

The Arts of Family Business Continuity – Beyond Best Practices

Fundación Rafael Del Pino

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The Family Business Consulting Group
International

Outline

- **Review the Field of Family Enterprise Over the Past 25+ Years.**
- **Propose *the* 10 Best Practices – and Their Limits.**
- **Explore Beyond Best Practices for Essential Capabilities – the Arts of Continuity.**

First, Some Background

- **Family Business Demographics**
- **Family Business Challenges**
- **Fundamental Family Business Dilemmas**

Family Business is Significant

- USA:** 20% of 1000 largest listed firms are family firms;
60% of 55,000 publicly traded
- India:** 20 groups (16 family controlled) = 66% private
sector assets
- Chile:** 15 family groups > 50% Santiago Stock Exchange
- Korea:** 10 family groups (Chaebols) = 60% GDP (2001)
- Sweden:** Wallenbergs control 45% market cap
- Hong Kong:** 15 family groups represent 84% of GDP
- Philippines:** Ayala family controls 25% market cap

Family Businesses in Holland

<u># Employees</u>	<u># Companies</u>	<u>% Family Businesses</u>
1-9	450,000	80%
10-100	45,000	77%
>100	4,000	45%

<u>Generation</u>		
1 st	41%	70-80% Owner-Managed 67% ≥ 3 Owners
2 nd	26%	
3 rd	21%	
4 th +	12%	

“Shirt Sleeves to Shirt Sleeves”

Padre Bodeguero

Hijo Millonario

Nieto Pordiosero

Förvärva

Ärva

Fördärva

Erwerben

Vererben

Verderben

富
不
過
三
代

Pai Rico

Filho Nobre

Neto Pobre

La première génération la crée

La deuxième la développe

La troisième la tue

Theseus

Pericles

Alcibiades

Haveli ki umar saath saal

“The children of the children are indifferent.”

- Shakespeare

“Generations pass while some trees stand, and old families last not three oaks.”

**- Sir Thomas Browne,
Hydriatophia, 1658**

Shirt Sleeves to Shirt Sleeves

I must study politics and war that my sons may have liberty to study mathematics and philosophy, geography, natural history, naval architecture, navigation, commerce and agriculture in order to give their children a right to study painting, poetry, music, architecture, statuary, tapestry and porcelain.

**John Adams
Paris, 1778**

Let us now return and explain the genesis of the democratical man. An oligarchical father has a son whom he brings up on narrow and parsimonious principles. The young man tastes the honey of drones, and sedition is engendered within his soul. A struggle ensues, the unnecessary desires prevail and the young man becomes an impartial devotee of pleasure in all its forms and consequently a follower of democracy.

Plato

WHY?

- 1. Next Generation Competence**
- 2. Senior Generation Keeping Control**
- 3. Sibling Conflict**
- 4. Disparate and Disinterested Cousins**
- 5. Economic Freedom**
- 6. Limited Capital**
- 7. Business Challenges**

WHY?

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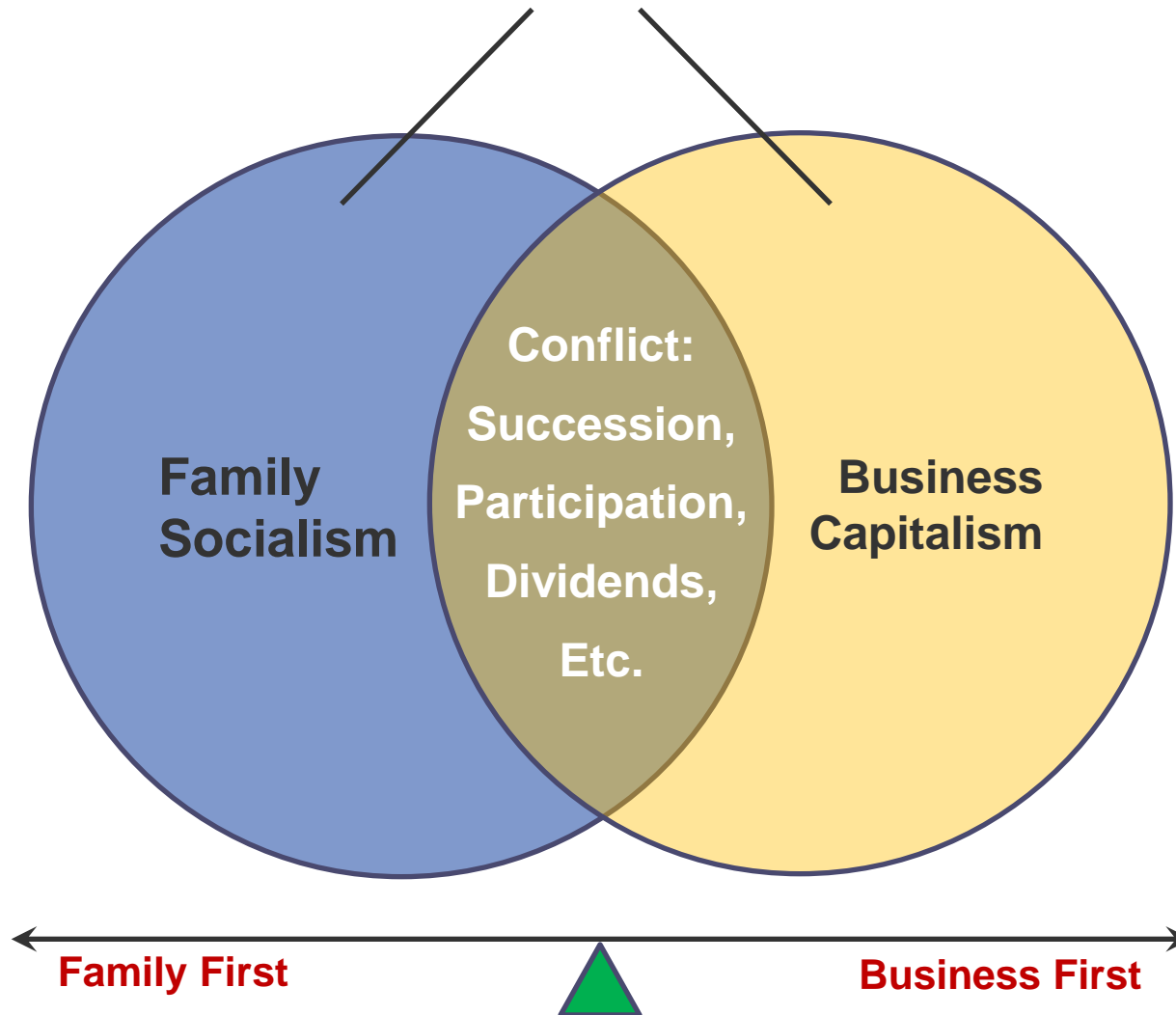
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Fundamental Family Business Dilemma

Is There a Paradoxical Synthesis?



Performance and Demography of Europe's Mid-Sized Companies

(250-5000 employees in France, Germany, UK, Italy and Spain)

Total Companies: 34,000

#FBs	38%
Turnover FBs	44%
Job Creation	55%

Performance (2005-2007)

	<u>Non-FB</u>	<u>FB</u>
Jobs Created	+5%	+13%
Turnover Growth	+17%	+21%
Cash Flow Growth	+21%	+33%
ROE	20%	25%
Asset Renewal	36%	40%

BEST OF THE BEST

A NEWSWEEK study shows family firms outrunning their rivals on all six of the leading stock indexes in Europe, and ranks the top 10 companies

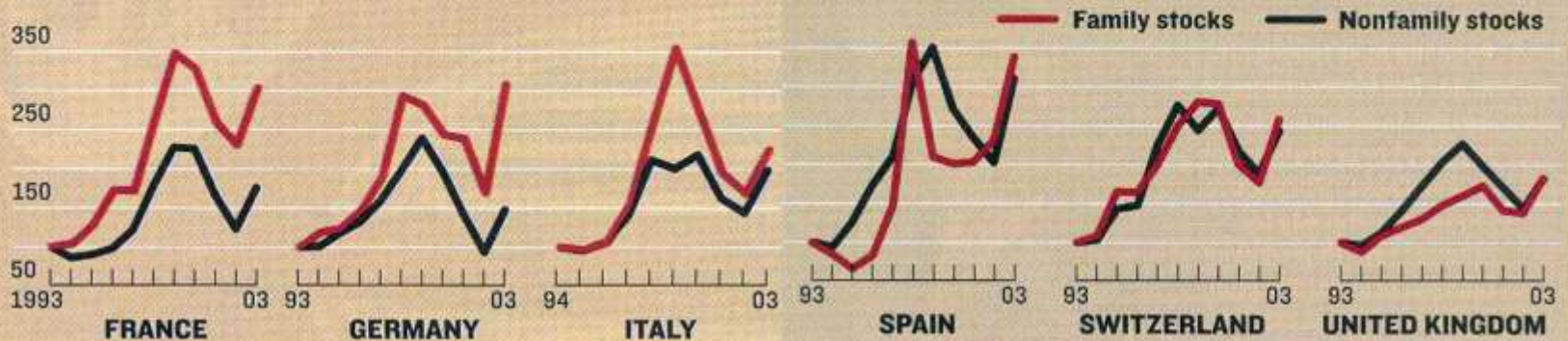
April 12, 2004, p. 42

The Family Factor

A Thomson Financial study for NEWSWEEK compared family firms with rivals on the six major indexes in Europe, and ranked the top family company stocks, with surprising results.

CHARTING A HOT BUSINESS MODEL

Companies with a big family shareholder outperformed on six key indexes.



...and Continue

FBs: 20% → 50 years

S&P 500: 15% → 40 years

McKinsey 1000: 14% → 37 years

Kellogg 1000: 30% > 100 years

The Professional Business Paradigm

“The separation of ownership and control [management] is essential to the development of the modern economy and the modern corporation.”

*Berle and Means 1932
The Modern Corporation
Harvard Business School Press, and
Alfred Chandler, Strategy and Structure*

The Family Business Paradigm

For the Family Firm

The purpose is continuity

The goal is to preserve the assets and reputation of the owning family

The fundamental belief is that the first priority is to protect downside risk

The culture is values driven first

The strategic orientation is adaptation

For the Non-Family Firm

The purpose is maximizing near-term share price

The goal is to meet institutional investor expectations

The fundamental belief is that more risk promises more return

The culture is strategic fit

The strategic orientation is constant growth

The Family Business Paradigm

(continued)

For the Family Firm

The strategic orientation is adaptation

The management focus is continuous incremental improvement

The most important stakeholders are customers and employees

The business is seen as a social institution

Leadership is stewardship

For the Non-Family Firm

The strategic orientation is constant growth

The management focus is innovation

The most important stakeholders are shareholders and management

The business is seen as a disposable asset

Leadership is personal charisma

Different Values

Non-Family Business

Innovation
Empowerment
Teamwork
Change
Leadership
Efficiency
Quality
Creativity
Learning
Customer Service

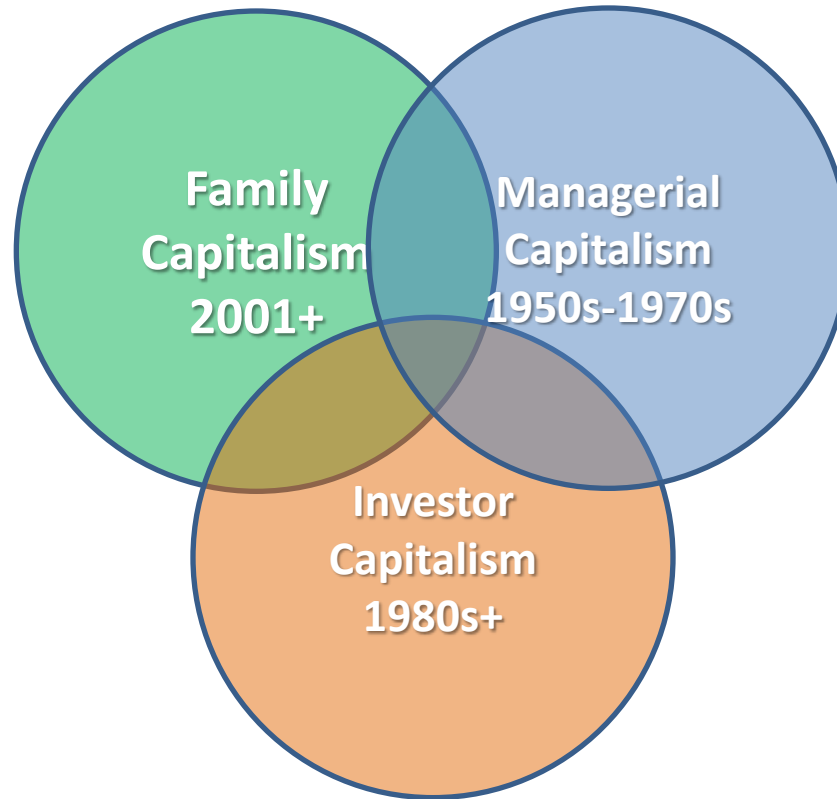
Family Business

Courage
Dignity
Fairness
Open-mindedness
Authenticity
Hard Work
Dependability
Curiosity
Humility
Do The Right Thing

The Field of Family Enterprise

ENRON, etc.

**Anderson-
Reeb, etc.**

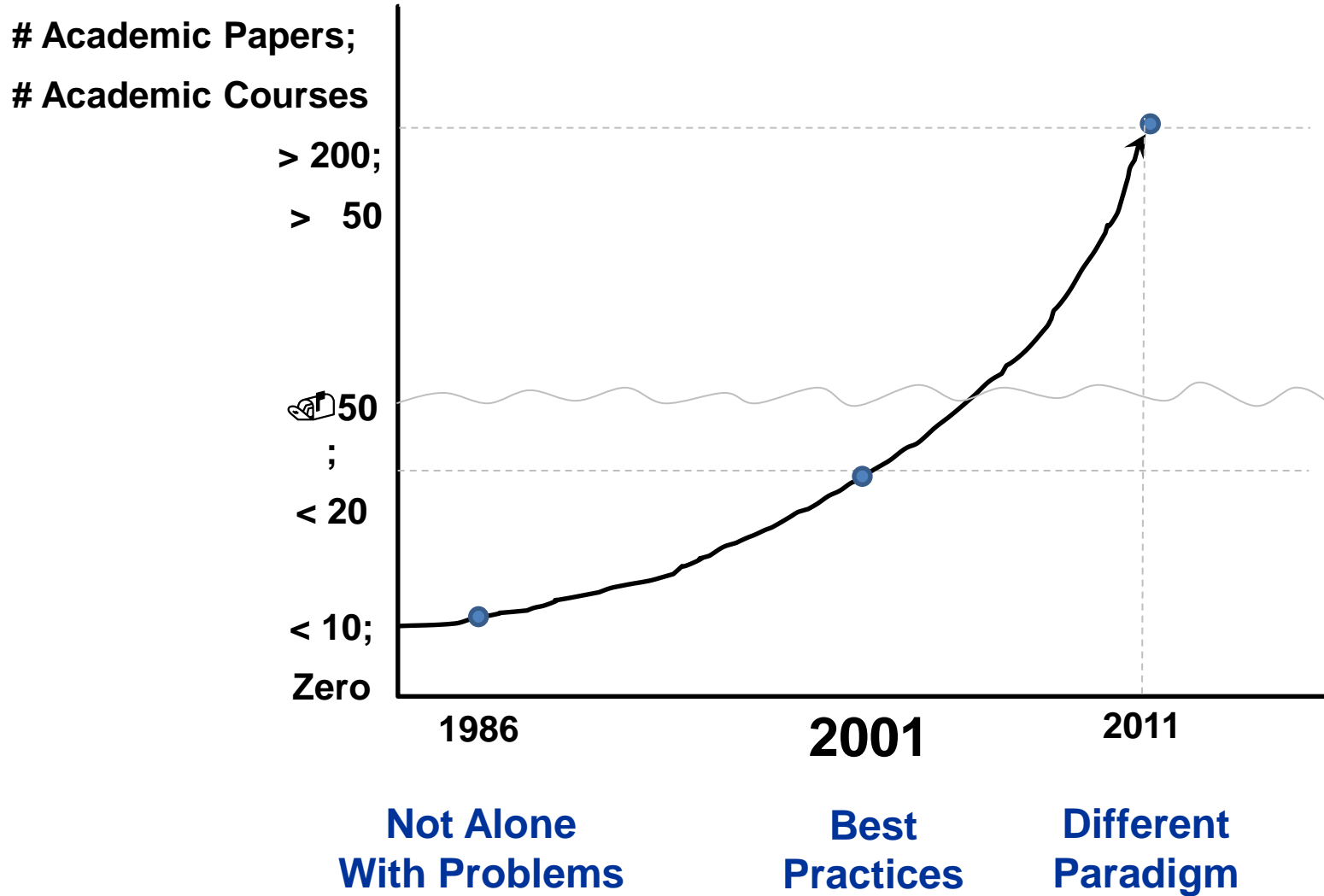


**Enlightened
Statesman
Committed to
Company**

**Self-Interested Agent and
Impatient Owner**

**⑧ Action, Heroes,
Transformations**

The Field of Family Business



From Best Practices to Essential Capabilities

- 1. Succession Plan**
-)(2. Family Employment Policy/Outside Work Experience**
- 3. Family Constitution**
- 4. Independent Board**
- 5. Family Council**

From Best Practices to Essential Capabilities

(continued)

6. **Family Meetings and Education**
7. **Shareholders' Agreement and Redemption Policy**
8. **Portfolio of Engagement Opportunities**
- ⌘ 9. **Appreciate Competitive Advantages and Distinctive Capabilities of Family Capitalism**
- ⌘ 10. **Implementing Family Business Culture and Performance Management**

#1 Succession Plan

“Letting Go”

“Taking Charge”

“Choosing”

and

“Implementing”

**The beginnings:
Attracting NxG**

**The endings:
Succession Task Force**

Attracting NxG

1. Internships
2. Early Interactions
3. Family Harmony
4. Frequent “Tweets”
5. Some Ownership
6. Education in Family Business
7. Outside Experience
8. Parents’ Expectations
9. Excellent Governance
10. Formal Reports

**Adapted from Bjornberg &
Nickelson plus Ward**

By the Way...

Kellogg MBAs 5 Years Out

Intended to Join: 80% Do

Unsure to Join: 22% Join

No Intention: 22% Join

The Succession Task Force

WHO?

WHEN?

WHAT?

Communications

Strategize Stakeholder Relations

Remuneration

Board and Advisor Evolution

Monitor Culture

Symbols & Ceremonies

Family Career Impacts

Organizational Development

Etc.

⑧ Facilitate Transition

Therefore,

Continuity Planning

#2 Family Employment Policy and Outside Work Experience

YES, 60% and 60%

BUT

**“How to really develop next
generation leaders?”**

Is it Possible?

CONTEXT

What is Leadership?

Not Charisma → **Humility**

R. Khurana, Harvard

Beyond Skills and Knowledge → **“Practical Wisdom”
(Phronetic Leadership)**

Nonako & Takeuchi,
Hitotsubashi U., Tokyo

Our 7 Myths of Successor Leadership

Charisma Trap

- **#1 Perceived Quality**
- **Founders were charismatic; successors want to be; *luckily* they are not likely so**

Nigel Nicholson, LBS

- **CEOs as Heroic Visionaries and Transformers**

— **Another Product of Investor Capitalism**

Problems with Charismatic Leaders

- **Belief in the superiority of change**
- **Overestimated impact on results**
- **Destabilize organization and culture**

*“The Curse of the Superstar CEO”
Harvard Business Review*

Instead, Humility

- **Know strengths and weaknesses**
- **Select complements**
- **Accept Context and Complexity**

Limits of Knowledge

“The scientific, deductive, theory-first approach assumes a world independent of context and seeks answers that are universal and predictive.”

Rather, Practical Wisdom

Experience, guided by morals and values for prudent judgments

Phronesis

Toku

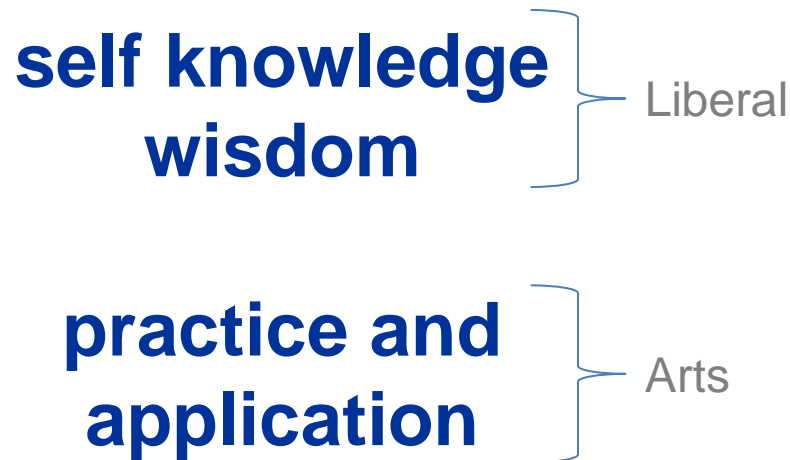
Yukta

Source: Nonako & Takeuchi

Peter Drucker, too

“Management is the last of the liberal arts.

“The fundamentals of the liberal arts are



**“We need to bring art back into management,
thinking and teaching...”**

In other words,

“Do the Right Thing”

...of course

How to Develop?

- **23 Principles***
 - **One Win, Nine Losses***
 - **5 Times Why? Purpose of Company**
 - **Apprenticeships and Mentors**
 - **Stories and Metaphors**
- and...**

*Tadashi Yanai, Fast Retailing/Uniglo (Japan)

Both/And Synthesis

(“Aufheben”)

“Phronetic leaders understand it’s essential to appeal to both logic and emotion

and also strive to understand all the contradictions of human nature

good and bad

civil and uncivil

optimistic and pessimistic

diligent and lazy

and, more than balance them, synthesize them at a higher level.”

One More Family Successor Advantage

Idiosyncratic Experience and Knowledge

Passing on a Legacy

Jacques-Yves Cousteau (100)

Creativity

Researcher

Determination

Photographer

Passionate about youth

Film Maker

Vibrant Energy

Inventor

Ability to seek out hope

Adventurist

Story Teller

Jean-Michel Cousteau

Ocean Futures Society

Philippe Cousteau

To 1979 Seaplane
Oceanographer

SOURCE: "Cousteau's Legacy", Susan Castle, 2010

Passing on a Legacy

“People will protect what they love”

Fabien (43)

Environmental economics
Quit office NGO job
PBS Ocean Adventures
Plant a Fish
Shark submersible

C☺line (38)

Cause Centric Productions
Tells environmental stories
TV series in Chile
Reefs at Risk

Alexandra (34)

Earth Echo
National Geo Explorer
Bio diesel bus
Colorado River Watershed
Uses all social media to tell stories

Philippe (30)

First film of BP for ABC/CNN
Students Reporting Environmental Action
(Citizen Journalist)

“We are not Cousteaus because of our birth certificates. We are Cousteaus because of the values we share and the actions we take on behalf of our planet. That’s a legacy each and every one of us can share.”

SOURCE: “Cousteau’s Legacy”, Susan Castle, 2010

A Family Successor Disadvantage

- **Feedback**
- **Career Pathing**
- **Coaching**

Our Belief,

Family Human Resources Committee

Our Lessons, 7 Myths

Operator	→	Active Owner
Entrepreneur	→	Champion
Visionary	→	Culture
New Strategy	→	Strategic Processes
Charisma	→	Servant Leadership
High Reinvestment	→	Personal Financial Security
Change	→	Enduring Values

Liberating Family Leader Myths

John L. Ward

Very often family business successor generations place a heavy burden of inappropriate expectations on themselves. These expectations and their weight come from past paradigms, no longer true. We present some in the following schema:

1. You don't have to be an operator employed full time in the enterprise. Instead, you can contribute very valuably as an active owner assuring good governance and providing caring oversight and support.
2. You don't have to be an entrepreneur who invents new sources of wealth. Instead, you can champion existing ideas.
3. You don't have to be a strategic visionary for the enterprise's future. Instead, you can seek excellence in all the enterprise does – especially its culture, with a continuous improvement spirit.
4. You don't have to be the author of a new strategy. Instead, you can lead processes that gain the strategic ideas of others.
5. You don't have to be a charismatic leader to achieve the ends. Instead, you will earn authority and effectiveness by being a servant leader for the aspirations of others.
6. You don't have to reinvest all the profits to protect the enterprise. Instead, you can embolden the business to be more ambitious and unconventional by providing owners with some personal financial security.
7. You don't have to lead dramatic transformation change to earn credibility. Instead, you will earn respect faster by emphasizing the enduring values you don't intend to change.

#3 Family Constitution

+ 50% Do

< 50% Successfully

7 P's of Highly Effective Family Agreements

- **Positive**
- **Personal**
- **Philosophic**
- **Professional**
- **Participative**
- **Process & Project**
- **Paradoxical**

SOURCE: Montemerlo & Ward, 2005

Process over Policies

Best,

Preambles

Participation Policy Preamble

(900 Words)

As a family we have drafted this participation policy for future generations. Before you read it, we want to explain why we have written a policy that at first reading might sound overly restrictive. There are several issues that this letter will address:

- 1) The role of merit in hiring and advancement**
- 2) The importance of family values**
- 3) The hiring of family members at the management level & potential for executive leadership**
- 4) The value of outside experience**
- 5) The ineligibility of spouses and their relatives for employment**

Participation Policy Preamble

(900 Words)

- 1) Be believe... as an individual, you have the best chance for success when you are in a job that you are prepared and qualified for. Self worth is very much tied in to being productive and successful at work, whatever field or type of work one chooses.
- 2) ...when a family member is employed by the company he or she is naturally held by all concerned to a higher standard than other employees
- 3) We believe that for the sake of family equity and harmony, as well as for the good of the company, qualified family members should enter the business at middle management or above... Having family members in a lower level positions can create distortions in the workplace hierarchy; etc.
- 4) Along with this Preamble you should also find a letter your uncle/father has written on the value of outside experience. His letter explains the thinking behind that part of our Participation Policy...
- 5) ...however we believe it is best to exclude spouses and their relatives from future employment at ABARTA for several reasons. With 17 members of the 4th generation we already have a very large talent pool for the future; etc.

Your family worked long and hard drafting this Participation Policy. It took about five years for us to come up with a policy that we all could feel comfortable endorsing. Along the way there were lengthy deliberations and tough decisions. Please understand that this policy was created to ensure continued success for our family business without compromising our family values and standards. It was written with the utmost love and compassion for future generations of this family.

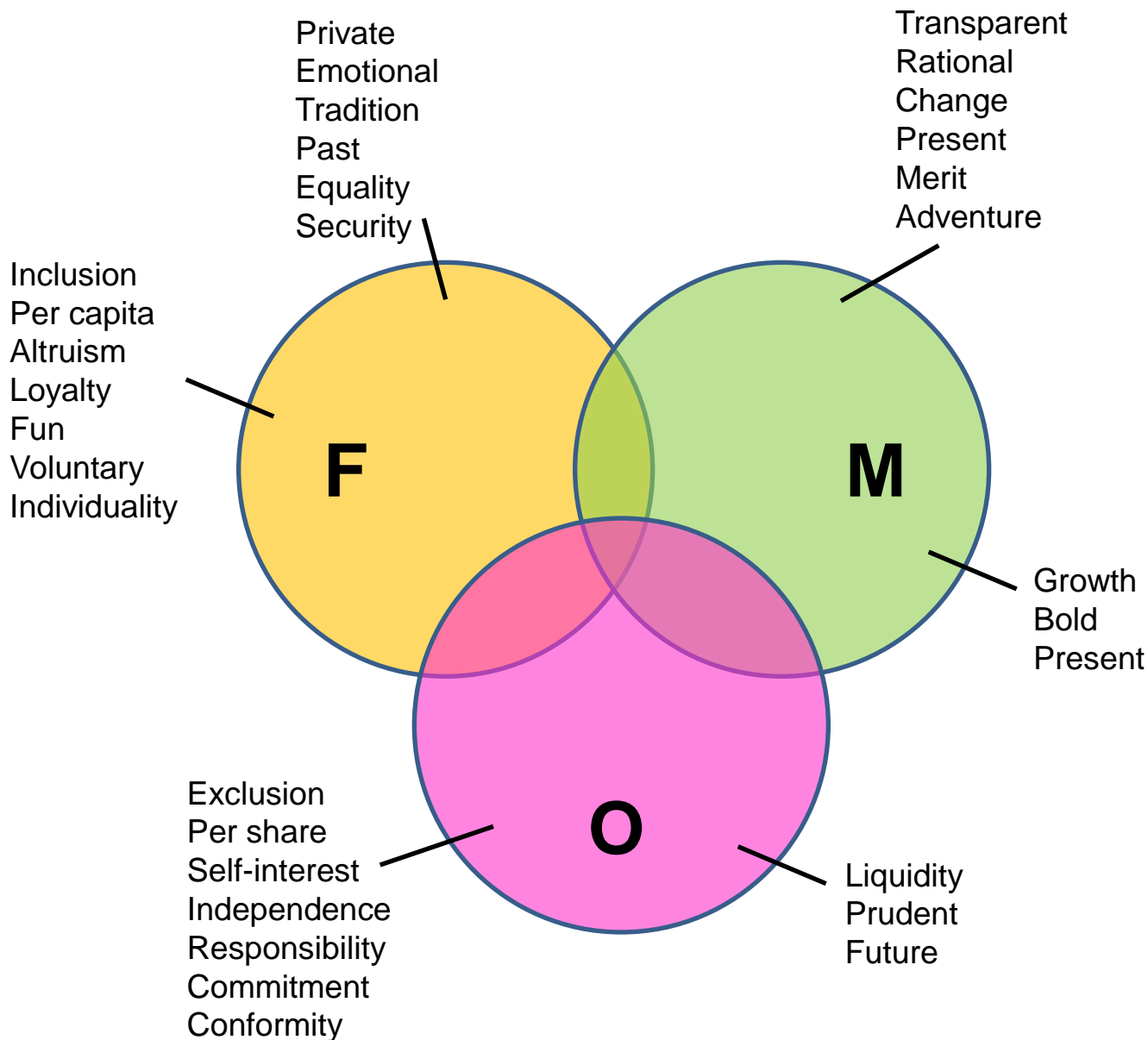
Family Constitution (continued)

- **Family Statement**
 - **Values, Vision, Principles**
 - **Family Mission**
- **Protocol/Family – Business Policies**
 - **Policies & Procedures**
 - **Charters of Roles, Responsibilities and Expectations**
 - **Commitment to Business Continuity**
- **Owners' Charter**
 - **Shareholders' Agreement**
 - **HOW OWNERS ADD VALUE**

#4 Independent Board

- **Evidence is Persuasive – yet 15-20%**
- **Questions Many:**
 - **Who Nominates?**
 - **Interaction with Family?**
 - **Holding Company – Subsidiaries Roles?**
 - **Mixed Ownership?**
 - **Governance Values Contradictions?**
 - **Building Trust!**

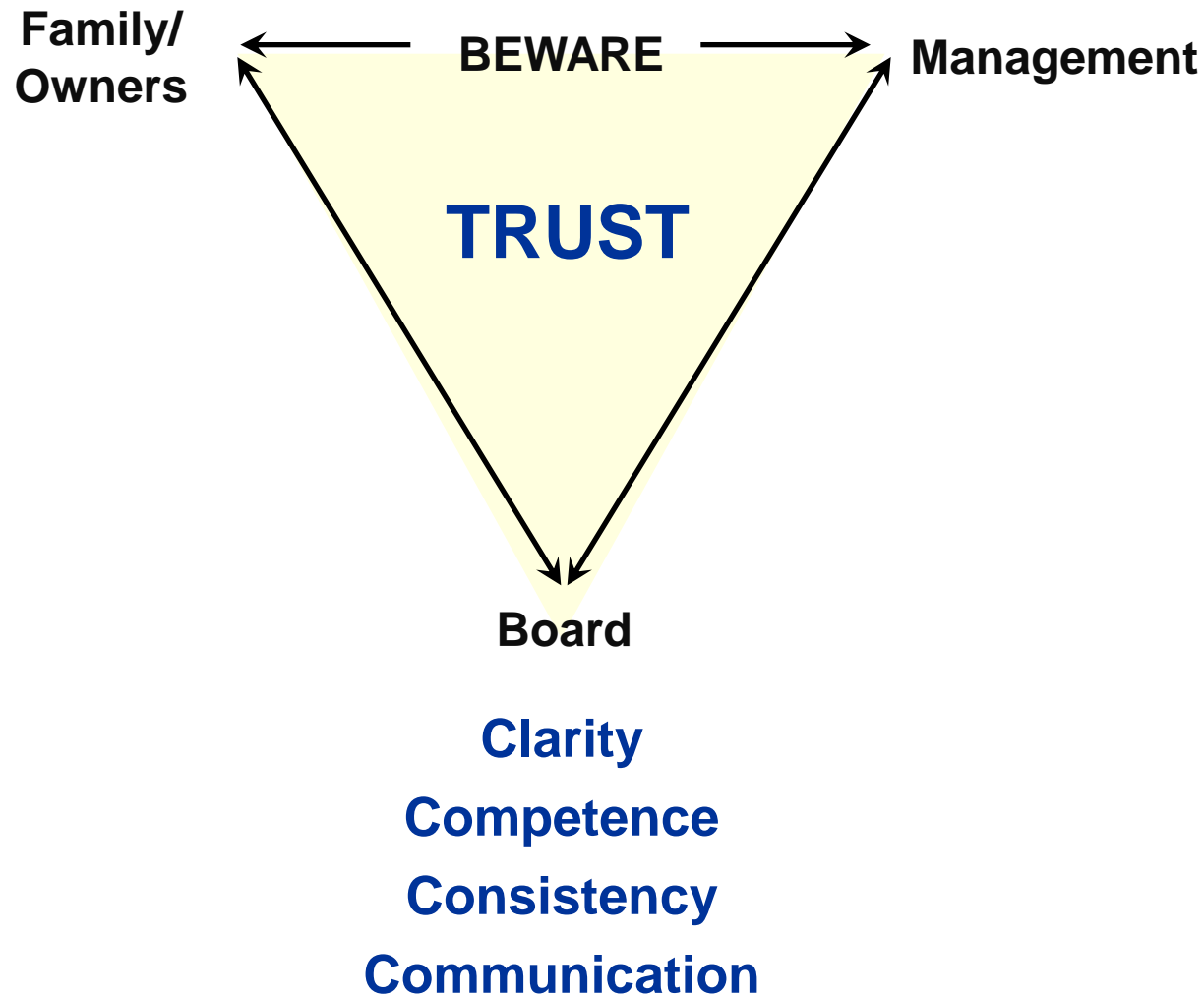
“Tricky” Family Enterprise Governance Contradictions



Ranked of 35 “Tricky Issues”

- **Family Council – Owners’ Council**
- **Family Member Accountability**
- **Burnout and Apathy**
- **Nose In – Fingers Out**

TRUST: The Ultimate Family Business Competitive Advantage



SOURCE: "How Values Dilemmas Underscore the Difficult Issues of Governing the Large, Enterprising Family", John L. Ward, Family Values and Value Creation, Palgrave 2008

Essential Capability

Non-Employed Family on Board **60%**

Family Education for Board Role **20%**

#5 Family Council

ONE BUSINESS

ONE FAMILY

How “Professional” is the Family Council

- **Merit**
- **Assessment**
- **Development**
- **Compensation**
- **Elected**

MOST IMPORTANTLY

)WHY FAMILY?

WHY FAMILY?

“A family is a community in a world where connectedness is increasingly difficult to find...”

Scott Family

“We recognize that our families have provided us with a strong platform for success, and we believe that a sustained, positive experience of family will continue to bring us together and provide similar opportunities to those that follow...”

#6 Family Meetings & Education

Key Functions:

1. **Family Decision-Making & Governance**
2. **Background Information**
3. **Social/Fun**
4. **Education**
 - **38% family history and values**
 - **38% business, industry, finance**

Family First or Business First Curriculum?

Personal Health

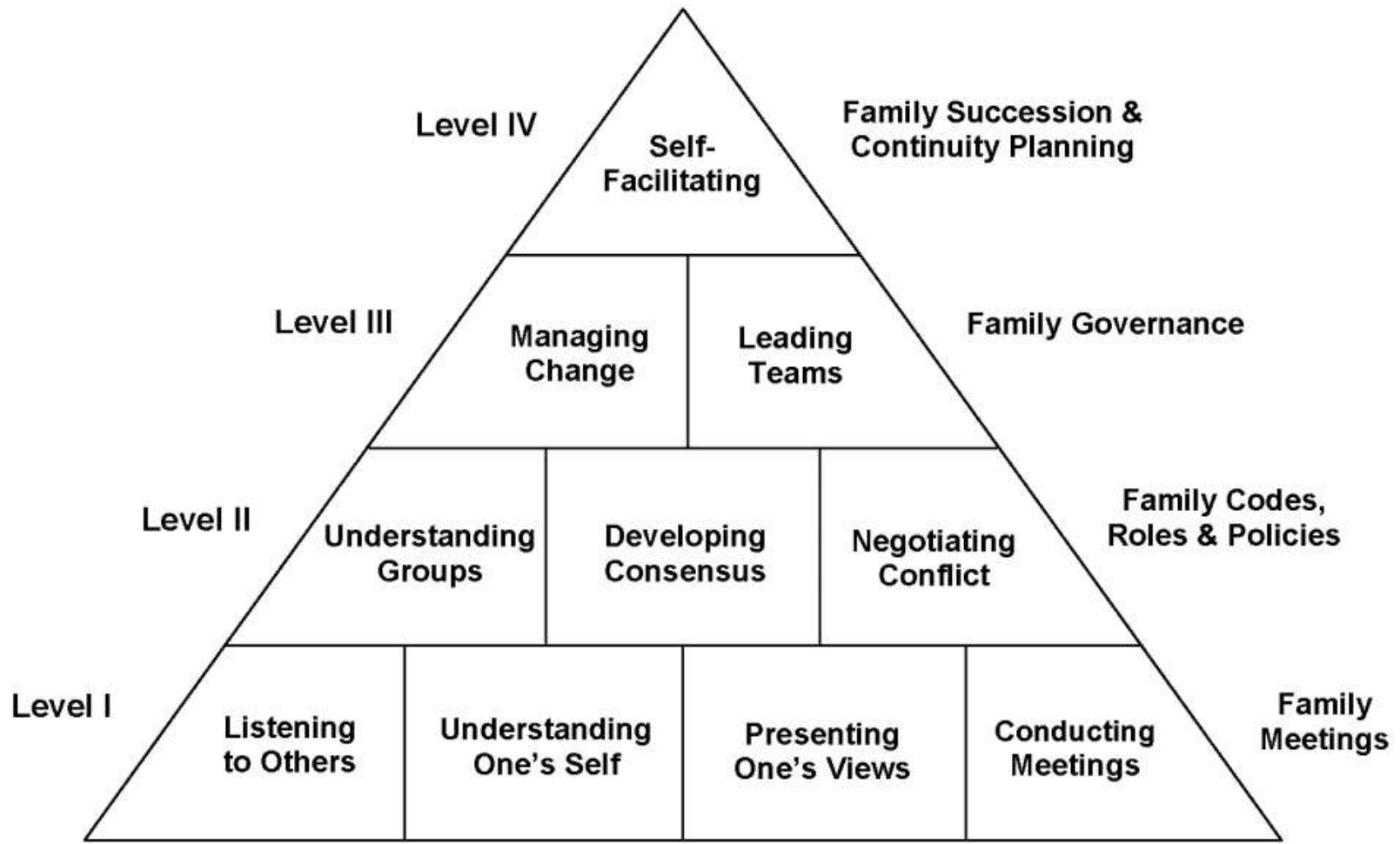
The “Art of Giving”

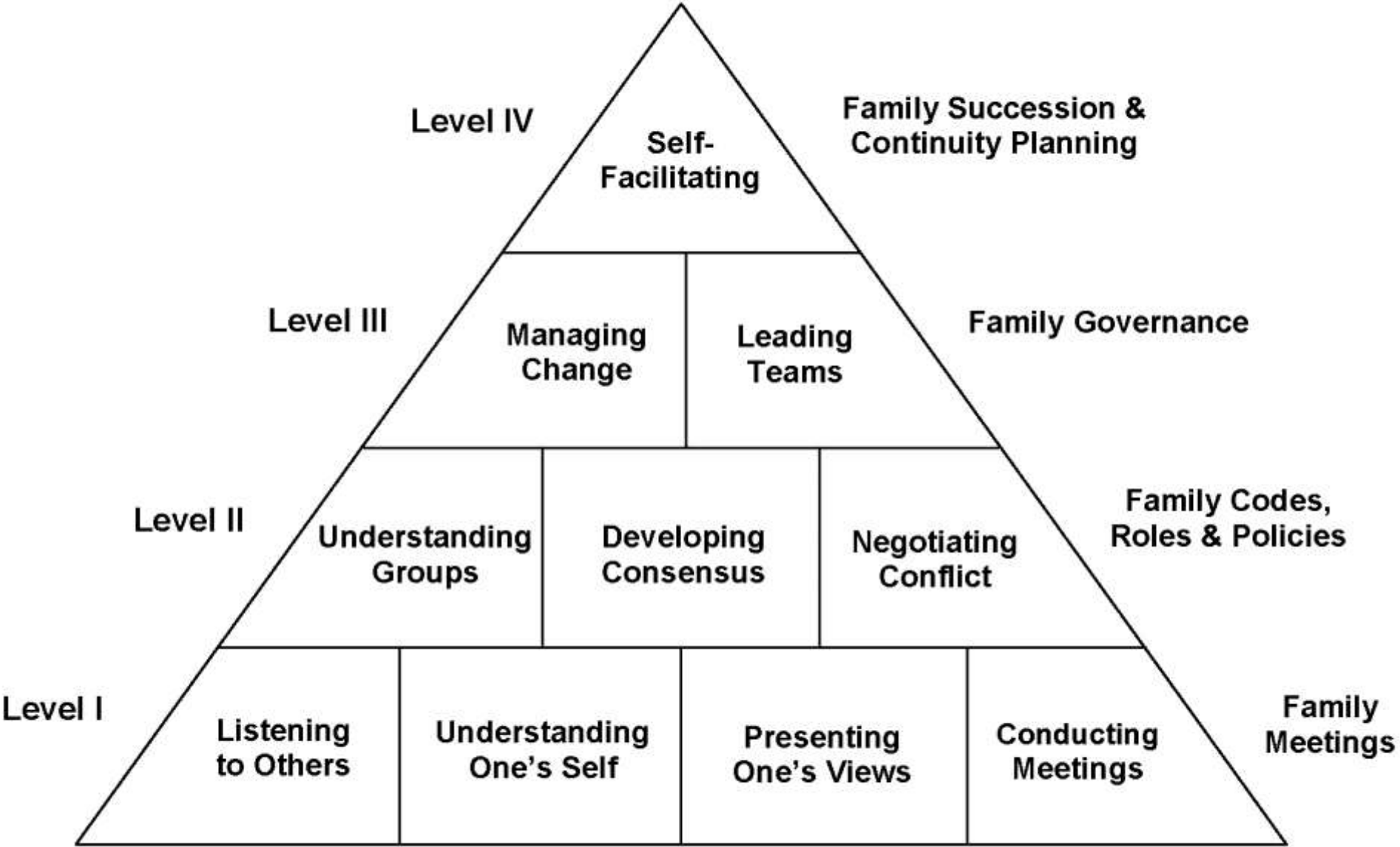
Meaning of Family

Etc.

Etc.

Interpersonal Skills Curriculum





Education as Means...

to Education as an End

- **Family University as “Business Unit”**
- **Learning Culture –**

Sharing with Other Families

Creating Proud, Compelling Sessions

#7 Shareholders' Agreement & Redemption Policy

Policies Before Need

Who?

How Much?

What Terms?

24% have had exit; 45% no policy

KEEP IN – LET OUT

Dilemma

- **Trusts & Politics**
- **Faith**

Freedom and/or Loyalty

Voluntary Commitment

Building the Emotional Asset

#8 Portfolio of Opportunities

To engage individual interests and common good:

- Family Philanthropy**
- New Venture Funding**
- Family Office Employment**
- ...As Well as Family Governance Roles**

BEWARE...

Too much accommodation of individual interests fragments family and compromises meritocracy.

BETTER...

- **Family and Business Philanthropic Synthesis**
i.e., workplace safety and safety products
- **New Ventures Where Markets Aren't Efficient**
i.e., unconventional, unique insight
- **Governed, not Managed Family Office**

#9 Maximize Family Business Competitive Advantage

- Market Perceived Quality
- Long-Term
- Unconventional, Contrarian*
- Fast/Agile

...because of ownership
concentration and commitment

*vertical integration, diversification
per Villalonga & Amit, 2004



We'll pick you up.™

Short-Term-Itis

- **“Only 1% of corporate directors reported that they had never encountered the dilemma between maximizing the stock price and acting in the long-term interest of the firm.”**

Lorsch & MacIver, HBS

- **“Stock market’s attention to quarterly earnings has contributed to a decline in long-term investment... and competitive edge.”**

82% of 100 USA CEOs

- **“78% of CFOs would give up economic value in exchange for smooth earnings.”**
 - 80% would reduce R&D to meet targets
 - 41% would reduce +NPV investments

Short-Term, Near-Term, Present Orientation

- **More Extrapolation**
- **More Conventional Sources of Information**
- **Overconfidence**
- **Over Consensus**
- **Over Simple Implementation**
- **Speculation**
- **Less Personal Responsibility**

Speculation vs. Preservation

“Corporate managements are being pushed into subordinating everything (even... market standing, technology, wealth creating capacity) to immediate earnings and next week’s stock price. A Marxist might well say that corporate capitalism has turned into ‘speculators capitalism’!”

Peter Drucker

Our Survey Results

	<u>NFB</u>	<u>FB</u>
• I believe my company under invests in the future (CEOs)	43%	8%
• Our planning horizons are getting shorter	84%	59%
• There is no doubt in my mind who will control this company in five years	40%	82%
• If I see a near-term problem I shift my focus to it to the detriment of long-term initiatives	74%	47%
• The future will be better than the past	68%	90%
• In our company we actively promote the past	21%	75%

IRR & DCF => Disinvestment

- But, Relative Risk (and discount rate) Declines with Time Horizon

$$\text{Risk} = f (1/\sqrt{t})$$

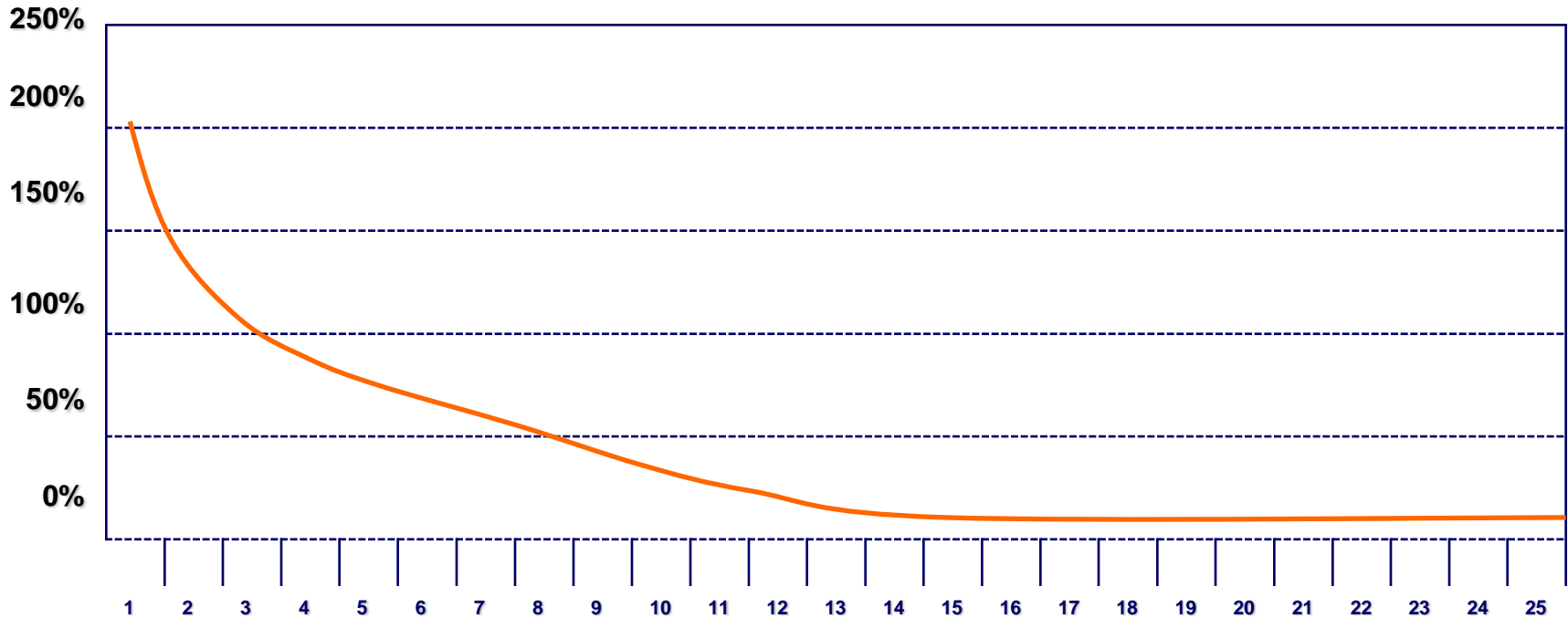
If t = 4 years, Risk = 1/2

If t = 9 years, Risk = 1/3 (16% less)

If t = 25 years, Risk = 1/5 (60% less+)

SOURCE: Tom Zellweger

Risk/Reward Ratio = SD/Return

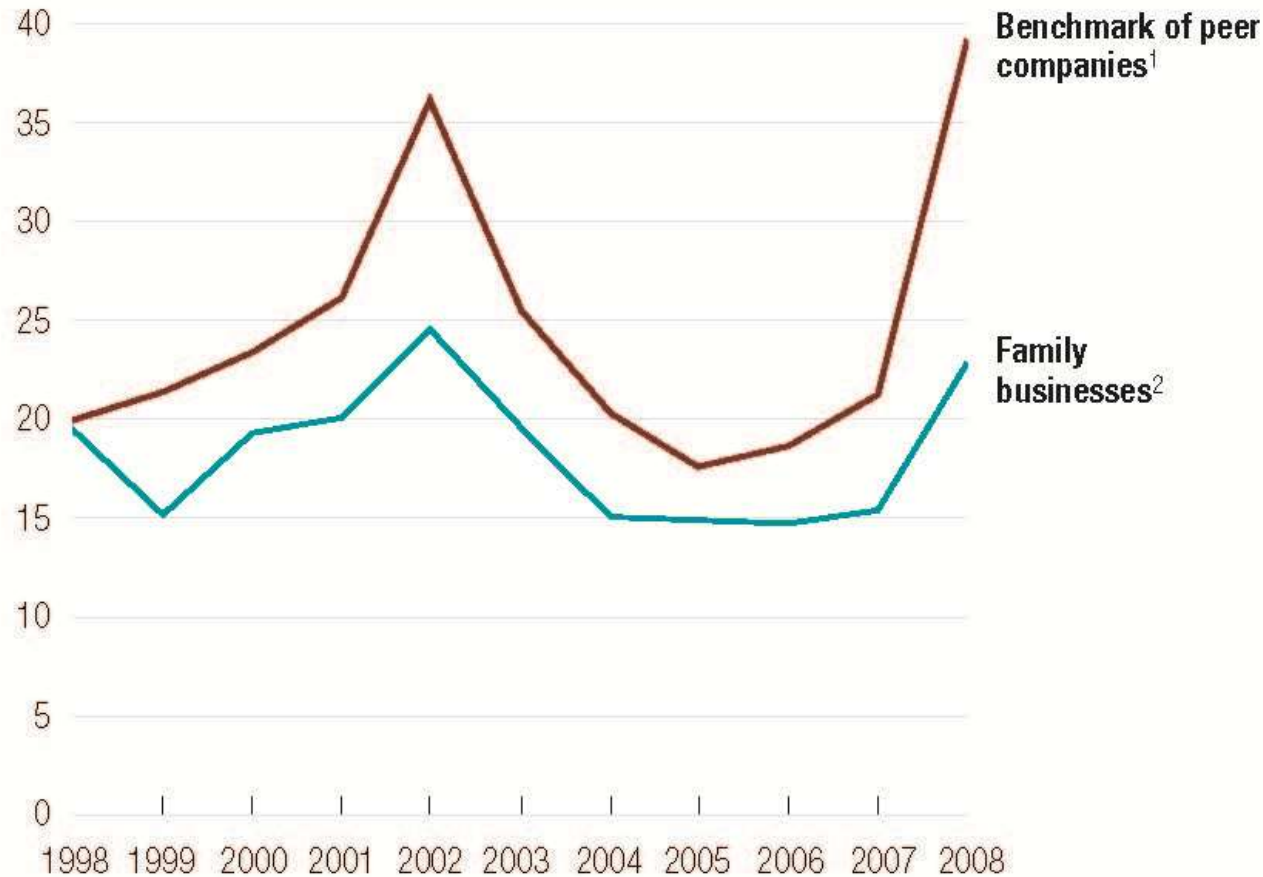


Risk/Reward Ratio With Increasing Holding Period for an Investment with Annualized Return of 10% and a Standard Deviation of 20% SD = Standard Deviation. (Source: Tom Zellweger)

Taking the Long View

Lower levels of financial leverage ...

Median debt-to-equity ratio, %



... and a lower cost of debt

The average yield spread on corporate bonds is 32 basis points lower for family-owned businesses³

Source: "The Five Attributes of Enduring Family Businesses", *McKinsey Quarterly*, January 2010

Managing As If the Future Mattered

- **Paradoxically, Push the Past**
 - Post Audits
 - Performance Management
- **S-T-R-E-T-C-H the Future**
 - Planning Horizons
 - Define Purpose & Principles
- **Think Options & Scenarios**
 - Preserve Balance Sheet
 - Controlled Growth

Managing As If the Future Mattered

(continued)

	Short-Term	Long-Term
Risk (Probabilities)	DCF/NPV IRR EMV	
Uncertainly (Ambiguities)		Scenarios Options Principles & Purpose

Family Businesses

Think Options Naturally

- **Limited Capital**
- **Prudent**
- **Incremental**

10. Managerial Implementation in the Family Business Context

- **Hiring for “Fit”**
- **Orientation and Development**
- **Operationalizing and Measuring Values and Culture**
- **Rewarding the Unmeasurables – Performance Management**
- **Managing Paradoxes**

Hiring for “Fit”

“Slow to Hire; Hasty to Fire”

- **Many Interviews; Many People**
- **What Questions to Ask?**

Managing Paradoxes

**“In this world full of paradoxes,
companies that manage
paradoxes well out-perform
companies that don’t.”**

**Joe Page
CEO, Cargill**

Paradox

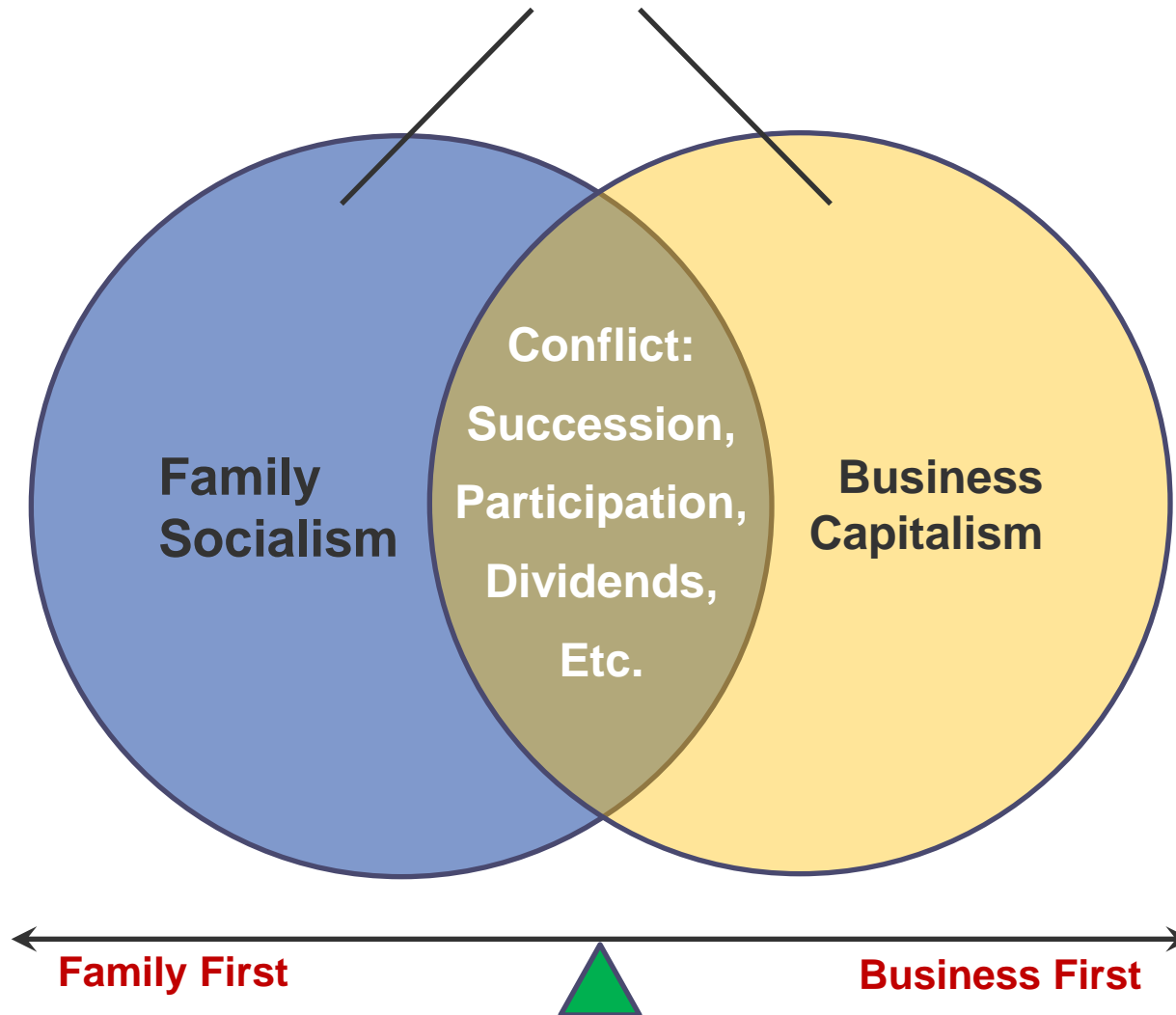
A *paradox* is comprised of two sides that *appear* to be opposing, but, in fact, are mutually supportive.

or

“two perceived contradictory truths”

Fundamental Family Business Dilemma

Is There a Paradoxical Synthesis?



Understanding Paradox Across Generations

	1st Generation	2nd Generation	3rd Generation
Family Priorities	Roots & Wings	Change & Tradition	Loyalty & Freedom
Strategic Choice	Emergent & Plan	Diversify & Focus	Invest & Harvest
Management Philosophy	Expediency & Patience	Heart & Money	Privacy & Transparency
Decision Making	Control & Trust	Process & Task	Democracy & Consensus
Ownership Focus	Selective & Inclusive	Equality & Merit	Branch & One Family

METHODS

- **Choose**
- **Compromise**
- **Balance**
- **Polarity Map**
- **Synthesis**
- **Fusion**

Alexandre Lombard of LODH, mid-1800s

**“Preoccupation with striking the right
balance between passion and reason,
between prudence and audacity,
between innovation and tradition...”**

From Experience to Expertise
Lombard Odier, 2009

An Enduring Phenomenon

Living a spiritual life means we are able to live our life in total polarity. This means we are at ease in the in-between spaces...

- Between tradition and progressive viewpoints
- Between rational and emotional responses
- Between taking action and just being there
- Between solitude and leisure
- Between fasting and feast
- Between discipline and wildness



If we are not growing in our spiritual life then we get stuck on one end of the spectrum or other and we can end up bland, lukewarm, mediocre and isolated. The only way to live a spiritual life is to be able to touch both sides at the same time...

Saint Teresa of Avila

Basic Steps to Managing a Polarity Well Over Time

Action Steps

How will we gain or maintain the positive results from focusing in this left pole?
What? Who? By When? Measures?

Partner with experts in related fields

Write books on applications

Follow up on potential clients who have expressed interest

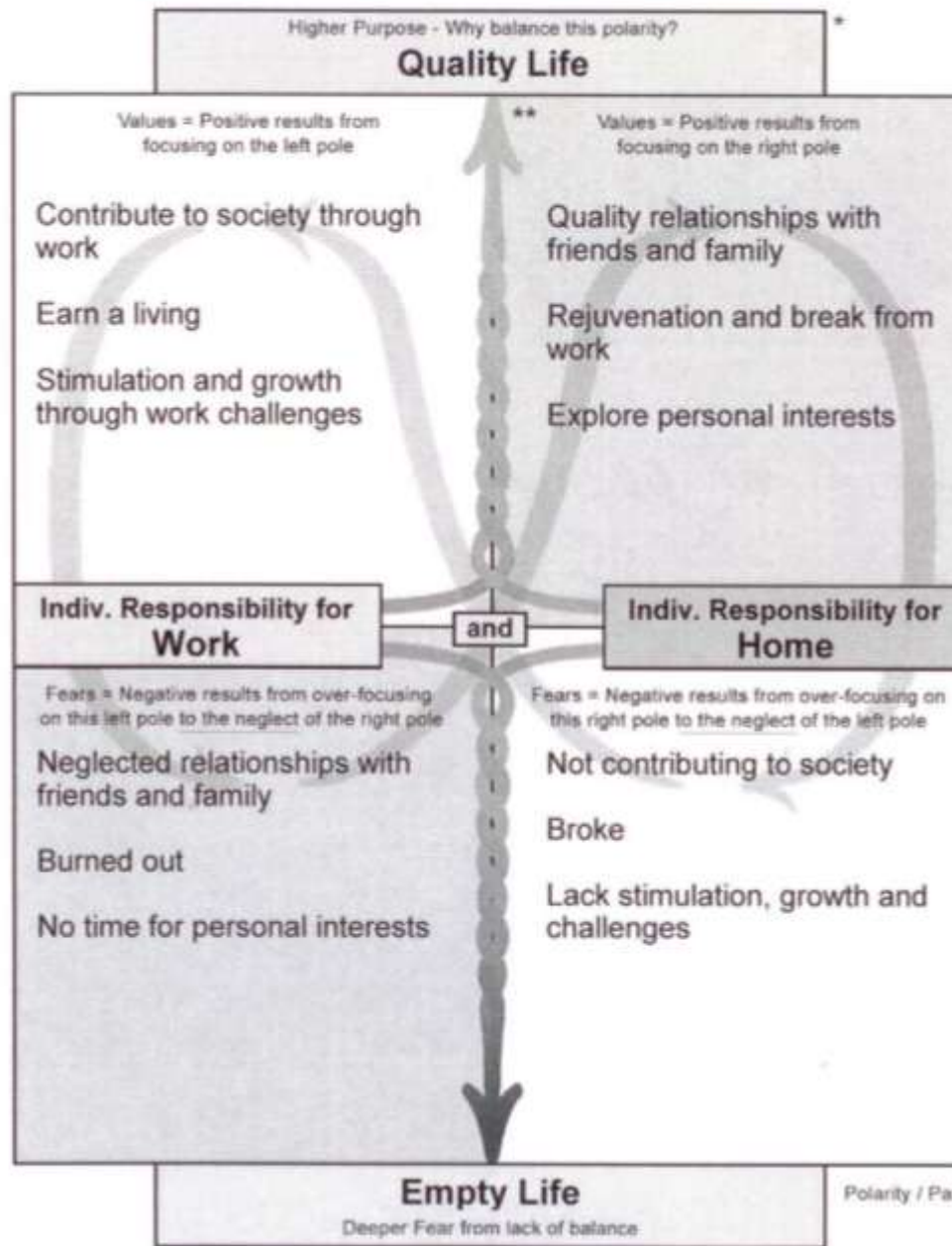
Early Warnings***

Measurable indicators (things you can count) that will let you know that you are getting into the downside of this left pole. Who will know?

Feeling tired and unable to concentrate on work

Dana and friends tell me they are worried about me looking exhausted and having poor contact with them

I forget things both about work and about home commitments



Action Steps

How will we gain or maintain the positive results from focusing in this right pole?
What? Who? By When? Measures?

Schedule 'free time' each quarter for next 15 months

Have a 'date night' each week

Increase skills in white water kayaking

Early Warnings

Measurable indicators (things you can count) that will let you know that you are getting into the downside of this right pole. Who will know?

Feeling guilty for not contributing to society

Money is tight and there is not much work on the calendar

Feeling bored - missing the stimulation and challenge of work

Polarity / Paradox Map®

Synthesis

Liquidity *and* **Growth**

Freedom *and* **Loyalty**

Prudence *and* **Audacity**

Past *and* **Future**

SYNTHESIS

“What is needed is a realization that power without love is reckless and abusive, and love without power is sentimental and anemic. Power at its best is love implementing the demands of justice, and justice at its best is power correcting everything that stands against love.”

The Reverend Dr. Martin Luther King, Jr.

FUSION

- Tradition *is* Change
- Work *is* Fun
- Personal Responsibility
- Stewardship *is* Fulfillment
- Diplomatically Honest

Tradition Is Change

- **“My goal is to build on our tradition of change.”**
- **“I want to remind everyone that innovation is our tradition.”**
- **“Our Legacy of Innovation.”**
- **The Motto: “New Ideas; Old Ideals.”**
- **“Preserve the Best; Reinvent the Rest.”**
- **“Tradition is not history. Tradition is eternity.”**
- **“We embrace both tradition and the modern way of doing things.”**
- **“Always changing to remain the same.”**
- **“Celebrating 100 Years of Innovation.”**

Strauss-Elite Co. Values

Daring

+

Caring

Passion

+

Responsibility

Teamwork

+

Each Person Counts

And So...

For our purposes – paradox is important because it invites us to hear each other, with respect and eagerness, especially when we are representing different perspectives. Wrestling with our differences also makes us stronger!

In Sum,

- 1. See Succession Planning as Continuity Planning**
- 2. Define “Leadership” for Development**
- 3. Make Process More Important Than Constitution**
- 4. Prepare Owners for Board**
- 5. Think One Family (as well as One Business)**

In Sum (continued)

6. **See Family Education as an End, a “Business Unit”**
7. **Build the Emotional Asset**
8. **Focus on Shared Vision More Than Individual Interests**
9. **Manage Thinking About the Future**
10. **Rejoice. “How wonderful that we have met with a paradox. Now we have some hope of making progress.” – Niels Bohr**

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

– F. Scott Fitzgerald

We all like certainty. We enjoy identifying a problem, solving it, and moving on to the next problem. Thankfully, this problem-solving skill is a real strength at Cargill.

The world, however, doesn't always cooperate. More than 2,000 years ago, observers like Plato realized that the world involves paradoxes. Authors like Fitzgerald gave eloquence to the insight, and more recently, business leaders are recognizing paradoxes as a necessary part of our corporate lives.

A paradox involves two interdependent opposites. Both points of view are accurate, but neither is complete. In fact, both points of view are essential for either of them to be successful.

A simple example is cost vs. quality. A single-minded focus on either extreme is going to result in unhappy customers or business ruin. We must both seek the optimum quality and still make our products affordable. This fluid situation changes as circumstances change. There is no one, finally "right" answer.

This is not just philosophic musing; rather this is how companies must operate to be successful.

I started this discussion about paradoxes four years ago at Cargill's global management meeting. I had been getting many pleas for certainty, and I could see the energy people were wasting in a search for finality. It is wasteful, and even wrong, for Cargill to act, as one business unit leader wonderfully expressed it, "with a false sense of concreteness."

In this world full of paradoxes, companies that manage paradoxes well out-perform companies that don't. But, we can't manage paradoxes until we identify the difference between a paradox and a problem. Problems can – and should – be solved.

Paradoxes differ from problems because they do not go away; they must be managed, not solved. Each side of a paradox has both positives and negatives. The aim is to manage paradoxes in Cargill so that we can reap the benefits, and avoid the negatives, of both sides of any paradox. It takes constant communication and collaboration to find the right balance.

Consider what has now become a very familiar paradox: whether our businesses should be centralized or decentralized. When Cargill announced its intent to become a customer solutions company in 1999, we became more decentralized. We needed our businesses to focus on their customers and develop deep insight into what customers needed for success. We have had great successes because we opted for more decentralization. But, we also are seeing some downsides of decentralization: some activity can be annoying to customers, such as getting calls from multiple Cargill salespeople, and we have created inefficient duplication of systems and resources.

Our new "Go-To-Market" initiative is one way we are working to manage this decentralized/centralized paradox. We are learning that we have to be decentralized

and centralized at the same time. We want the accountability, sense of urgency, pride and deep knowledge that goes with being decentralized. We also want to harness the power of one Cargill and bring the breadth of Cargill's expertise to help solve the problems of our customers.

This is not a pendulum where the "right" organizational structure has swung from centralized to decentralized and is coming back again. Rather, we are harvesting the upsides of both sides of the paradox. We are holding these opposing thoughts in our minds at the same time, and we are learning to function at ever higher levels of performance.

Another paradox involves shareholder value vs. business goals. We have said that we want to be a designer of food systems, yet we haven't taken the simple and clear route of just acquiring businesses to reach that goal. This frustrates some people. But, we have to manage both sides of this paradox, and we know we cannot realize this vision without having enough regard for price or value. There are too many examples of companies that have harmed their shareholders by overpaying for acquisitions to hastily meet strategic goals.



Paradoxes can be frustrating – no doubt about it – but we ignore them at our peril. We must face them, aggressively manage them to capture the positives they offer, and learn to perform in the ambiguity they bring.

The way to deal with that ambiguity is not by demanding clarity, but through active communication – trusting each other to speak openly and listen responsibly to determine if an issue is a problem or a paradox. If it's a problem, solve it. Discuss, decide and support the decision and do so promptly. If the issue is a paradox, determine the upsides and downsides of both positions; then focus your energy and the energy of your team in creating a plan to capture the upsides. Do this promptly as well.

Paradoxes are not a cause for delay or postponed action. Managing them requires empathy – so that we can see the "other" side – and action, all the while holding those two opposing ideas in our minds.

Putting our collective energy to work harvesting the upsides of paradoxes, rather than working to find finality, will allow all of us at Cargill to outperform our competitors, win with our customers and build trust with each other. □

***"In this world full of paradoxes,
companies that manage
paradoxes well out-perform
companies that don't."***

Basic Action Steps to Manage a Polarity Well Over Time

Action Steps

Action steps to gain or maintain the positive results from focusing on this left pole.

1. Be more clear about decisions, creating action steps and timelines (and consequences) coming out of discussions/meetings – publish agreements and action items
2. Be clear when we disagree with someone else in a meeting
3. Be clear on what are group issues
4. Be more specific and use examples to clarify the issue
5. Be clear on what was agreed to (publishing agreements)
6. Communicate when circumstances and/or agreements have changed
7. Be candid/challenge the group if a resolved issue comes up again and circumstances have not changed

Early Warnings***

Measurable indicators (things you can count) that will let you know that you are getting into the downside of the left pole.

1. Reduction in meeting participation
2. Engagement survey scores on specific questions (Eve to provide q #s)
3. Less collaboration on projects (see scorecard)
4. Poor meeting report card (specific measures to be defined)

Higher Purpose = Why Balance This Polarity? *

Trust

Positive results from focusing on this left pole:

1. Confront the brutal facts
2. No hidden agendas
3. Efficiency
4. Clarity
5. Transparency
6. Your intent is clear
7. Identify the real issues
8. Gets issues out on the table
9. Sense of urgency
10. Reduced stress from trusting the reliability of what's said

**

Positive results from focusing on this right pole:

1. Prevents hurt feelings
2. Impact on others is seen as important
3. Colleagues interests and intent is respected
4. Others feel heard/listened to
5. Create buy-in by others
6. Engenders a further discussion
7. Opens the door for collaboration/taps collective wisdom

**Candor
(self)**

and

**Diplomacy
(other)**

Negative results of over-focusing on this left pole to the neglect of the right pole:

1. Hurt feelings
2. Undermines collaboration
3. Unilateral hierarchical
4. Others don't feel listened to
5. Low affinity
6. Shuts down discussion
7. Don't get the best data pool
8. Creates avoidance from others who have a diff point of view
9. Low self awareness/out of touch with your impact on others

Negative results of over-focusing on this right pole to the neglect of the left pole:

1. Lost time/inefficient
2. Duplicity/deceit
3. Lack of focus/precision
4. Difficult to get to the real issues
5. Misconceptions/misperceptions
6. Lack of transparency
7. Unclear intent
8. Lack of urgency
9. Greater stress/frustration because less reliability of what's said

Deeper Fear from Lack of Balance?

Mistrust

Action Steps

Action steps to gain or maintain the positive results from focusing on the Right pole.

1. Listen to those who disagree with the intent to understand or as if there is wisdom behind it
2. DISCUSS, decide, support
3. Acknowledge that none of us own the truth (on our own)
4. Inquire what the impact on others would be
5. Seek common understanding of the question/issue
6. Confirm concurrence (silence is not consent)

Early Warnings

Measurable indicators (things you can count) that will let you know that you are getting into the downside of the left pole.

1. Not meeting results or commitments
2. Action items going unfulfilled and unconfrosted
3. Lack of specificity in action items and decisions
4. Disconnect between PMP ratings and business results
5. Issues keep coming up again when circumstances haven't changed, and the resurfacing goes unconfrosted
6. Statements of people being surprised or confused
7. Poor meeting report card (specific measures to be defined)

* Thanks to John Scherer, Center for Work and the Human Spirit

** Thanks to The Strategy Academy, Rotterdam, The Netherlands

*** Thanks to Todd Johnson, Riverdown Consultants

Lessons from Japanese Long-Lasting Companies

There are 5000 companies in the world older than 200 years. More than 3000 are in Japan. Because these companies have provided a long secure base of jobs for the Japanese economy, the Bank of Korea undertook a study of them – to learn what lessons are helpful for Korea with only three firms older than 100 years.

Following are the lessons and facts from this study:

- These companies are devoted to earning the trust of their customers, their employees, their community.
 - They are “anthropocentric” – realizing that talented people are the most resilient force.
 - They also believe that honesty with customers will provide loyal customers, even in a crisis.
- The companies deliberately stay small. Average size is 115 employees. Only 6% are larger than 300 employees.
- They are conservative. They control growth. They are internally financed. They avoid speculation.
- They invest in the skills and loyalty of their people. They believe in craftsmanship.
- They are dominant in small markets. Sixty percent are the leader in market share; 30% are the market share leader in the country; only 13% export.
- The study illustrates the advantages to small, nimble size for survival through a metaphor: There are now only two species of elephants in the world, whereas 75% of all living things are insects.
- These companies have been fortunate to have been in protected environments – including no wars for most of history.
- Interestingly, they have not fully embraced primogeniture. They are very comfortable “adopting a son” to be the better successor.
- In fact, 25% of successions are to non-family, adoptive successors. Only 75% follow family lineage. For the most part, they forbid the employment of in-laws.
- To quote the research paper, “their ultimate purpose of the company is not the profit, but its continuation.”

In our own studies we have found these observations to be true the world over. “Family Capitalism” is a very different species.

Schumpeter | Mittel-management

Germany's midsized companies have a lot to teach the world

The Economist



MANAGEMENT gurus are constantly scouring the world for the next big idea. Thirty years ago they fixated on Japan. Today it is India. The more restless are already moving on to Peruvian or Zulu management. Yet in all this intellectual globe-trotting the gurus have sorely neglected the secrets of one of the world's great economies. Germany is the world's largest goods exporter after China despite high labour costs and a strongish euro. It is also stuffed full of durable companies that have survived hyperinflation and two world wars. Faber-Castell, a giant among pencilmakers, boasts that Bismarek was a customer.

Thankfully, a couple of management thinkers have defied the boycott on Germany. On November 18th Bernd Venohr, of the Berlin School of Economics and Law, gave a fascinating talk on the "secret recipe" of the country's *Mittelstand* at the second annual Peter Drucker Forum in Vienna. Last year Hermann Simon, of Simon-Kueher & Partners, a consultancy, published an even more gripping sequel to his 1996 book on "Hidden Champions". Put the two together and you get a good idea of the management theory at the heart of Germany's success.

Although the term *Mittelstand* is sometimes applied to quite small, parochial firms, the most interesting ones are rather bigger and more outward-looking. Most shun the limelight: 90% of them operate in the business-to-business market and 70% are based in the countryside. They are run by anonymous company men, not hip youngsters in T-shirts and flip-flops.

They focus on market niches, typically in staid-sounding areas such as mechanical engineering rather than sexy ones like software. Dorma makes doors and all things door-related. Tente specialises in castors for hospital beds. Rational makes ovens for professional kitchens. This strategy helps them avoid head-to-head competition with global giants ("Don't dance where the elephants play" is a favourite *Mittelstand* slogan). It has also helped them excel at what they do.

Globalisation has been a godsend to these companies: they have spent the past 30 years of liberalisation working quietly but relentlessly to turn their domination of German market niches into domination of global ones. They have gobbled up opportunities in eastern Europe and Russia. They have provided China's "factory to the world" with its machine-tools.

The *Mittelstand* dominates the global market in an astonishing range of areas: printing presses (Koenig & Bauer), licence plates (Utsch), snuff (Pöschl), shaving brushes (Mühle), flycatchers (Aeraxon), industrial chains (RUD) and high-pressure cleaners (Kärcher). Kärcher's dominance of the high-pressure market is so complete that in 2005 Nicolas Sarkozy caused a scandal, after a spate of riots, by calling for a crime-ridden *banlieue* to be cleaned out "au Kärcher".

How durable is the *Mittelstand* model? Sceptics worry that it will eventually become the victim of globalisation: emerging-world companies will learn to produce their own clever machines at a fraction of the cost. They also worry that *Mittelstand* companies are too conservative. American start-ups can become global giants in a generation (Wal-Mart, now the world's biggest retailer, was not even listed on the stock exchange until 1972). German companies are content to remain relatively small.

The first criticism is overstated. *Mittelständler* have not only focused on sophisticated niches that are hard to enter. They have thrown their energies into building up ever more powerful defences. They constantly innovate to stay ahead of potential rivals. They are relentless about customer service. Their salespeople are passionate about their products, however prosaic, and dogged in their determination to open up new markets. Mr Simon's "hidden champions", mostly German *Mittelstand* firms, typically have subsidiaries in 24 foreign countries, offering service and advice. Many get the bulk of their revenues from service rather than products. Hako, which makes cleaning equipment, generates only 20% of its revenue from sales of its machines.

The second criticism has more substance. Germany has a poor record at generating start-ups or at quickly turning smallish firms into giants. *Mittelstand* firms are finding it increasingly difficult to persuade the world's best and brightest to make their careers in rural backwaters. But for all that, the record of the *Mittelstand* over the past three decades has been a history of global conquest rather than missed opportunities. Koenig & Bauer, for example, gets 95% of its revenue from outside Germany.

German lessons

So the *Mittelstand* is likely to keep powering Germany's export machine for years to come. But does it have any lessons for the rest of the world? Mr Simon says that although 80% of the world's medium-sized market leaders are based in Germany and Scandinavia, successful *Mittelstand*-style companies can be found everywhere from the United States (particularly the Midwest) to northern Italy, so the model does seem to be transferable.

Three general lessons—for politicians as well as corporate strategists—follow from this. First, you do not need to try to build your own version of Silicon Valley to prosper; it is often better to focus on your traditional strengths in "old-fashioned" industries. Second, niches that appear tiny can produce huge global markets.

The third lesson is that Western companies can preserve high-quality jobs in a vast array of industries so long as they are willing to focus and innovate. Theodore Levitt, one of the doyens of Harvard Business School, once observed that "sustained success is largely a matter of focusing regularly on the right things and making a lot of uncelebrated little improvements every day." That is a lesson that the Germans learned a long time ago—and that the rest of the rich world should take to heart.

The Economist, November 25, 2010

Perpetuating the Family Business Checklist: 50 Lessons

- | | <u>Yes</u> | <u>No</u> |
|--|------------|-----------|
| 1. | _____ | _____ |
| Are the business's leaders committed to long-term continuity for societal and philosophic reasons? | | |
| 2. | _____ | _____ |
| Does the business have an independent, outside board of directors? | | |
| 3. | _____ | _____ |
| Is there a mandatory retirement age for all executives, directors and especially owners? | | |
| 4. | _____ | _____ |
| Does the family get together regularly for fun, not just for business reasons? | | |
| 5. | _____ | _____ |
| Are family owners actively learning about the field of family business? | | |
| 6. | _____ | _____ |
| Do family members live modestly, beneath their financial means? | | |
| 7. | _____ | _____ |
| Is the owning family comfortable with its position of wealth – neither letting wealth define the family nor fearing the consequences of wealth on the family? | | |
| 8. | _____ | _____ |
| Are promotions and compensation of family members clearly based on merit? | | |
| 9. | _____ | _____ |
| Is the business attracting the most business-competent children in the next generation? | | |
| 10. | _____ | _____ |
| Does the business rely upon an important cadre of non-family executives? | | |
| 11. | _____ | _____ |
| Are the non-family executives provided with opportunities to gain personal wealth – beyond compensation? | | |
| 12. | _____ | _____ |
| Does the family openly share information about family member compensation and benefits? Do family members share information with one another about estate plans and gifts? | | |
| 13. | _____ | _____ |
| Are owners aggressively gifting or distributing shares to the youngest generations? | | |

Perpetuating the Family Business Checklist: 50 Lessons

- | | <u>Yes</u> | <u>No</u> |
|--|------------|-----------|
| 14. | _____ | _____ |
| Are there easy, graceful ways for family members to redeem their ownership if they wish to do so, thereby facilitating pruning of the ownership tree? | | |
| 15. | _____ | _____ |
| Is the business strategy enhanced with special competitive advantages from being a private, family-owned company – such as long-term orientation, trusted relationships, etc.? | | |
| 16. | _____ | _____ |
| Does the family generously “give back” the community to build social goodwill? | | |
| 17. | _____ | _____ |
| Does the family accept that the business must be run as an excellent business? | | |
| 18. | _____ | _____ |
| Is the family selective about which family members are qualified to work in the business? | | |
| 19. | _____ | _____ |
| Is the family providing business education and exposure to the youngest members of the family? | | |
| 20. | _____ | _____ |
| Does the family have a “Code of Conduct” to strengthen inter-personal relations and expectations? | | |
| 21. | _____ | _____ |
| Does the family study and practice communication skills? | | |
| 22. | _____ | _____ |
| Do family members have independent security beyond their ownership shares in the family business? | | |
| 23. | _____ | _____ |
| Do family members share information about investment opportunities outside the business? | | |
| 24. | _____ | _____ |
| Does the family have a process to welcome and acculturate new in-laws to the family? | | |
| 25. | _____ | _____ |
| Does the family have a statement of family values that it hopes to perpetuate? | | |

Perpetuating the Family Business Checklist: 50 Lessons

- | | <u>Yes</u> | <u>No</u> |
|--|------------|-----------|
| 26. | _____ | _____ |
| Does the family have identified family leadership? | | |
| 27. | _____ | _____ |
| Are succession plans in place for executive, governance and family leadership continuity? | | |
| 28. | _____ | _____ |
| Does the business's culture encourage quick responsiveness and change? | | |
| 29. | _____ | _____ |
| Is the family committed to being in the best businesses for the future -- even if that means leaving its business of origin? | | |
| 30. | _____ | _____ |
| Do family members feel heard, respected, and that decision-making processes are fair? | | |
| 31. | _____ | _____ |
| Does the company have a formal dividend policy that pays out according to profitability? | | |
| 32. | _____ | _____ |
| Do the family owners have a commitment to each other for the long, long term? | | |
| 33. | _____ | _____ |
| Do family members have opportunities to serve as cultural ambassadors on behalf of the business? | | |
| 34. | _____ | _____ |
| Do the family owners feel they hold their stock for the purpose of passing it on to future generations? | | |
| 35. | _____ | _____ |
| Does the owning family have regular family meetings? | | |
| 36. | _____ | _____ |
| Does the owning family provide education to the next generation on the privileges and responsibilities of ownership? | | |
| 37. | _____ | _____ |
| Are the family owners closely monitoring the business's strategy, culture, and board of directors? | | |
| 38. | _____ | _____ |
| Do non-employed family owners avoid meddling in management's operating responsibilities? | | |

Perpetuating the Family Business Checklist: 50 Lessons

Yes No

39. _____ Does the owning family have respect for managers and the challenges of managing? _____
40. _____ Is the owning family active in educational programs on such topics as interpersonal relations and understanding business? _____
41. _____ Is the owning family committed to helping all family members in their professional development, regardless of their interests? _____
42. _____ Does the family have a policy on how best to address family members who may be in financial need? _____
43. _____ Are there many different roles family owners can play in the family council or other family interests? _____
44. _____ Does the family have a Family Constitution? _____
45. _____ Are family branch politics and representation avoided in favor of everyone seeing themselves as members of one extended family? _____
46. _____ Has the owning family articulated a mission and purpose for the family? _____
47. _____ Has the family articulated how its values are important to the family's business? _____
48. _____ Does the owning family feel that the family business has a social purpose? _____
49. _____ Does the owning family feel enthused and motivated by the family continuity planning process? _____
50. _____ Is the family active in promoting and supporting the concept of family business in its community? _____