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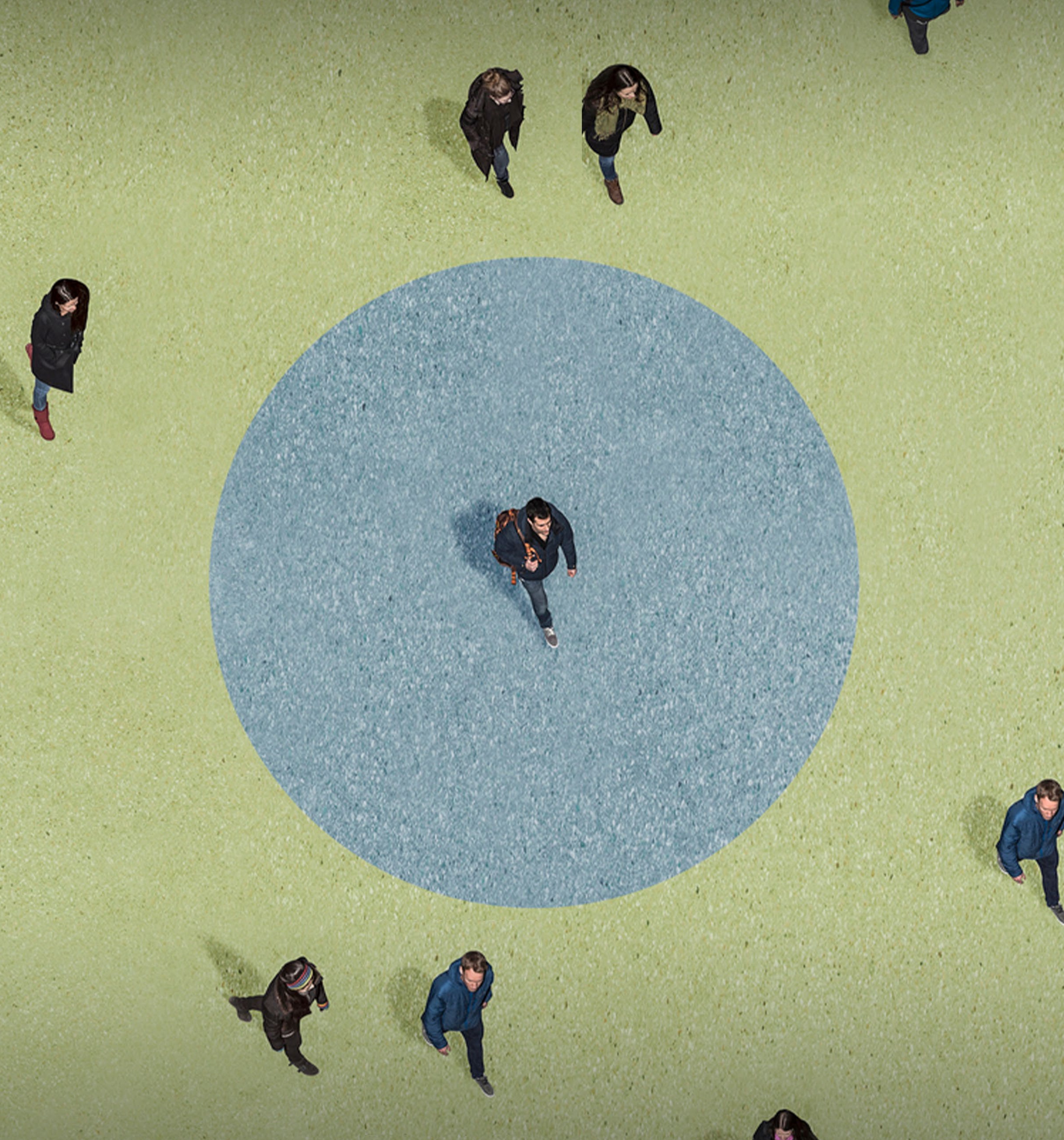


Planning beyond the horizon
A multi-generational outlook

May 2021

At a time of greater distance, family enterprises need to work more closely than ever.

Foreword

With their long-term vision, concentrated power and capital strength, family enterprises will be critical to the global economic recovery after the pandemic. But only if we improve the success of generational transition. Without the right planning and preparation, some family enterprises may fail to successfully transition to the second generation, and the process becomes even more challenging for third or fourth generations.

Often, the problem is misalignment between the goals, wants and needs of the business and individual family members. A 2019 Deloitte survey made this strikingly clear. It found only 35% of the family enterprises surveyed said their business objectives aligned with family goals and less than one-third of respondents said their families agree about the business' future development.[1] Yet family legacy and tradition was the respondents' highest priority over the next two decades.

Whereas, those who create successful and long-lasting family-owned businesses have mastered the art of multi-generational planning, which have at their core strong communication and trust between the generations.

This report is based on 35 years of data and experience from solving complex family and business issues with some of the world's largest and most successful family-controlled businesses.

It examines what it means to have a multi-generational outlook, the interdependence of family and business health and the red flags that suggest family issues could be putting the legacy of your family enterprise at risk.

We hope it offers you, as a family enterprise leader, a useful perspective and a starting point for safeguarding the future of your business.

Adrian Batty

Deloitte Private Australia, Family Enterprise Leader

[1] *Deloitte Global Family Business Survey*, Deloitte, 2019

The key role of family enterprises in the post-COVID recovery

As the global economy reels from the multiple blows dealt by the COVID-19 pandemic, family enterprises will be vital to driving recovery and creating jobs.

The pandemic has magnified the power of family business owners. Family ownership is prevalent and substantial among the world's most successful companies, with significant capital to be deployed globally. In challenging times, well-managed family businesses outperform non-family competitors, due to the uniquely long-term nature of their vision, their ability to take bold, decisive and quick action and their willingness to invest in challenging times to keep working towards their goals.

Where other large corporates see risk, family enterprises see opportunity. In previous economic recessions, family-owned companies have survived at a greater rate than non-family companies by keeping their eyes on the road ahead, launching new products and preserving their emphasis on corporate social responsibility.[2]

A recent study by Bocconi University showed that family enterprises were more resilient than non-family organizations, with the best financial performance delivered in businesses where a family was both the controlling shareholder and held the CEO position during the pandemic.

This success is partly because the form of ownership gives families hidden power. Leaders can immediately and fundamentally change every aspect of how their company works. Family enterprises have the combined power to make the smart decision and the ability to execute it.

Successful family enterprises also operate to perfection. Rather than being satisfied by hitting corporate targets, the work is never done. These organisations constantly find areas that can be improved.

But their biggest strength in a crisis is that family enterprises are underpinned by a strong culture that sheets back to family values. This culture not only saw many family enterprises giving back during the pandemic, it also inspired loyal employees, often with decades of tenure, to rally to the cause. Charismatic and respected family owners create a huge amount of trust and goodwill. And that cuts both ways. Family businesses are willing to avoid layoffs during downturns, promote from within and invest in people.[3]

Most family-owned companies are also set apart from corporate counterparts because they have a higher central purpose than simply returning money to shareholders. Once successful, family enterprises are all about legacy. Not just protecting the family but standing for an idea, taking on a respected role in society or simply being the best in the world at what they do.

By holding on to purpose during challenging times, and being prepared to invest for longer returns, family enterprises avoid the short-term, knee-jerk decisions that can be disastrous in a crisis. We were not surprised to see that, during the pandemic, family-controlled companies were the ones most likely to double down or make a move to seize market share.

Finally, family enterprises have the advantage of experience. Many great family enterprises of the world have endured a crisis before and have been more resilient to the pressures of the crisis than less-experienced organisations.

In short, we believe family enterprises will be at the epicentre of the world's recovery and growth – particularly in Asia.

[2] Saim Kashmiri and Vijay Mahajan, Why Family Businesses Come Roaring out of Recessions, Harvard Business Review, April 7, 2014.

[3] Nicolas Kachaner, George Stalk, Jr., and Alain Bloch, What You Can Learn from Family Business, Harvard Business Review, November, 2012.

What does it mean to have a multi-generational outlook?

While public companies think in quarters, family businesses think in generations.

In a fast-changing world, family owners know they cannot sustain a single business forever. Global multi-generational business families are rarely in the same business they were in a generation ago – let alone a century ago. Family businesses diversify, start new businesses, sell old ones and foster entrepreneurship alongside tradition.

One Japanese kimono manufacturer, dating back to 1688, has expanded into carbon fibre production for materials companies. Its core competency, 3-D weaving, remains the same.

It takes a different mindset to steer a company across centuries. And that starts by taking a multi-generational outlook. In practice, this involves changing the conversation from talking about ownership to a dialogue where the spotlight is on stewardship.

This new lens means that the role and responsibility of existing owners is to nurture the business and ensure it is placed safely into the hands, processes and operations of the up and coming generation.

In our 2019 survey, almost two-thirds of respondents said long-term value was more important than short-term results. Only 8% said they felt under strong pressure to meet short-term financial results.

This is the opposite of the way listed companies think about and operate their businesses. Public enterprises look 1-5 years ahead and try to sense and respond as quickly as possible to events as they happen. Conventional thinking says this approach is the best way to cope with change and uncertainty.

We disagree. In our experience, it often results in companies spreading themselves ever more thinly to deal with an ever-expanding array of initiatives – projects that tend to be incremental because they are responding to short-term events, not long-term trends.

We believe this 'short-termism' is why the average return on assets for all public companies has declined by more than 75% since 1965.[4]

Whereas, in a family enterprise with a multi-generational outlook, the 1-5 year horizon gets almost no attention. Instead, we start with the 10- to 20-year period (zoom out). This is when we assess what an enterprise's industry or relevant markets will look like, and what it needs to do as a company to be successful in that environment. Then, we bring it back to the present (zoom in) by selecting two or three initiatives the enterprise should be pursuing over the coming year to move towards that future.

[4] John Hagel, John Seely Brown, Maggie Wooll, and Andrew de Maar, The paradox of flows: Can hope flow from fear?, Deloitte University Press, December 13, 2016.

This 'zoom out to zoom in' approach is especially well-suited to family enterprises, allowing them to both prepare for the future and achieve greater near-term impact. It works because family business leaders tend to stay in their positions longer than a corporate CEO. This means that they and their successors are far more likely to see major projects and initiatives through to conclusion – and to keep regularly stepping back to evolve their outlook.

It's important to take the time to discuss long-view issues not only in every management meeting but in every family council meeting.

Families that can appropriately define both their 10- to 20-year aspirations and their 6 to 12-month initiatives – and maintain a clear line of sight from one to the other – will stand a far greater chance of staying ahead of the game for years to come.

But this may not happen unless family enterprises:

1. **Formalise planning processes**
Typically, companies hold annual off-site meetings, in which free-wheeling discussions may not translate into concrete action once everyone returns to work. However, when we 'zoom out to zoom in', we put capability-building on a schedule, deploy actual resources toward chosen initiatives and put in place metrics to measure whether they are progressing as planned.

2. **Put family governance in place**
Family enterprises typically have excellent business governance, but few operate with the same level of rigour when it comes to family meetings or communication. Yet, to plan beyond the horizon, it's essential for the next generation to be included in their long-term decision making – to align family strategy with business strategy. In this case, family governance is the foundation of business governance.

3. **Prepare the rising generation**
Letting go is not simply about the incumbent generation giving up power. It's about preparing and educating the rising generation. Heirs to family businesses can't sustain their leadership through raw power. The previous generation and their stakeholders must grant them the authority to lead. Preparation should be focused on how to nurture the rising generation, setting multi-generational targets together and using any deviations from meeting these targets as learning experiences. Learning together as a family sustains the family's power to adapt to disruption.

Zoom out questions

What will our relevant market or industry look like 10 to 20 years from now?

What kind of company will we need to be 10 to 20 years from now to be successful in that market or industry?

Zoom in questions

What are the two or three initiatives that we could pursue in the next 6 to 12 months that would have the greatest impact in accelerating our movement toward that longer-term destination?

Do these two or three initiatives have a critical mass of resources to ensure high impact?

What are the metrics that we could use at the end of 6 to 12 months to best determine whether we achieved the impact we intended?

Case study

Preparing the 5th generation

Established in 1869 as a blacksmith's shop in the Netherlands, the Terberg Group of companies is now a US$1 billion supplier of specialized vehicles, from terminal tractors to cars, offering both conversions and new builds. It operates 28 companies in 12 countries. George Terberg, chairman of Terberg Group's board of directors, represents the fourth generation of the Terberg family.

The Terberg Group is currently led by the family's fourth generation, but of the 40 family members in the fifth generation, two are also active in the company. "A 'fifth generation committee' is helping the fifth generation become committed, enthusiastic, passionate, and inspired family members," said Terberg. Fifth-generation family members pay an annual visit to one of the Terberg Group's operating companies and get career advice, but they can't join the company automatically.

Standards are high, Terberg explained: "Family members who want to join the company must have the potential to become leaders of one of the bigger companies. They must have a university degree or a degree from another higher professional education body. They must also have at least five years of work experience outside Terberg. After that, they can apply for a job, and we will make an assessment. These are high thresholds, but it is also a better way to guarantee the continuity of our family business. Ultimately, my generation is responsible for properly passing this company on to the next generation."

"A 'fifth generation committee' is helping the fifth generation become committed, enthusiastic, passionate, and inspired family members."

George Terberg, Chairman of Terberg Group's board of directors

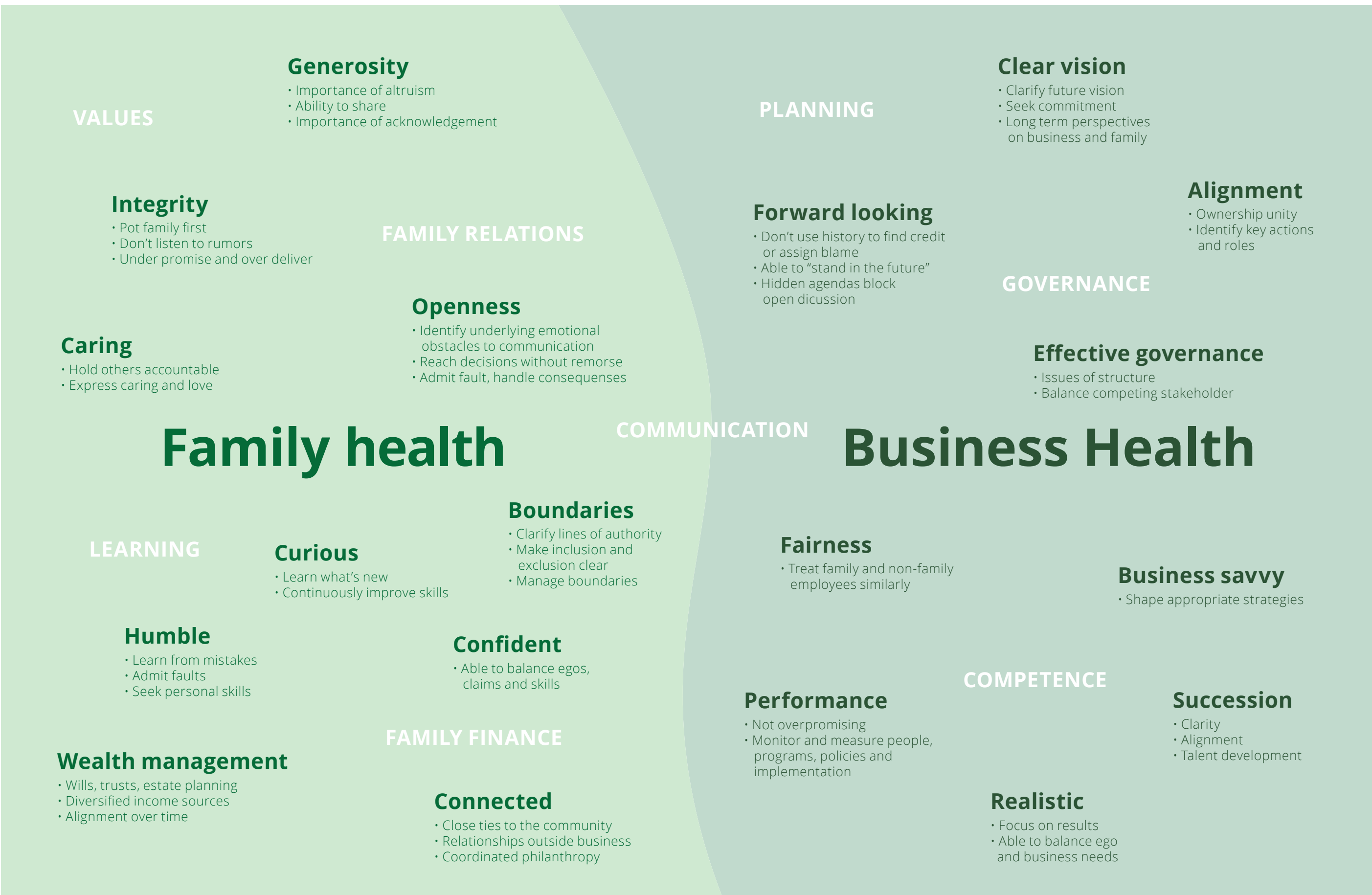
How well are you balancing family and business health?

Underlying family dynamics amplify or detract from the success of your business.

Well-managed family businesses outperform their listed competitors when family members develop strategies and governance processes to manage their interaction with the business. But, without defining the roles of family and business, or formally managing the overlap, the result can be fractured relationships, loss of wealth, destruction of business value and no legacy.

After decades of helping family enterprises work through complex issues, we have seen first hand the impact and correlation that a business issue has on a family's health – and vice versa

And a toxic family situation can be more disastrous than a bad business strategy. In our experience, a business problem causes family issues over the next 12-24 months. However, where issues emanate from family friction the business is impacted in a far shorter time frame.



As a result of working with many of the world's leading family businesses, Deloitte has developed a field model that helps families understand the interplay between business and family health. It helps family enterprises look through two lenses:

Business health	Family health
Planning	Values
Governance	Family relations
Competence	Learning
Communication	Family finance
	Communication

Red flags that your family health is not up to scratch

In terms of how it interacts with the business, family health depends on values and trust, concern and care for each other, a sense that the future needs to be different from but build on the present – and the confidence to pursue the family's ambitions.

Warning signs that these vital elements may not be in place include:

Lack of communication/ transparency

Communication is the vital link between the business and the family. Without a shared sense of values and an agreed strategy across the generations, family enterprises can lose their way. Often, families struggle to hold meaningful conversations about both family and business issues, which remain left unsaid, fostering resentment. Common danger signs are the lack of proper discussion forums and a 'black book' where the founder keeps a private record of who has been given what. Without the right facts, children make incorrect assumptions. And this is made worse if the family has lots of informal or piecemeal discussions – perhaps around the dinner table at the weekend, with kids running around and some family members absent or in the kitchen. Sometimes, siblings plead their case privately with one or other parent, resulting in informal 'promises' that rarely pan out, unintentionally creating more inequality. In other cases, no one is comfortable raising an issue for fear of being excluded from the next discussion.

Preceding generation still in control

Many family business leaders seem to perceive succession as an event that they would rather not acknowledge or deal with. Yet an orderly succession can be crucial to keeping the business on track for both the immediate and the far future. We've heard every excuse from founders struggling to let control pass to the next generation: "They're not ready yet. There's a big deal coming up." It often takes a health issue to force a handover, which is the worst possible time and way to manage transition. As a founder, it's important to set up clear roles, pathways, accountability and support structures for family members to be successful. Children need independence – including financial independence. Too many founders handcuff family members to the business by keeping all the wealth and family assets under their control. Parents like to appear to be supporting the next generation, but often keep looking 'over the fence' to make sure things are being 'done right'. That sort of subtle oversight can undermine children. The answer is to support the transition of power by setting (and respecting!) decision-making responsibilities.

Lack of education for the next generation

After generations of compound growth, some family businesses get so big it's hard for the next generation to learn all aspects of the enterprise. Do children know how the family business was started? Can they read financial statements? Do they understand their career pathway – or why they're being asked to work in certain parts of the business? We recommend starting early, rotating family members through various departments, encouraging them to gain experience with an outside company and ghosting senior executives. Zoom out sessions are particularly useful for educating younger family members and helping them to think about the business – and for you to see who the truly strategic thinkers are. These planning sessions offer younger generations the opportunity to engage in the process as challengers, questioning the sometimes long-held perspectives about the state of markets and where they are likely headed. This allows them to contribute immediate value to the business – and see their future in it. Their insights are also useful as they are fresh and often not biase d by what has led to success in the past.

Inequality among family members

Healthy family governance starts with leaders dealing with any unfairness issues. Little things can cause big cracks. We've seen families explode over grievances such as who gets the Frequent Flyer points, unequal use of family holiday homes, siblings on different salaries and spouses working in the business. The answer is a transparent system that includes market salaries for those in the business (so children are paid what the work they are doing is worth), and more clarity on the amount and timing of distributions. Setting the rules early and then sticking to them is key. Take for example the question of whether spouses should be allowed to work in the business – explaining that the family has a rule of "no spouses" maybe a more prudent path to take than having to deal with a non performing spouse, which from our experience can almost certainly cause irreparable damage to at least one branch of a family.

Lack of governance/structure

Formal governance structures can create an environment where discussions can be held about culture, values, and vision, which are essential if family members hope to agree on their company's direction. The benefits can include greater harmony among family members, a more focused business, and easier transitions between generations. So it's important to ask: When was the last time the whole family came together to formally discuss the business? Some families opt to sign a formal agreement stipulating their values, investment parameters, decision-making responsibilities and communications schedules. This is helpful and in our experience advisable, but the most valuable part is all family members getting together to jointly decide what those things look like and how they will happen. When they understand the big picture, family members settle down and stop making incorrect assumptions. Once appropriate forums are available, the right topics are discussed and communication is effective, many apparently intractable problems also fade away.

Even one or two of these red flags can be enough to bring down a family enterprise. With the right help and guidance all of the above issues can be managed and the increased alignment will assist family enterprises to run in perpetuity.

Case study

Success factors of a 200-year-old family enterprise

Japan has 33,000 businesses at least a century old, but one of its most famous companies has been operating for more than 200 years controlled by the same family. While using a strict Japanese, one-branch succession plan, the family is also open to using and combining global family governance and business management best practice with Japanese best practice to create a unique family governance model to ensure the sustainability of both the family, the family's wealth and the business itself. Drawing on the best advice and practices available, this US$2.5 billion business has navigated successfully through major domestic and international changes and has continued to go from strength to strength during the pandemic.

> On the family side, the eighth-generation patriarch has already identified two generations of successors.

The keys to its success are:

Multi-generational planning
On the family side, the eighth-generation patriarch has already identified two generations of successors. On the business side, this company started investing internationally at the turn of the twentieth century in response to its awareness of the shrinking Japanese population and changing customer preferences.

Zoom out to zoom in
The business always attempts to assess what its market/industry/customer preferences will be like decades in the future to determine how they need to change today. A similar approach is used to plan the family's governance.

Strong family governance
Everyone understands that long-term family survival and sustainability is the ultimate goal. Family governance measures are constantly updated. The whole family knows what the plan is – and everyone is involved. Regular communications make it clear where control is going and who does what. Every change comes with a risk assessment – communicated to everyone – of how it will affect the family structure and what could be the implications.

Separation of family and business risk
Personal assets are kept strictly separate from the business entity. The family believes the business can always be restarted as long as they retain the family unit, their joint experience and assets to carry on.

Never sell strategy
The business has always remained private and the family will never sell, no matter how much money could be generated through an IPO, prioritising family sustainability and legacy over quick profit maximisation.

Blended Japanese and western governance
The patriarch seeks out strategies used by other successful families around the world. As a result, the family office uses foreign structures like trusts and foundations and looks to jurisdictions that aren't necessarily tax minimising, but have a very good legal base. The family has also worked hard to align their corporate and family governance.

Professional family office CEO
Who does not come from the family, is very diligent and always looks to blend the best practice of Japan and the rest of the world to meet the family short- and long-term needs.

Put your family and your business to the test

At Deloitte Private, we've developed a Family Dynamics Program to help family enterprises understand where alignment may need to be improved within the family or the business, deep dive into core issues and check whether governance needs to be improved. Some of our proprietary tools to get families started include the following but the real value comes from our team who have worked through almost every conceivable family issue imaginable:

Family and Business Health Diagnostic

A great first step to work with the entire family around making an assessment of where the families strengths and opportunities are within their family and business. This diagnostics frames up the importance of family and business health and quickly leads to the creation of tactical actions that can be taken to reinforce, adjust or improve the factors that underline your chances on sustaining a well functioning family and business into time.

Family Interview Process

This process is a natural extension to the Family and Business Health Diagnostic. During this process we interview all of the family members 1:1. It gives each family member an opportunity to talk in confidence about matters important to them. During the sessions our experienced practitioners explore each family members views on a wide range of topics to better understand where the family is aligned or otherwise. After interviewing all family members we then report back to the family our findings and make recommendations on specific things each family can consider implementing to enhance the chances of future success for the business and the family – one of these may well be formalising the decisions that were agreed upon during the interview process into a family agreement.

Family Governance Health Check

Many families may have progressed a number of elements we consider to be "best practice" in Family Governance in their own right. Our Family Governance Health check is a quick way for us to assess the appropriateness and completeness of a families governance framework and provide suggestions on how it maybe improved.

There's no single model of family governance. It's a matter of looking at all types of best practice, choosing what resonates with you and tailoring them to your unique business, culture and family situation.

Talk to us about how to take a multi-generational outlook and find out what type of family governance will work for you.

Deloitte Private Family Enterprise Global Centre of Excellence

With 175 years of experience serving family enterprises in more than 140 countries, Deloitte Private brings multidimensional perspectives —a 360-degree view—across all the challenges and opportunities you might face as a family enterprise.

Our multidisciplinary and purpose-led approach ensures that we bring the right solutions to you at the right time– through a holistic lens of understanding the specific family enterprise issues and dynamics you might be facing.

Through our Global Family Enterprise Center of Excellence we bring together our global network of trusted advisors, collective leading practices, sector expertise, and digital tools to develop world-class, bespoke solutions, and data-driven insights.

Our people bring not only their deep experience and connections to other family enterprises, but also the full Deloitte organization to you.

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