[Academic Script]

Management of Family Business - 1

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1. Introduction

An important and major element of Entrepreneurship is the institution of family business. It is an inevitable part of the concept of Entrepreneurship, missing it will result in a void. This unit is dedicated to the core concept of family business and is intended to orient you to the important dimensions of the concept. The examples and elaboration will communicate to you about its wide spread existence and their contribution to the economic state of any country.

Objectives of the Lecture

- To give you an overview of the emergence of the concept
- To acquaint you with the dimension of family capital
- To acquaint you with the kinds of capital relevant in the context
- To orient you to the existence of conflicts in family business
- To identify the causes of it and the challenges faced in managing them.

[A]Overview of Family Business Domain

The domain of family business has attracted a lot of academic attention because of the growing dominance of the family run enterprises on the economic frontier, which has also led to the rise in management courses dealing exclusively in the area. It is the oldest and the most common form of an economic entity. It would not be an exaggeration, claiming family business to be as old as humanity. Historically speaking, members of the family have always come together to work and earn and they have faced situations of conflict time and again. Still, family businesses are a major contributor to the world economic wellbeing and prosperity by way of innovation, employment and productivity.

There has always been an array of perspectives in defining a Family business. Many researchers have come up with various definitions, though largely there is a lack of consensus is arriving at one single way of defining the concept. Astrachan and Shanker (2003) have used three modes of family involvement to arrive at three definitions of family firms: One is based on the family's retention of voting control over the firm's strategic matters, the second is based on the involvement of the family in the day to day operations of the firm and the third which is a stringent form, looks at family firms as one only if they retain voting controls and the involvement of multiple generations of the family in the day to day operations of the firm. Thereby, a family business is a commercial organization wherein multiple generations influence decision making. The affect may be through leadership or ownership.

Some of the most noted family businesses include some of the biggest brands like Walmart, Samsung, Tata and Foxconn. According to the Global Family Business Index, a privately held firm can be termed as a Family firm when the family controls more than 50%of the voting rights, and a publicly listed firm can be termed as a Family firm if the family holds at least 32%of the voting rights. In family businesses, two or more members in the managing team are selected from the family that owns the business. Usually the family members are involved in the day to day operations in some or the other way. A frequently witnessed move is to hire a "non-family CEO or CFO" in such family firms.

In India, family businesses have always been prevalent, both in organized as well as unorganized sector. Family is the oldest running social unit in the world, thereby making the concept of family business nothing, but natural. As opposed to the West, the scenario of family business concept is different in India owing to the existence of large families, caste concerns making even the extended family as family, thereby multiplying the family interactions. However, with times the family structure are undergoing many changes like there is notable rise in the number of nuclear families owing to globalization, education opportunities, job based movements, urban living and a plethora of other social and cultural transformations.

2. Family Capital

It refers to the resources held within the family that can be accessed by the business. Whenever these resources or assets outweigh the liabilities of the firm, then it can be said that the firm has family capital. However in a broader perspective to the term, family capital refers to the summation of social, human and financial resources at a firm's disposal.

(I) Social Capital

It is the social capital parameter that distinguishes a family firm from the non-family firms. A family firm cannot hire social capital. It comes from the relationship fabric in the family, where more the trust, more it fosters cooperation. Such firms tend to attract high financial and human capital from the outside. Moral infrastructure is the key, providing the basis for family values, beliefs, norms and expectations. Many families take the route of meetings and councils to maintain social capital. Some firms resort to designing collaborative arrangements like a charter or a constitution which is based on the shared values, beliefs and norms.

(II) Human Capital

It refers to the knowledge, experience, ability, dynamism and energy roped by each of the individual family members. A strong human capital can be treated as a potential resource advantage. Even the family members who are not directly serving as an employee in the firm can be still treated as a human capital when they have positive social relationship with the employed family members. In family business, this stock of human capital can be allotted to business, governance system or family, making the resources mobile to the relevant areas. Thus a strong human capital extends advantage of extreme resource mobility to a firm.

(III) Financial Capital

A healthy family business usually witnesses sharing of financial resources among the members, directed at sustaining and developing the business. Family businesses that share a good reputation at the market place end up attracting financial investments from external agencies too.

Understanding Family Business Profitability

In a family business, profit is much more important in sustenance since it necessarily fuels survival and cushions liquidity concerns. Access to profits can be a very touchy area in family businesses, where the senior family members may question writing off too much stocks to the young adult stockholders, and family members may feel powered or threatened on the basis of this distribution.

Here are some points to consider to foster open discussions around profitability in a family enterprise.

- Designing exercises which revolve around comforting each family member in disclosing their expectations around money and profitability without the fear of judgments.
- Designing the family's vision and value statements clearly, so that the management can strategize goals that are directed at achieving this vision.
- Create clear key polices related to project compensation, employee compensation, non-family employee compensation, charities and so on.

3. Recognizing Conflict

Family enterprises tend to receive many advantages like being extremely vigilant about funds, heightened commitment, flexibility in roles, and being competitive. However, family business can be a very complex structure, which includes being exposed to challenges related to conflicts goals, conflicting roles and even boundary management issues. Keeping matters of family in family and not mixing it with business takes a great deal of understanding and work, which can be a real task at hand. A non-family business is free from such challenges. The pattern of the family is also bound to grow and evolve with time, making the family pattern dynamic far more complex to decode.

Some challenges can be as follows:

- On account of founder members, who are skeptical and in denial for chalking an effective succession plan.
- On account of the informal influence of the family members who are not owners nor are they part of the management team.

- On account of the disagreements related to “passing of the ownership” based decisions; often seen between parent and child relations, the passing of the beneficial treatment to the eldest son, can lead to concerns based on non-equality of rights.

A majority of the businesses are family owned. A McKinsey report claimed that 35% of billion dollar plus businesses in emerging markets will be family owned by 2025. The old adage of "blood is thicker than water" is losing its credibility and many family business conflicts are testimony to that. Sons separating or siblings creating uneconomical assets split to suit their greedy requirements to amass additional wealth and independence is widely prevalent. Another rising issue is the splitting of the spouses, leading to settlement based conflicts which can put to risk the company’s ownership structures and also at times, stake detrimental effects on share prices of the firm.

Most of India’s biggest companies, which apparently are global brands are Reliance, Dabur, Bajaj and Tata. Reliance was in the spotlight for a considerable time period over the unpopular family feud leading to the split of the business empire between the two brothers, Anil Ambani and Mukesh Ambani. Usually conflicts are based on power and ownership based issues. Such conflicts can bear adverse effects on the business in more than one way, like negative publicity, tarnishing of company’s reputation, splits, and disturbances in routine operations, external mediation and even closure of the firm.

Many a times, families witness conflicts owing to differences in the interests of the family members with regard to the future directions and decision making styles. For instance, a firm co-owned by two brothers A and B, are facing troubled times owing to disagreements on investment of the surplus funds. The conservative brother may be interested in deploying funds into expansion of the existing product line. The venturesome and adventurous brother may find a new business a more lucrative idea. If the two brothers are not able to align their interest with the other, than the situation can work up its way into a big conflict. Sometimes the conflict between family members who are not a part of the business can also lead to a conflicting situation. Especially in Indian context, where there are brothers owning the firm, and any tensions between their spouses can have some effect and tension in the boardroom too. There is also an unspoken obligation in family businesses and that is to employ the relatives. This can lead to hiring incompetent people to avoid any negative feelings in family relationships. An another problem in such cases is the awkwardness and complexities associated with reprimanding such non-performing family members. This makes it really difficult for the family members to maintain a balance between what is good for the business and relationship based considerations.

4. Decision Making and Conflict Management

Conflict is an inevitable element in family businesses and also a prominent characteristic. Such conflicts also attract lot of attention of the spectators. Although business finds its own ways of handling these conflicts, not much of it is made known to the outsiders. Conflict management primarily requires understanding the unique nature of the conflict in the family business.

There are some reasons that make family business conflicts, unique. They are:

- Family complexes the conflict by making it inevitable to accommodate the varying interest of the immediate as well as extended family members.
- It is the family norms that dictate the tone of the negotiations in wake of a conflict. When there are multiple family members working for the business, the role and influence of these family norms intensifies.
- The power dynamics in a family business is indeed very unique to family business. Unlike a non-family business, where the ultimate power to make decisions would rest with a CEO; in case of family business, this power can be far more scattered since most of the family members would have access to important information and decisions. Thereby even a non-owner family member may end up influencing important decisions.

5. Summary

The domain of family business is an age old institution marked with growth and dynamism. It is a commercial organization where family generations are involved in decision making. A striking point with family business is the family capital involved which can take forms of; social capital, human capital and financial capital. An inevitable element in family businesses is the existence of conflicts. There can be many causes to these conflicts, though largely they are owing to the issues related to ownership or power. However, the inevitability of conflicts do not connote their irreparability. There can be conflict management strategies that can suggest measures for conflicts based on the parties involved, the challenges underlying them and the

intensity and gravity of the matter and their foreseeable repercussions.