole.
7	Succession is the family's business.	Senior executives influence the succession process.
8	Decisions are taken informally here.	We have a codified process for the decision we take.
9	We have a cushion of extra staff and resources.	We run lean.
11	We focus on the future and what we can become.	We take our past, our culture and our history very seriously.
12	We rely on reason and intutition to assess the risks and potential rewards of an opportunity.	We use a risk management methodology to assess the risks and rewards of an opportunity.

The results revealed that simple **either/or choices would not provide the nuanced and sophisticated strategy** needed by the business and the family.

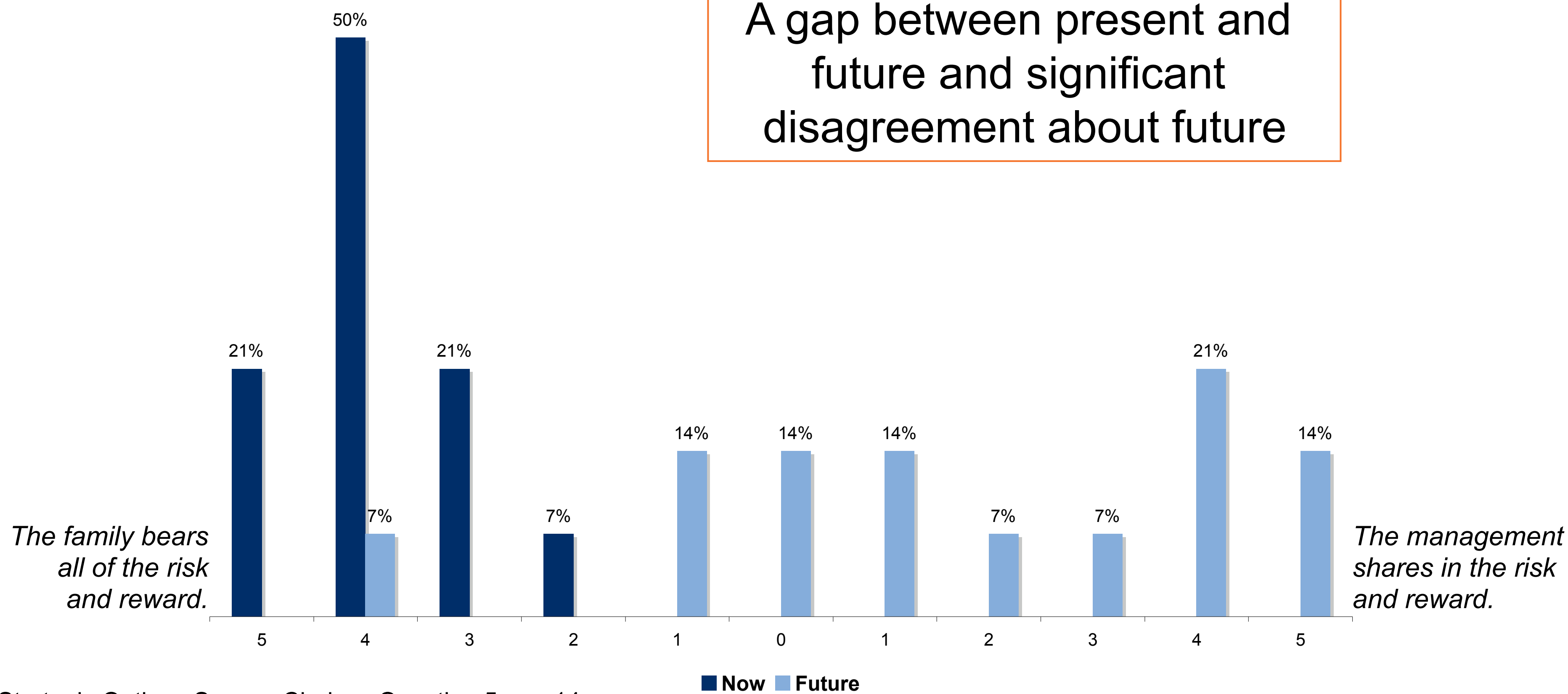
We are a mom or pop shop OR we are a well oiled professional machine.



Strategic Options Survey, Choices Question 1, n = 14

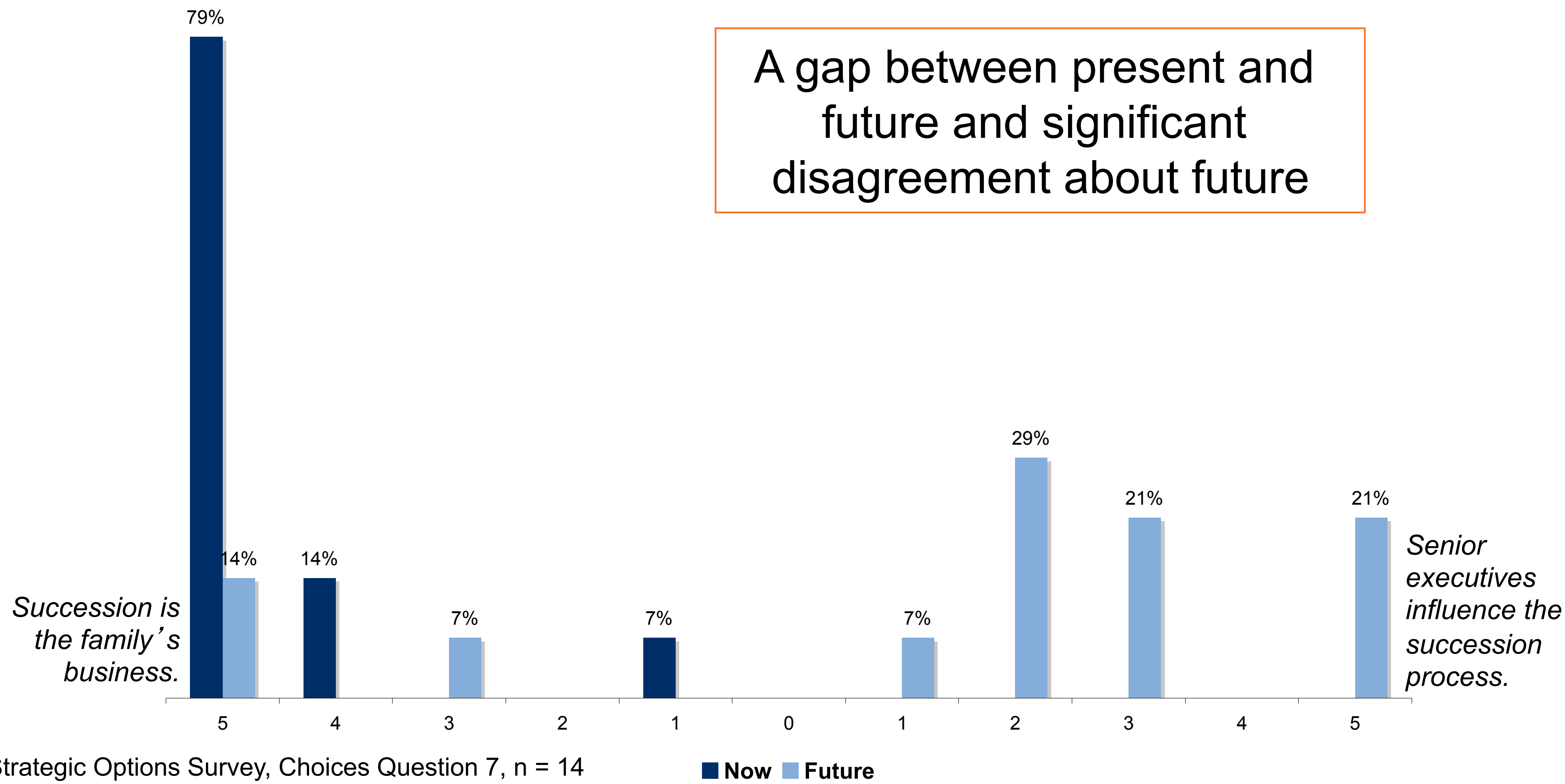
The family bears all of the risk and reward OR the management shares in the risk and reward.

A gap between present and future and significant disagreement about future



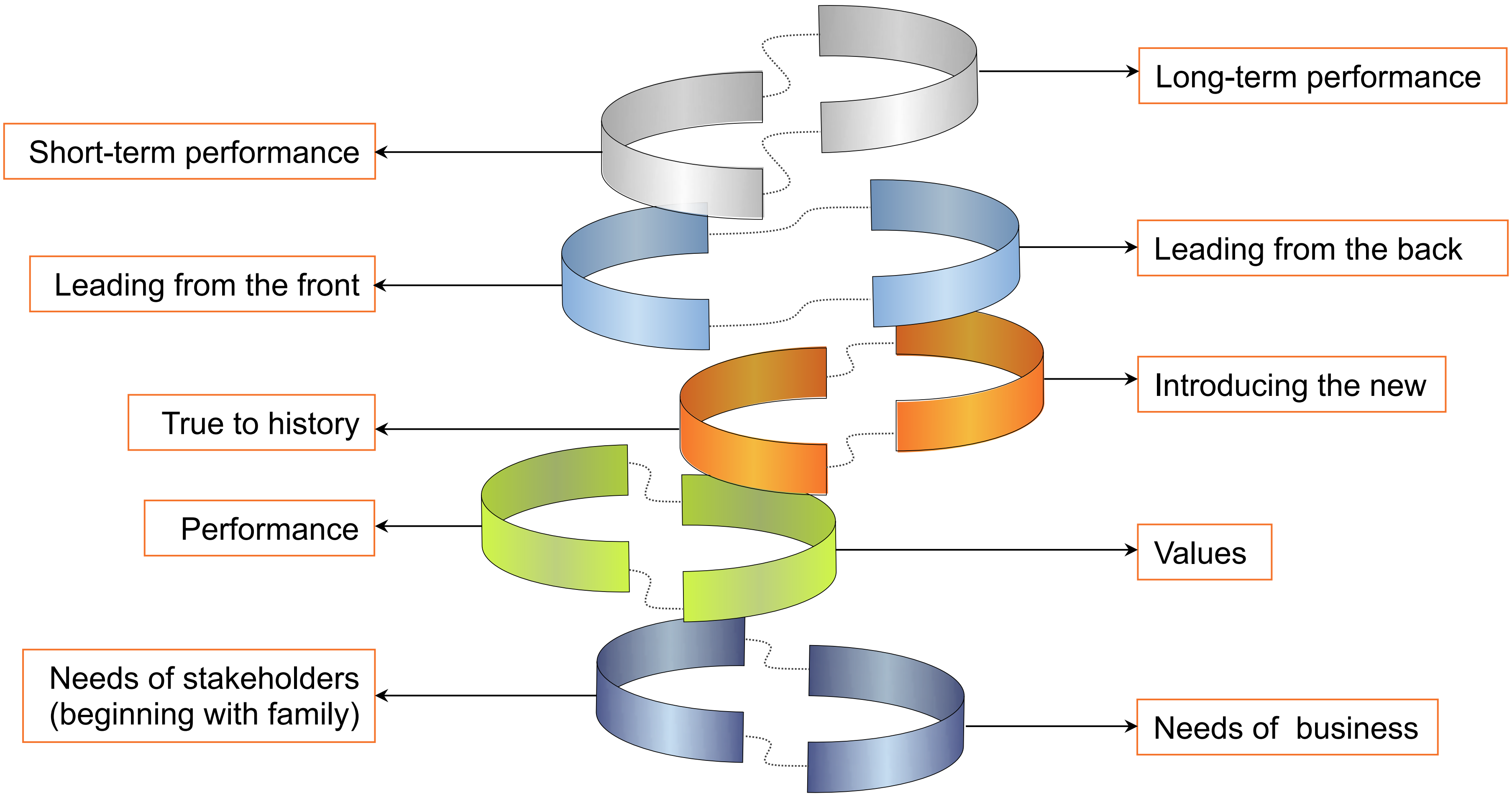
Strategic Options Survey, Choices Question 5, n = 14

Succession is the family's business OR senior executives influence the succession process.



Strategic Options Survey, Choices Question 7, n = 14

In practice, it is short sighted to choose either/or across multiple "goods."



Learning From Leaders: How do Successful Family Businesses Manage the Paradox of Performance?

Successful family firms THRIVE: they recognize and tackle dilemmas across (at least) five polarities:

T
H
R
I
V
E

- **Time** and **Trust**: Trust slowly built with a core and expanding group of family shareholders. A reservoir of *sufficient* goodwill to weather challenges—built on trust and fairness—enables taking long-term decisions while holding to standards of performance for the short term.
- **Humility**: In leadership *and* aspiration, dedicated to being their best—not necessarily biggest.
- **Review:** *Active* stewardship driven by benchmarks and standards for revenue growth, profitability and earnings, competitive orientation and desire to win—along with standards and benchmarks for values showing up throughout their organization, through employee engagement, customer care, and quality specifications.
- **Integrated Values**: Assumptions raised out of the culture—to be viewed and challenged and ultimately integrated into business decisions.
- **Enterprise**: Focusing on family, business(es), wealth, philanthropy, and community—rather than one to the exclusion of others.

Use TIME to build TRUST while delivering on real time performance standards

Focusing on Short term performance: setting and meeting quarterly, annual, *goals*

and

Focusing on Long term performance: clarity about the *kind of company* leaders want their business to be

- **Businesses** must perform—leaders set high standards for performance.
- **Employees** must perform— family or not, employees have to do a good job, and know when they don't.
- While performance against **metrics** is assessed at regular intervals, *decisions about what to do* have no set-in-advance timetable. Some levers are pulled immediately, some not until all opportunities for improvement are exhausted—this can be weeks or months, or longer
  - This happens in the face of increasing pressure for cash—reinvestment, dividends and distributions, etc.

Leaders use time to think developmentally about their firm and their family.

Managing "TIME and TRUST"—through transparency and fairness….

Transparency about trade offs

*"We can't sell at the industry standard of 3 times book and stay a family business. At the same time, some of our shareholders are interested in liquidity and need to understand the things we are committed to. We have **balanced this through transparency. People understand the formula** and we have had solid performance over the last 10 years."*

Sticking to deeply embedded feelings about "fairness"

*"We have always had a strong ethic that **everything gets shared equally** across the 3 original families. Even when one brother spun off a successful $300 million business, sold it for $400M, and could legitimately have taken more of the profit, we split it between all three families evenly. And we expect that others would do the same."*

… and keeping an eye on the far horizon.

Longer term view

"Our family understands equity and returns and they are comfortable looking out 100 years. We've been here 100 years so far, and expect to be here for another hundred. If we have a bad month or quarter, no one is after our CEO's scalp or anything like that. ***We have room to be strategic and build towards long term performance and durability."***

"HUMILITY" from strength—
lead from the back, or the front?

Leading from the front is how most founders have made the business successful

and

Leading from the back is how they create room for future generations to take leadership

- Much is written about charismatic founders who lead the business to success by sheer virtue of their personalities. In fact, founders often have to be at the front with lots of confidence, **louder than their accomplishments**, yet show, in order to be successful.
- In each of our businesses, there were prototypical first generation leaders. But a key factor in their success was their **ability to make room for other styles of leadership**. In the second generation, many "lead from the back" as well as from the front of the room.
- This requires a **valuing of differences**—and a real effort to make room for another style and skill set, listen and not just tell, let others do things differently.
- Similarly, these leaders recognize through their actions that their **goal is to be their best, not necessarily biggest.**

“HUMILITY” from strength—strive to be the best, not necessarily the biggest.

Pairing productively across differences to create space for leadership that looks different

In the first leadership transition, Bob Wegman (Dad) was the business guy and Danny Wegman (son) was the design guy. They **co-led through a transition period** that led to Wegman’s major growth and distinction in the market as the grocer who “followed the customer from 2 steps ahead.” Now another transition is underway, and this **pairing is repeating itself** as Danny’s daughter brings MBA skills to his design and customer sensibility.

Staying the course while competitors excel in the short term

I recall that a competitor company was flying high, getting incredible profits. I pointed out the performance to Leon about increasing our goals. He said, “You know,… L.L.Bean will be here another hundred years from now, they won’t. …Nobody has the capability of (those kind of profits) forever. L.L.Bean, on the other hand, we have real roots. We have a brand that’s much deeper than that. **It’s not just about who’s got the greatest colors on the shelf (this) season.”** *

*Gorman, Leon. L.L.Bean: The making of an American Icon. Harvard Business School Press. Boston, MA. 2006.

"REVIEW"—when to stay the course, when to change?

Staying true to history and sources of success: "Staying the Course"

and

Introducing the new: ideas, business practices: "Welcoming Innovation"

- Private companies do not have the same external forces requiring disclosure, transparency, and public review
- In the worst of cases, **the lack of required transparency can lead to inattention to metrics and review.**
- Coupled with the **weight of a successful past**, to "do what we have always done" especially when the culture is kept in place by long tenured employees, family businesses are at **risk of not recognizing the devolution of strategy and practice, and of not having processes for finding what's next.**
- And yet, **if captured by the new**, particularly in generations beyond the founder, family firms leave behind those very qualities that distinguish them from others, that represent their core, heart, and keys to long term success.

Managing the "REVIEW" dilemma—not going far enough

Putting values at risk

In response to a business downturn, one of our businesses decided that it might be time for **a new CEO**. Driven in part by a value of equality, the two brothers who had led the company for 20+ years asked a relative in the third branch of the family—who was a successful business leader outside the company—to lead the company and bring ideas from the outside.

He brought an ambition to take the business beyond their natural marketplace where they had found their niche and enjoyed relatively little competition. **Seemed like a good idea**, as business in their current market was faltering, and here was someone in the family who had achieved success elsewhere.

Managing the "REVIEW" dilemma—not going far enough (Part II)

Shortly after the new CEO joined the business though, many employees complained that **he represented different "people" values**. At the same time, **the company now faced extreme competition** in a market they were ill equipped to serve, and as a private company lacked the resources to stay in and fight.

Result—

A siege from the 4th generation from all three branches—and the departure of the CEO from the business, but not from the family.

Managing the "REVIEW" dilemma—going too far

Putting the business at risk

Only a year ago in 2000, Mr. Nasser was considered a hard-charging, innovative executive who styled himself after (Jack) Welch… Then came the bruising dispute with **Bridgestone/Firestone** over what role tires played in fatal rollovers of the Ford Explorer. Dealers, meanwhile, rebelled at Mr. Nasser's plans to build dealerships directly and sell cars online. Managers chafed at a strict new grading system…and Ford fell behind G.M. and Chrysler in quality rankings

- *"Go back to last year this time, Ford was the premium company out of the three,"* said Kevin Rendino, manager of the $8.6 billion Merrill Lynch Basic Value fund, which has reduced its holdings of Ford stock by 70 percent since the middle of 2000.
- *"Now,"* Rendino said, *"it's almost flip-flopped and Ford has the worst reputation."*

Hakim, Dan. "Restoring the Heart of Ford" *New York Times*, November 14, 2001

“REVIEW” requires consistent application of benchmarks and standards.

Making hard choices

After years of trying to make a “home improvement” department work, a major retailer finally **cut its losses and shut down that business** just years before the founder’s death. Upon reflection, he suggested to his team that he was the only one who felt passionate about the idea while others accurately thought **it took them away from their core value proposition to their customers.**

The Chairman of one of our businesses made a hard decision to ask his brother to step down from a leadership role when through repeated quarterly reviews it became clear that he was not good at running a profit center. The clarity of the metrics made it possible to manage a transition to a successor and **find a better place for his brother** so that he did not feel kicked out, but rather moved to a role more appropriate to his skills.

"INTEGRATED VALUES" guide company decisions *and* influence performance.

Prioritizing Performance **and** **Prioritizing Values**

- One stream of business literature discusses values in the form of mission and vision statements that set a "north star" for leaders and employees.
- Another stream focuses on increasing shareholder value, discussing various methods for doing so, and provides detailed finance formulas by which to judge. These formulas can be applied by both public and private firms by sophisticated people with sophisticated tools.
- Not often is the **relationship between real values and increasing shareholder value** illuminated. If values are put first, we may see performance lag, and if performance is put first, we may see that leaders suspend their commitment to certain values.
- Family businesses are still seen as an anachronistic form: if they were not dominated by family they would be held to some "higher" standard—this view suggests that values impede performance. Not so. Our discussions consistently take us in the opposite direction:

Values are the centerpiece of high performance standards.

“INTEGRATED VALUES” guide company decisions *and* influence performance. How?

Transmitting values and influencing performance

Wegmans has a program called the **“Spirit of Giving”** that gives one-time financial help to an employee in need. The company made a donation of $600 was to a woman who worked at the deli counter when her colleagues learned that she had been living without electricity. Months later, the deli manager at the same store was under fire from Bob Wegman about the deli display: the same woman who had received the gift to restart her electricity contributed a display idea that **led to thousands in increased sales.**

Building a structure to align values with market need

Gilbane deeply valued community, and family’s longstanding ability to establish roots. As a result, they had always stayed a local company. They were successful, but were loosing good people who hit a ceiling too early without room for promotion. They decided to **decentralize and create multiple local offices,** giving people the opportunity to build community in multiple places, and creating opportunities for high potentials to run larger initiatives. To support their nationwide system, the company had to invest in a cutting edge IT structure—reaping an **unforeseen benefit** when this structure provided competitive advantage in their construction and real estate development industry.

Kohler's stance—linking economics and values in guiding principles

Kohler's Guiding Principles*

- Living on the leading **edge**, meshing art and advanced technology to create new products, new markets and new niches within existing markets.
- Maintaining a single high standard of **quality** in all products and services to make them capable of delighting the senses and sensibility of end users consistently.
- Continually **reinvesting** the majority of our earnings in operational excellence.

"*These principles have been powerful in driving the long-term success and character of the Kohler organization. Yet, a company cannot be explained in terms of mission or principles alone.* ***Human energy is required to give life and direction to a mission.***"

(conversation with Herb Kohler)

* http://www.kohler.com

"INTEGRATED VALUES"—not a balancing act but an intentional mixture

Integrating values into business performance requires leaders to answer these questions:

- **How do values get transmitted?**
  - From family to business and business to family
  - From one generation to the next and from the next generation back up
  - From shareholders to business leaders and from business leaders to shareholders
  - Across family branches, within a generation
  - From areas of innovation to the core, enabling and reining in the "new."
- **How does acting on these values positively influence performance?**

> *"I work to advance living environments and I get really excited about that. Doing it quietly, without hassle, and doing it better than anyone else."* *
>
> —Herb Kohler, the Kohler Company

http://www.kohler.com

“ENTERPRISE”—concentrated *and* distributed economics

Prioritizing stakeholder needs, starting with Family

and

Prioritizing business needs

- We all know stories of failure when the **multiple systems** at play pull a business apart rather than work powerfully together to make it successful.
- We hear about family business leaders who justify bad business decisions as “doing what is necessary to keep the family together.” But they discover that **if the family suffers, so does the business.**
- Throughout its lifecycle, the **needs of family and business expand**. Structures and processes that recognize this expansion make room for difference.
- Thinking only about the polarity of “Family or business” is too narrow a stance to foster success over multiple generations.

"ENTERPRISE"—also means thinking expansively

Explicit structures to manage the dynamic dilemma

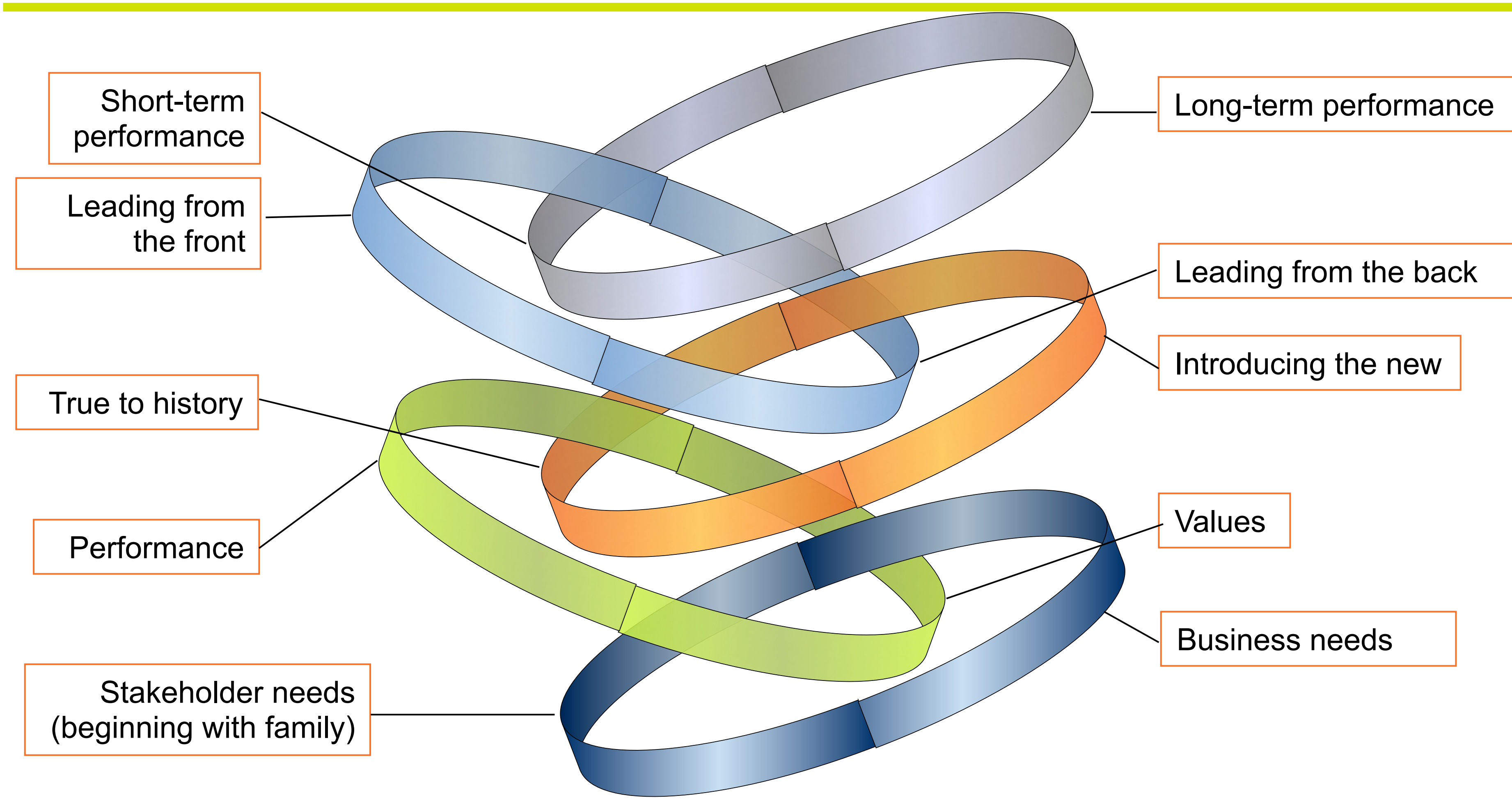
- At a key generational transfer with the first outside CEO in 60 years, Welch Allyn established a **voting trust** to manage the pulls between family and business interests.
- Another of our businesses created a **"cousins' consortium"** to integrate family interest in values and legacy, with company goals.
    - *"You want your **stockholders to think like stewards rather than investors**. When family members feel like investors, you have lost them. At the same time, you don't want stockholders feeling trapped. We came up with a fair formula for a family business and people understand what the formula is."* *

Meeting family needs in more than one way

- Bob Wegman bought **land** in the community early in his business career, when he ran only one store. Later, this became an area of smart business for both the family and the business—one family member went into real estate while the business used the land for their store expansion that came years later.

* Interview with private business

Polarities—managing dilemmas is a *continuous* process of sustaining creative tension.



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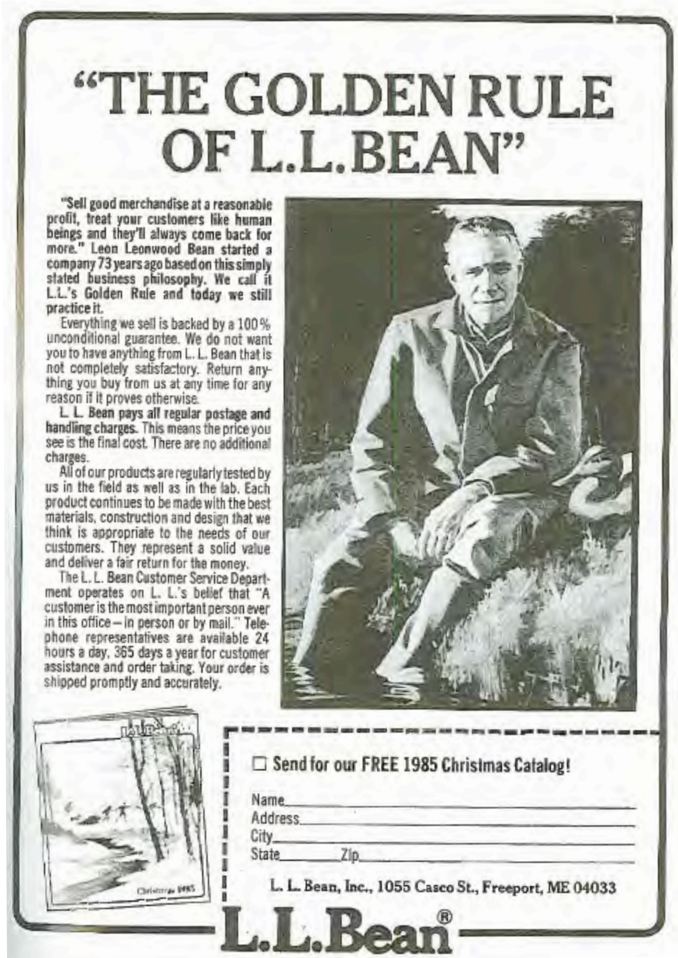

Gorman, Leon. L.L.Bean: The making of an American Icon. Harvard Business School Press. Boston, MA. 2006, p. 160.

… and results.

Gorman, Leon. L.L.Bean: The making of an American Icon. Harvard Business School Press. Boston, MA. 2006, p. 160.

Lessons Learned—business success and family values are integrally connected.

Values and Performance are two sides of the same coin

- Values and performance can seem to pull in opposite directions, making many ask "can we afford to stick with our values?"
- Time after time, we have seen errors in both directions—putting either core identity or the business at significant risk.
- Successful and enduring family business leaders have realized that values and performance are integrally connected—each one makes the other possible.
- As a result, successful family businesses have found ways to make explicit their connection in practice.

"We are competitive because of our soul"

—Herb Kohler

There is power in polarities.

Managing core dilemmas is a vehicle for building sustainability and strength

- Managing the multiple dilemmas that make family businesses thrive is overwhelming. Is it worth the work?
- The active work entailed **creates a vehicle for transmitting implicit knowledge and appreciation to others in the business**
  - Transmitting culture
  - Building consistency and quality
  - Opening discussions that result in better outcomes and stronger relationships
- As a result, the very things that make the business competitive permeate every fiber of the business

As one client says: **the *process* is the plan**.

The work is never done, but that's a good thing.

- **Each generation faces its own version** of these dilemmas.
- External and internal forces change, requiring vigilance about change.
- The process of defining and addressing them gives each generation an opportunity to shape the business in ways that **amplify rather than dilute** their predecessors' success.

About CFAR

- **Roots in an academic institution**: we started with an action research orientation descendent from the field of clinical or applied research.
- **Multi-disciplinary**: our consultants are deeply steeped in their disciplines of origin—business strategy and finance, organizational psychology, negotiation and mediation, anthropology, economics, policy and more.
- **Our work teams combine different professional perspectives in the service of solving client problems:** our systems and processes focus extensively on the development of multi-disciplinary teams in ways that bring creative solutions for our clients.
- **We are actively becoming inter-generational:** we have founders and a next generation explicitly working together on succession and strategy.