

1

The Growth Dilemma in Family-Owned Firms

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IMD – International Institute for Management Development – has been the global meeting place for families in business since 1988. For almost two decades members of more than 600 families from more than 60 countries have been coming to IMD's campus in Lausanne for family business education. Most have participated in the renowned Leading the Family Business program; many other family business leaders have taken part in collaborative programs with the Family Business Network, with industry groups, and with IMD's Building High Performance Boards program.

Confronting this global diversity challenges IMD faculty to think wider and deeper and differently. Conventional paradigms of thought are tested as top executives from the world's most sophisticated businesses share their experiences and views. Learning at IMD is a two-way street. The faculty learn from successful family firms; families in business learn from the real-world research of the faculty. Conventional wisdom comes face to face with reality. New ideas and new insights are inevitable. Many are counterintuitive, at first. The real world is always more complex than current theory.

IMD prides itself on its constant quest for fresh and different thinking. It is able to facilitate this search as a result of its global perspective and its constant interaction – in the classroom and outside – with leading business leaders and owners. IMD is devoted to *developing* new practical knowledge, not just teaching it.

Nowhere is this philosophy more important than in family firms. There has been remarkably little research into family-controlled businesses, yet, with their very special challenges, they are in many ways a distinct type of business from which all organizations can learn. IMD is committed to providing the leadership to unlock these mysteries. IMD's Lombard Odier Darier Hentsch Family Business Research Center is devoted to developing ground-breaking research for the leading family businesses of the world.

While many things are different about family firms, compared with other companies, one thing is not: the imperative to grow the company. All too often family firms fail to appreciate that company growth helps fuel everything else; all too often they let their culture and family priorities block their ability to grow. But in the end, the issue is 'either you grow or you eventually go out of business.' There are, however, two particularly thorny issues when it comes to growth in family-owned firms. One has to do with the 'silos,' or 'kingdoms,' that can form within family firms as a result of their very nature. For example, certain family members with executive positions in the firm might feel that they have 'territorial rights' to some parts of the firm and do not necessarily see the need to communicate more broadly, in a more 'meeting place oriented' atmosphere. Whereas professional managers tend to realize that they must perform or be forced to leave, their family-business counterparts might see their jobs as absolutely secure.

A second issue that affects growth in family-owned firms has to do with developing 'internal entrepreneurs' so that they can function properly.

Here, the family-members-cum-owners often feel that they need to have total control over growth initiatives. They simply do not want to allow outsiders in to play the internal entrepreneur role. On the other side of the coin, professional managers might feel that younger family members will eventually be given such opportunities, so the motivation for taking on difficult, energy-consuming internal entrepreneur roles might be limited. It will therefore typically be hard to attract outsiders for such critical assignments.

A disguised case study will illustrate these issues. The two above-mentioned challenges are of course found in *all* corporations, not only in family-controlled firms. But, as we shall argue, they can often be particularly difficult to cope with in such a setting.

Case study

Company X is a third-generation family-owned firm, with the family holding all of the shares in the company. Not surprisingly, the CEO is a family member. He has two sons and a son-in-law actively involved in the business. There are three divisions, one of which is run by one of the sons. The other two divisions are run by outside professionals. The other son is the chief strategic officer, a staff position. The son-in-law is presently a special projects manager, working on ad hoc business development issues.

The company employs more than a thousand people and has been growing at a strong rate, with a compound average of 10% per year sales growth over the last five years. The profitability of the company has also been strong. Moderate dividends have been paid out to the family members, but the

board, consisting entirely of family members, has reaffirmed the long-term objectives of the firm, namely to be willing to invest for future growth, and therefore to pay only relatively moderate dividends. Realistic growth is therefore *the* key agenda item.

Recently, however, the company has faced two difficult issues relating to growth, as follows.

Silos, kingdoms

As noted, one of the sons heads one division; outside professional executives head the other two divisions. Over time, a culture has developed in which each division sees itself as entirely freestanding. Know-how, technologies and clients have come to be viewed as divisional property, not as corporate-owned assets. Could this perhaps eventually limit the firm's growth prospects? Indeed, the CEO had belatedly reached this conclusion – but how could the firm crack this silo mentality?

Specifically, how could a 'meeting place' culture be developed between the divisions so that opportunities could be examined in a broader context? For example, if the strengths of the various divisions were considered together, this might reveal new strategic opportunities for the whole firm. Thus, perhaps clients that have traditionally been served by one division could be addressed on a broader, company-wide basis. Furthermore, by combining the intellectual efforts of the entire management team, not only drawing on the know-how of the subteams in each division, specific challenges could perhaps be handled more effectively.

The problem, however, seems to be that each division has become too accustomed to being on its own and its attitudes are quite entrenched.

In particular, the behavior of the son who is division president seems to promote this. He feels that it is essential for him to have a degree of independence – a certain mandate – relative to his father, whom he sees as rather dominant. Also, he feels that his position gives him a right to independence, more generally, compared with the rest of the family. His way of coping is to say, ‘Leave me alone to run my division and don’t interfere with me.’ While the CEO/father clearly appreciates this to some extent, it also seems to be the case that the dynamics of the father–son relationship – or more broadly the relationship between any family members working together – often leads the ‘junior’ party to feel the need to retain independence. Family-specific arguments can, however, be taken too far – even to the extent of being used as an ‘excuse’ for having silos! After all, companies are meant to be communities of executives working together, so using a family relationship and the need for sibling independence as an ‘argument’ against a broader ‘meeting place’ cooperation might be seen as dysfunctional.

With the division run by one of the sons taking such an independent stance, it is easy to see why the other divisions have developed similar behavior. They are also using the precedents set by the family-member-led division as the basis for developing wider independence and autonomy. The net effect has been that Company X has not been able to create a ‘meeting place’ culture, where opportunities are pursued on a broader basis, where potential challenges or even problems are resolved based on the maximum capabilities of the group, and where technical and commercial assets are in effect seen as ‘suboptimal’ when they relate to a particular division only. Clearly, the ability to pursue effective growth is at stake here. An inbuilt tendency for family-owned firms to develop a particularly strong silo mentality can indeed result in growth being compromised.

The internal entrepreneur dilemma

Internal entrepreneurs are typically needed to help spearhead internally generated growth. Such internal entrepreneurs need to have *both* an ability to see business opportunities before they are obvious to everyone else, i.e., a clear commercial sense, *and* an ability to know where the internal resources are in the firm and to be able to draw on all of them – as well as on resources from outside if they are not available internally. They must be able to inspire and lead typically ‘flat,’ new business development teams, relying on their own innovative leadership capabilities, rather than on a hierarchical sense of power and control. The internal entrepreneur clearly needs to be close to the CEO, who can provide the necessary backing and support for the usual requests for additional resources, as well as recognizing the need to take certain risks. The CEO can also offer ‘cover’ when critical voices are raised, as so often happens with growth projects. Perhaps paradoxically, the internal entrepreneur also needs a certain distance from the CEO, i.e., the freedom to maneuver, to move fast, without the constraints of micro-management and having to ask for permission to do everything.

What, then, are the problems when it comes to developing internal entrepreneurs in the family firm? And why is the ideal profile for an internal entrepreneur in the family-owned firm so hard to develop? In the case of Company X, for example, should the CEO/father appoint his son who is the chief strategic officer to spearhead internal entrepreneurship, or should he ask his son-in-law to do it as part of his ad hoc business development? Or should he ignore the family and choose an outsider for the role?

First, when it comes to seeing business opportunities, family members may not always find it easy to ‘tolerate’ the idea of an outsider having a more insightful approach to the business. All too often, the situation arises because

family members feel that they 'know best' what a good business approach is – and that they need to know best because of their position. They might find it difficult to allow others to come up with 'more insightful' ideas. Clearly, on the one hand, it might be hard for an internal entrepreneur from the outside to compete with the family and, on the other hand, an internal entrepreneur from the family itself might be too shortsighted in his or her views on new breakthrough business opportunities.

Second, identifying *where* the resources can be mobilized *from* can also be a difficult task in the family firm. Family members often have particular favorites – sympathies and antipathies – in terms of both business areas and employees. Thus some parts of the firm might be called on heavily for business ideas and support, while other parts might be ignored through lack of understanding of what they can offer. Similarly, when it comes to outside resources, some family members might have particular views on *which* outside entities to work with, often based on other motives, such as previous family history, past conflicts or friction. The net result is that in a family firm it might be more difficult to mobilize the optimal mix of resources needed to go after a new growth opportunity. If a family member is the internal entrepreneur, he or she might have a rather shortsighted, even blinkered, view of where the relevant resources might be. Conversely, if the internal entrepreneur is a non-family member, there might be too many 'sacred cows' that he or she cannot mobilize.

Third, when it comes to inspirational leadership, which is so critical in growth-oriented, project-based 'flat' team initiatives, it can perhaps be more difficult for a family member to play the role of an effective catalyst. The perception might be that he or she has the mandate by inheritance. Whether the family member in question is competent or not can often be difficult to 'prove,' since the rest of the organization typically assumes – often

justifiably – that he or she attained the position through the family connection and did not necessarily earn it by performing well. Hence, it is often difficult for a family-member-cum-internal-entrepreneur to effectively lead a growth team. But the dilemma in deciding who to appoint is that a non-family internal entrepreneur might find it equally difficult to lead the growth team, given that he or she will have to rely on family members for legitimacy and the power to perform the leadership tasks in question. And, above all, how can he or she have a deeper business insight than the family members who have grown up in the business?

Fourth, as noted, the CEO should in theory give the internal entrepreneur ‘cover,’ so that resources can be allocated to the growth project on a strategic basis to achieve a breakthrough dimension – *not* merely incremental extensions of the present situation – and so that the inevitable risks can be taken. In practice, it is often hard for a family firm with a family CEO to allow a non-family member to enjoy this independence and accord him or her the necessary support. The family CEO may want to reserve these types of powers for him- or herself and/or for close family, say, offspring. By contrast, in the case of a family member who is the internal entrepreneur, the issue might be that the CEO family member cannot be seen to be favoring one of his family over the others. The family CEO may therefore be reluctant to provide special support to one family member and not to the others. Once again, the result might be a weakened internal entrepreneur function.

Finally, when it comes to the ‘distance’ between the CEO and the internal entrepreneur, the arguments follow similar lines. A non-family internal entrepreneur might not be given sufficient freedom and distance because the CEO and/or other family members may, deep down, resent having someone outside the clan running new business initiatives. If, on the other hand, it is a family member who is the internal entrepreneur, the CEO

might find it equally difficult to grant him or her the necessary freedom, at the expense of the others.

Overall, establishing an effective platform for internal entrepreneurs in a family firm can be difficult. Whether the internal entrepreneur is a family member or not, there are deep dilemmas.

Any solutions?

It is, of course, difficult to come up with simple solutions to these dilemmas. Perhaps one of the most important factors to recognize is that internally generated growth depends fundamentally on a number of organizational culture issues – and these need to be addressed whether it is a family firm or not. Specifically, a growth culture needs to encompass:

- A ‘meeting place’ cultural dimension, where opportunities are discussed on a wider basis, say, once a month for a day or so, and typically with a rather open-ended agenda. These ‘retreats’ should be as free-flowing as possible, with no hasty decisions taken or quick conclusions drawn; they should simply be a brainstorming forum. Perhaps through this sort of experience, one might see the benefits of such a ‘meeting place’ culture when it comes to creating more powerful ideas for growth.
 - A ‘must do’ cultural dimension is also key. In family firms, the concern that everyone has for each other might typically lead to slow decision-making. People do not want to hurt each other’s feelings. Again, an open, brainstorming ‘meeting place’ approach might lead to more of a ‘must do’ culture.
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- A clear business plan pointing toward growth is also necessary, where one builds on established strengths, either by taking these strengths into new markets and/or by selectively adding new competences to broaden the business base, by carefully adding to the strengths. Here, experience has clearly shown: internal entrepreneurs are typically *critical* for spearheading these growth initiatives based on one's strength. Again, the realization that business growth is not magic, but simply depends on using the positions one has already established, might serve to depoliticize the image of the internal entrepreneur, might make the internal entrepreneur more legitimate. Perhaps this can help to develop a climate of acceptance of internal entrepreneurs in family firms, to establish a more realistic basis for growth.

Conclusion

Family firms often respond well to the growth challenge, and their performance reflects this. There is no doubt that they can have many advantages – particularly relative to large publicly traded firms, which are often overly complex and political. The challenge for the family-owned firm is to make sure that politics stemming from family dynamics are minimized and that bureaucracy is not allowed to develop based on family considerations. The following chapters of this book raise particular dilemmas for family firms and show the unconventional approaches successful family firms around the globe have used. In these chapters, IMD faculty members share their counterintuitive thinking as they tackle the real-world issues of enterprising families.

References for further reading

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