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Private

Global perspectives for family businesses

Plans, priorities, and expectations

Family Business Centre, March 2018


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Introduction

Plans, priorities, and expectations

In January 2018 we launched *Global perspectives for private companies*, our first global survey of some 1,900 private company leaders to understand the plans, priorities and expectations of their companies. In this report we focus on the 400 or so family businesses that participated in the survey.

We found that executives in family businesses around the globe share the same optimism as their counterparts in non-family private companies:

- Two-thirds of family businesses expect increased revenues and profit over the next 12 months. 42 per cent even predict an increase in revenues of 26 per cent or more
- 42 per cent of family businesses expect to acquire another company over the coming 12 months
- 48 per cent expect to hire more full-time employees.

Family businesses need to maintain a balance between their business goals (such as growth, innovation and recruiting talented staff) and their family goals, such as maintaining family values and protecting the family wealth. We might expect this to result in different views and approaches, compared to non-family private businesses. Our study found differences in their perceptions of risk, financing growth and workforce:

- Family businesses rely on internal sources for funding growth. They are not keen on engaging with private equity or selling equity to the stock market
- Unlike non-family private companies, they do not perceive economic uncertainty or geopolitical factors as the major risks to growth, given the resilience of their business in turbulent times
- Family businesses will invest slightly less in leadership development than the other private companies in our survey.

The difference we found regarding the workforce is remarkable. Family businesses are proud to say that their workforce is very loyal to the company and the family. This is a huge advantage, although maintaining strong positive attitudes will probably call for more investment in future than ever before.

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Business outlook

Two-thirds of family businesses expect increased revenues and profit over the next 12 months

Family businesses make up by far the largest part of the worldwide economy, and their leaders share the current general optimism about the economic outlook.

The majority of our respondents expect revenue, profits, productivity and capital investment to increase in the year ahead. 48 per cent expect to hire more full-time employees.

Two out of three family businesses in the survey expect their revenues to increase. The same proportion of companies thinks their profits will rise. 42 per cent predict an increase in revenues of 26 per cent or more.

The main growth strategies for family businesses over the coming 12 months are:

- Growth in existing markets (37 per cent)
- Development of new products and services (35 per cent)
- Increasing productivity (34 per cent).

Only a fifth of respondents are considering entry into new markets abroad.

Figure 1. Do you expect the following key metrics to go up, stay the same or go down in the next 12 months?

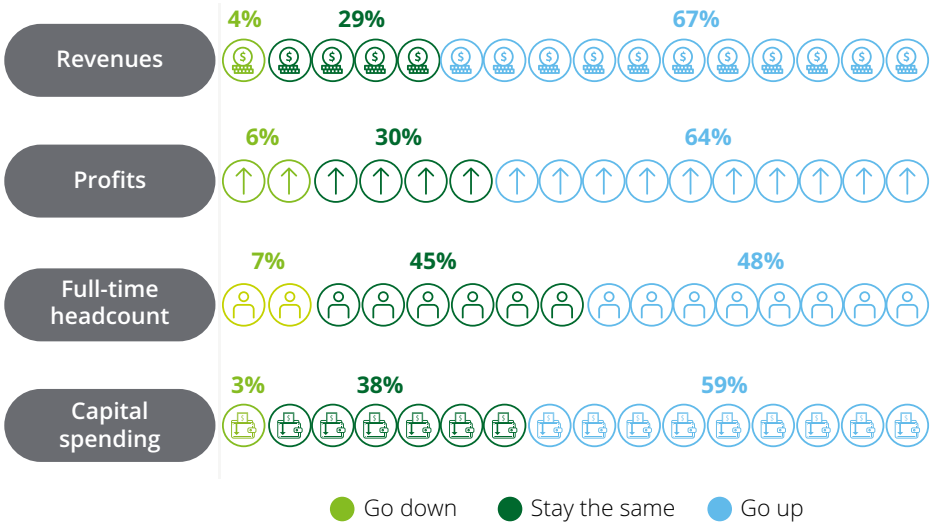
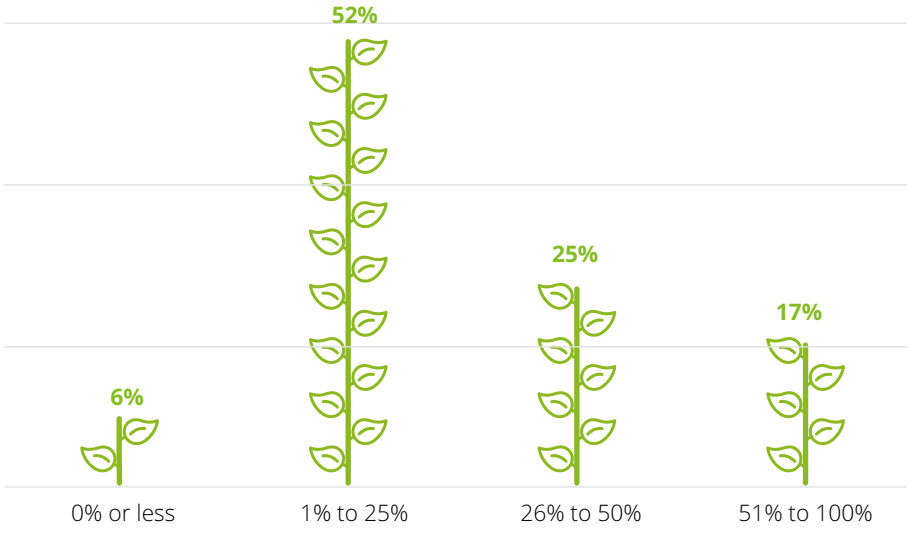


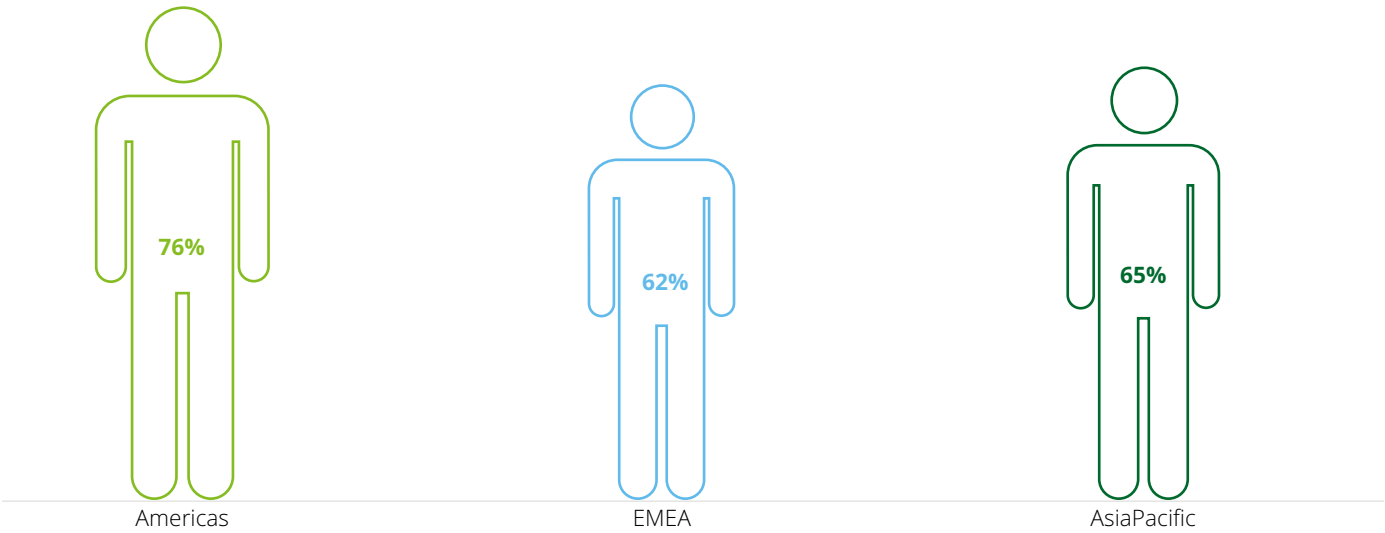
Figure 2. What would you estimate your family business revenue growth to be over the next 12 months?



Business outlook – international comparison

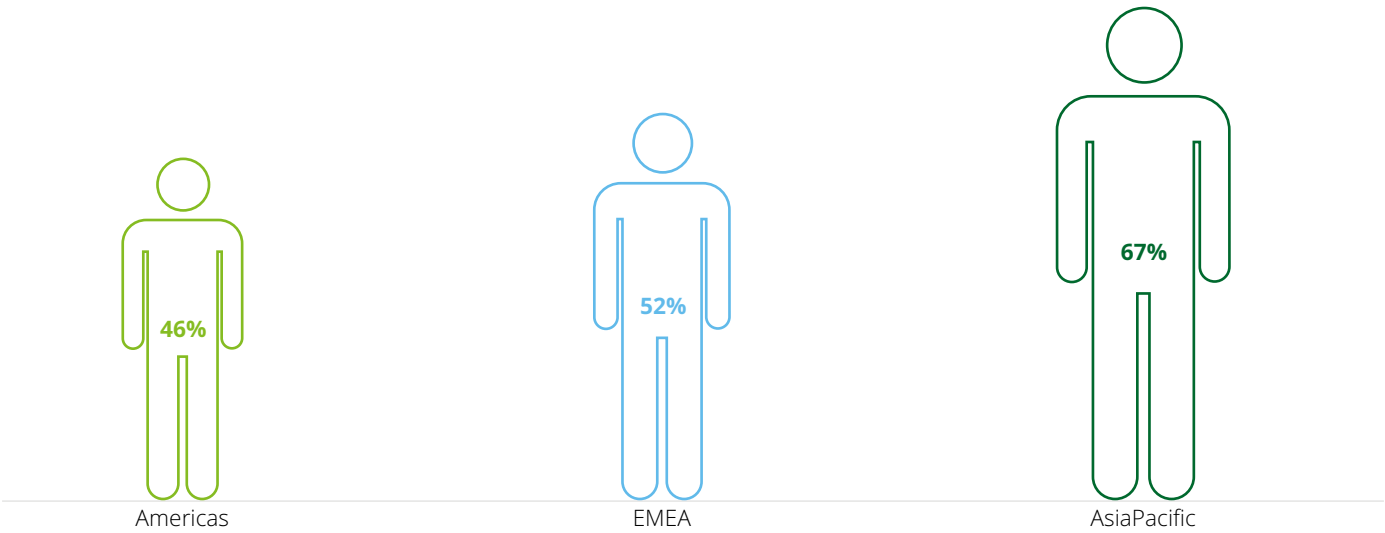
Family business executives in the Americas have more confidence in the success of their companies than those in EMEA and AsiaPacific. The uncertainty is greatest in AsiaPacific.

Figure 3. Percentage of respondents who are 'extremely confident' or 'very confident' in the success of their company over the next 24 months (based on revenue, profitability and growth).



Survey question: what is your level of confidence in the success of your company over the next 24 months (based on revenue, profitability and growth)?

Figure 4. Percentage of respondents who believe that the current level of uncertainty in their home country, based on factors that drive business prospects is 'much higher' or 'higher' than one year ago.



Survey question: What is the current level of uncertainty in your home country, based on factors that drive business prospects (for example, taxes, regulations, credit availability and the economic outlook)?

Financing growth

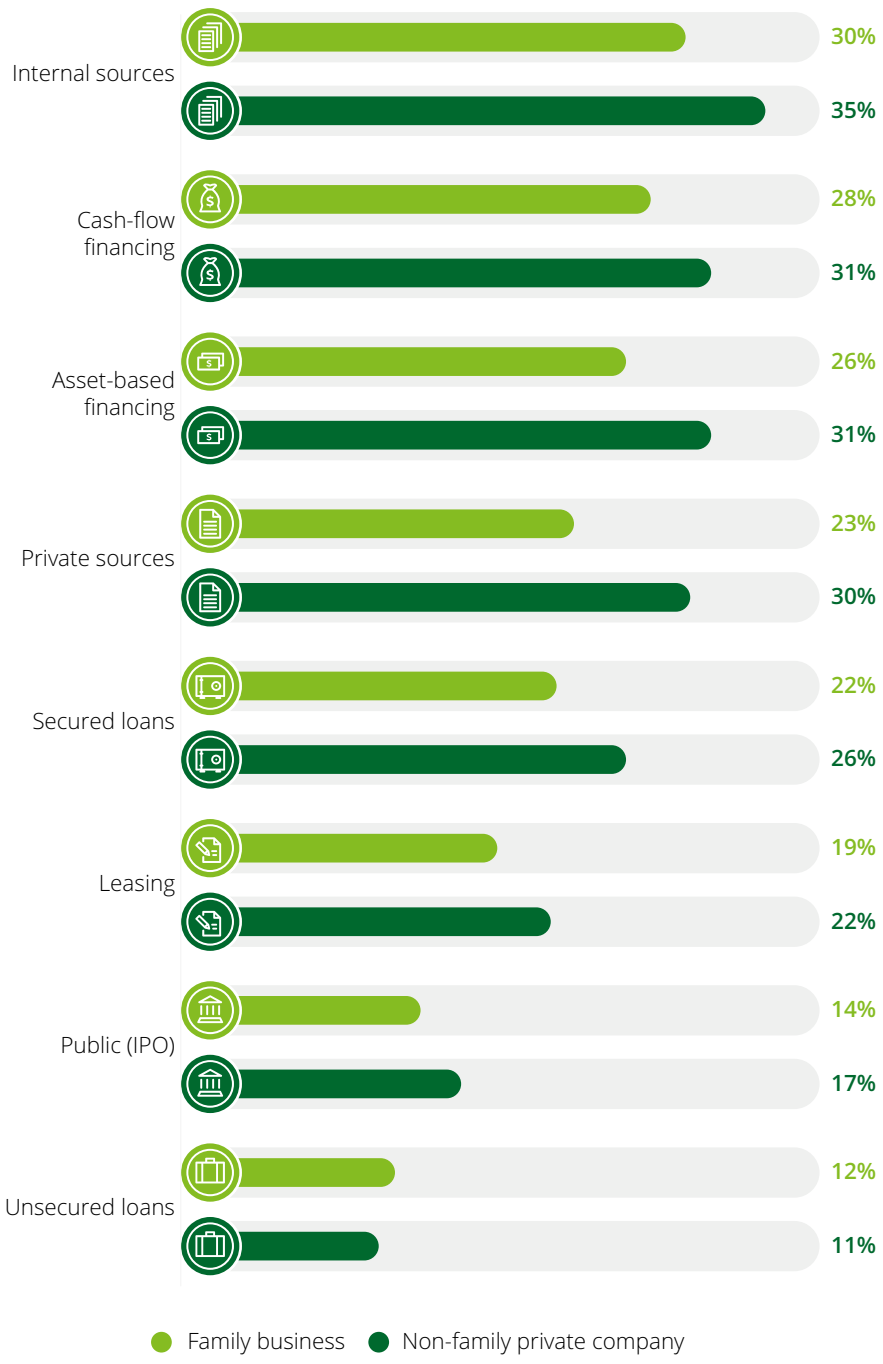
Family businesses use internal sources primarily to fund growth

There is a commonly-held view that family-owned businesses are totally self-financing, but this is not entirely true. Family companies do make use of external financing for growth and expansion. Our survey found that family businesses intend to fund their growth over the next 12 months primarily using internal sources such as retained earnings (30 per cent of businesses), cash flow financing (28 per cent) and asset-based financing such as working capital lines (26 per cent). Non-family private companies will use these methods of financing slightly more than family businesses.

Only 14 per cent of family businesses say that they would consider an initial public offering (IPO) to finance growth. Selling equity - either to a private investor or on the stock market - is not popular because families are usually keen to retain ownership of their business, and even see it as a key success factor. An IPO results in the dilution of control. Family businesses tend to have a long-term view, and do not think in terms of publishing quarterly financial statements. IPOs are more popular with executives of non-family private companies (17 per cent), but only slightly.

The biggest difference in preferred methods of financing is in the use of private sources (private equity or private investors). Only 23 per cent of family businesses expect to use private sources, compared to 30 per cent of non-family private companies. In general, family businesses are not keen on engaging with private equity firms for the same reasons that they would not consider an IPO.

Figure 5. What types of financing do you expect your company to pursue in the next 12 months?



Risks to growth

43 per cent of family businesses perceive the level of economic and financial uncertainty impacting their business to be higher than one year ago

A range of different issues may present a risk to growth in the coming 12 months. Both family businesses and non-family private companies see the cost of raw materials and other input costs (such as energy prices) as their main risk.

The ability to hire and retain employees is seen as the second-biggest risk by family business executives. A family business faces specific challenges compared to other companies, especially during times of leadership transition when the next generation takes over from the previous one but leadership remains within the family. There is also a challenge to family businesses when it comes to appointing non-family members to management roles. Family businesses are always challenged to incentivise non-family senior management if they don't want to give them equity. It is also important, in some cases, that family businesses manage the perception of glass ceilings on non-family employees' career.

The differences in perceptions of risk between family businesses and non-family private companies are fairly small. However it is interesting that non-family private companies include the uncertain economic outlook and geopolitical uncertainty in their top five risks to growth, whereas these issues are absent from the top five risks for family businesses. Family businesses are usually more resilient in turbulent times because of their long-term planning horizon and because they tend to have a more secure financial structure. They are also usually quick and decisive when it comes to decision making.

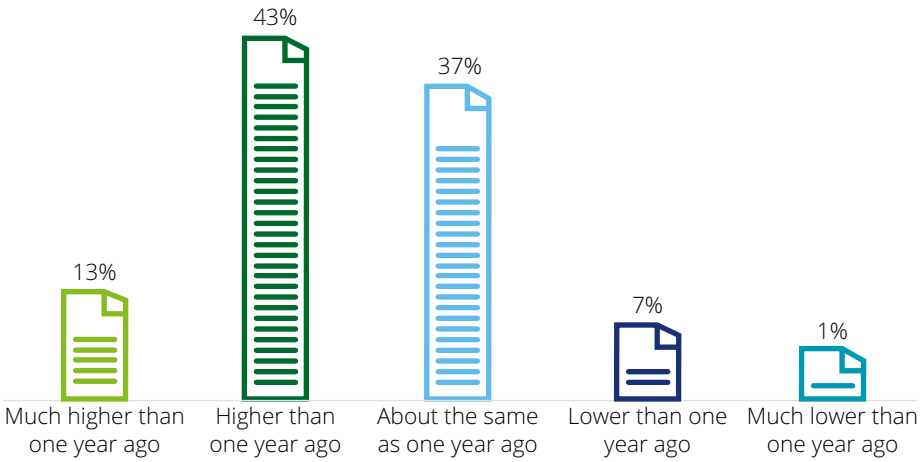
Even so, for 56 per cent of family businesses, the level of uncertainty in their home country with regard to factors that drive business prospects (such as taxes, regulations and credit availability) has increased compared to a year earlier.

Apart from strategic, financial and operational risks, family businesses also face risks relating to the family, from matters such as lack of succession planning, divorce, death and family conflict. There is a link between risk-taking and business value, which may lead to risk-averse behavior in order to preserve the family's wealth.

Table 1. Which of the following may present a risk to your company's growth in the next 12 months? (Top 5)

	Family business	Non-family private company
1	Cost of raw materials and other input costs (24%)	Cost of raw materials and other input costs (22%)
2	Ability to hire and retain employees (23%)	Uncertain economic outlook (in home country) (21%)
3	Competition from market disruptors (22%)	Ability to hire and retain employees (21%)
4	Increased regulatory requirements (21%)	Competition from market disruptors (20%)
5	Foreign exchange rate fluctuations (19%)	Geopolitical uncertainty (20%)

Figure 6. The current level of uncertainty in my home country, based on factors that drive business prospects, is:



Mergers and acquisitions

42 per cent of family businesses expect to acquire another company over the coming 12 months. 27 per cent of family businesses expect to be acquired over the same period.

Despite limited mergers and acquisitions activity in the past year, our survey signals a potential bounce back for M&A as a tool for strategic growth.

Some 27 per cent of family businesses in our survey polled say that they have completed at least one merger or acquisition in the past 12 months.

42 per cent of family businesses say that they are likely (or very likely) to acquire another company over the coming 12 months. On the other hand, 27 per cent expect to be acquired in the same period.

Mostly expect the counterparty in the transaction to be a direct competitor from their home country.

The main drivers behind mergers and acquisitions for family businesses are:

- to expand/diversify the client base (33 per cent)
- to achieve efficiencies of scale (31 per cent)
- to enter new global markets (29 per cent).

Figure 7. In the past 12 months, has your family business completed any mergers or acquisitions?

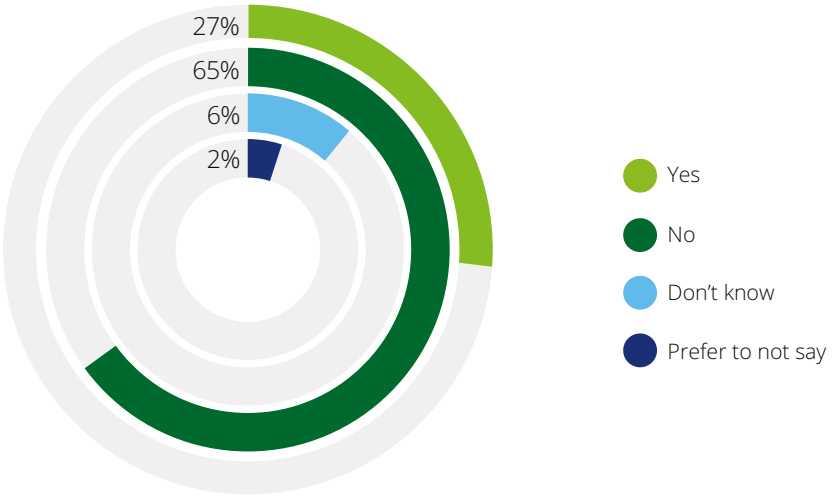
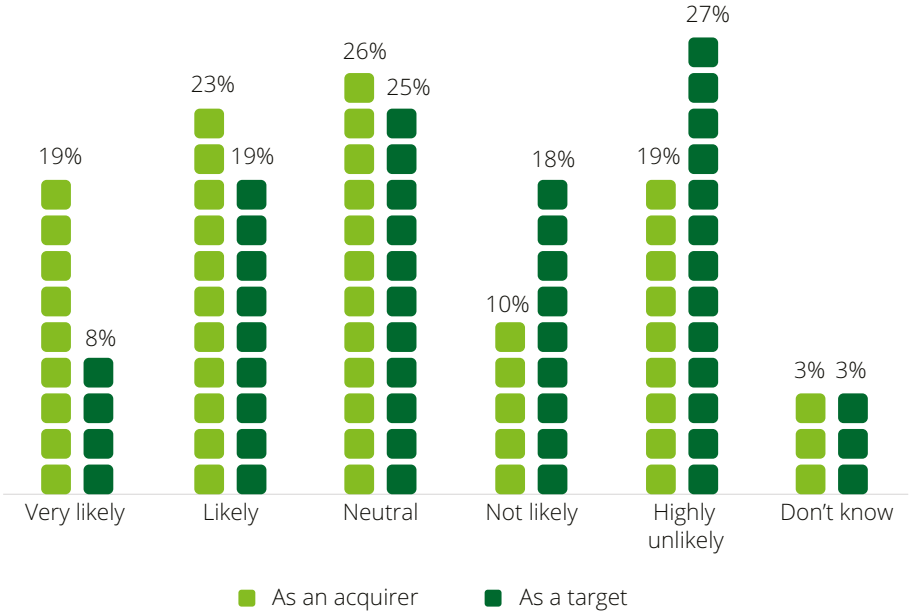


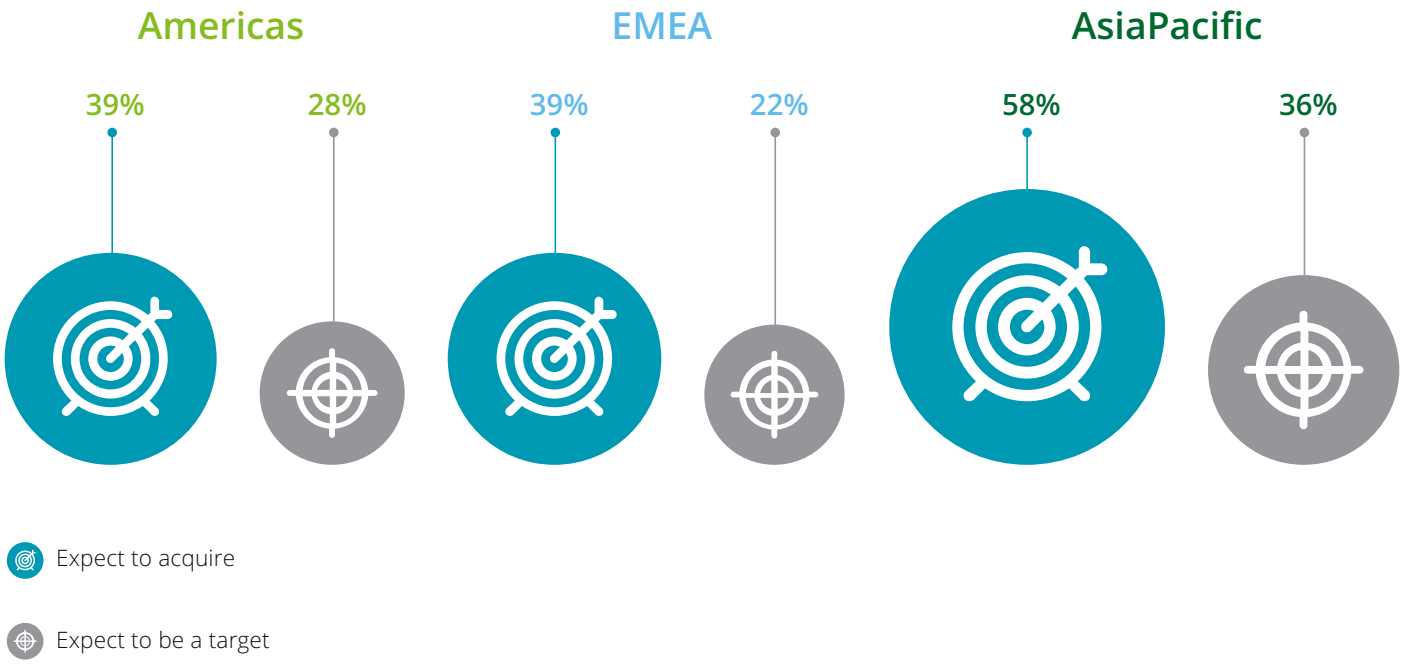
Figure 8. How likely is it that your family business will participate in a merger or acquisition in the next 12 months ... as an acquirer or a target?



Mergers and acquisitions – international comparison

More than half of AsiaPacific-based family businesses expect to grow via acquisitions in the next 12 months. Only 22 per cent of EMEA family businesses expect to be acquired.

Figure 9. How likely is it that your family business will participate in a merger or acquisition, as an acquirer or target, in the next 12 months?
(Percentage of respondents who answered 'likely' or 'very likely.')



Shared markets, supply chains

79 per cent of family businesses rely on international markets for some portion of revenue, and almost half rely on international markets for more than a quarter of their revenue

Family businesses are increasingly interconnected and international, and are less exposed to single markets for their performance.

79 per cent of family businesses rely on international markets for some portion of revenue, and almost half (46 per cent) for more than a quarter of their revenue.

23 per cent say that their business does not generate any revenues abroad. In the next 12 months, this will fall to 19 per cent, suggesting that family businesses are continuing on their path towards globalisation.

Sentiments about supply chains point to increasing global economic integration and a shared sense of optimism. 85 per cent of family businesses say that global trade is important to their supply chain.

Figure 10. What proportion of your family business revenue do you think will come from outside your home country, now and in the next 12 months?

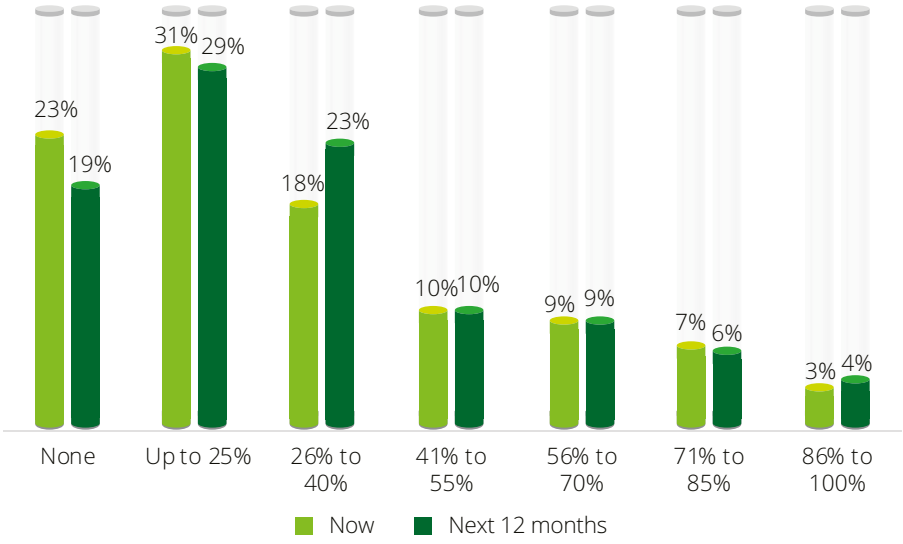
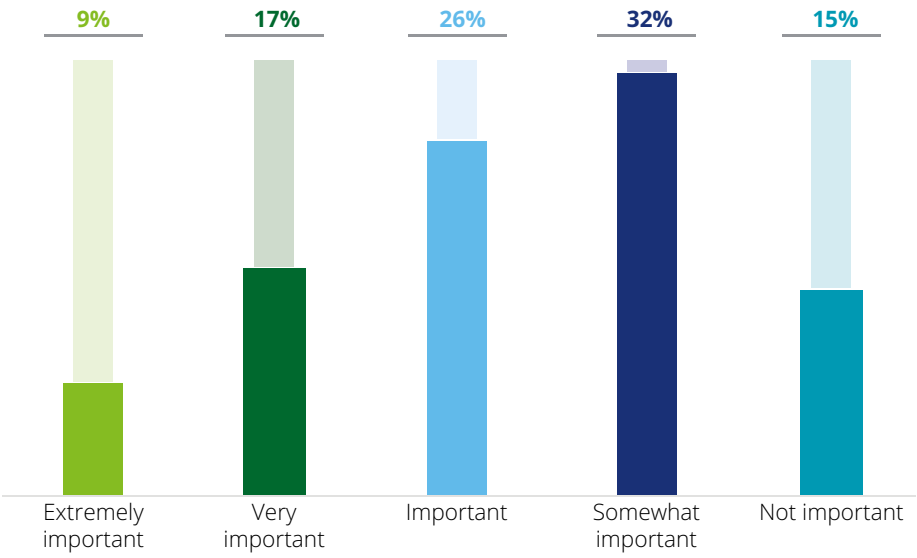


Figure 11. How important is global trade to your supply chain?



Investment in talent

Family businesses value training for their employees and a quarter will invest in leadership development

Family business executives care about their employees, who are often very loyal to their employer. They have a strategy for investing to meet their future workforce requirements, which involves finding a balance between new hires and cultivating the talent they already have in-house.

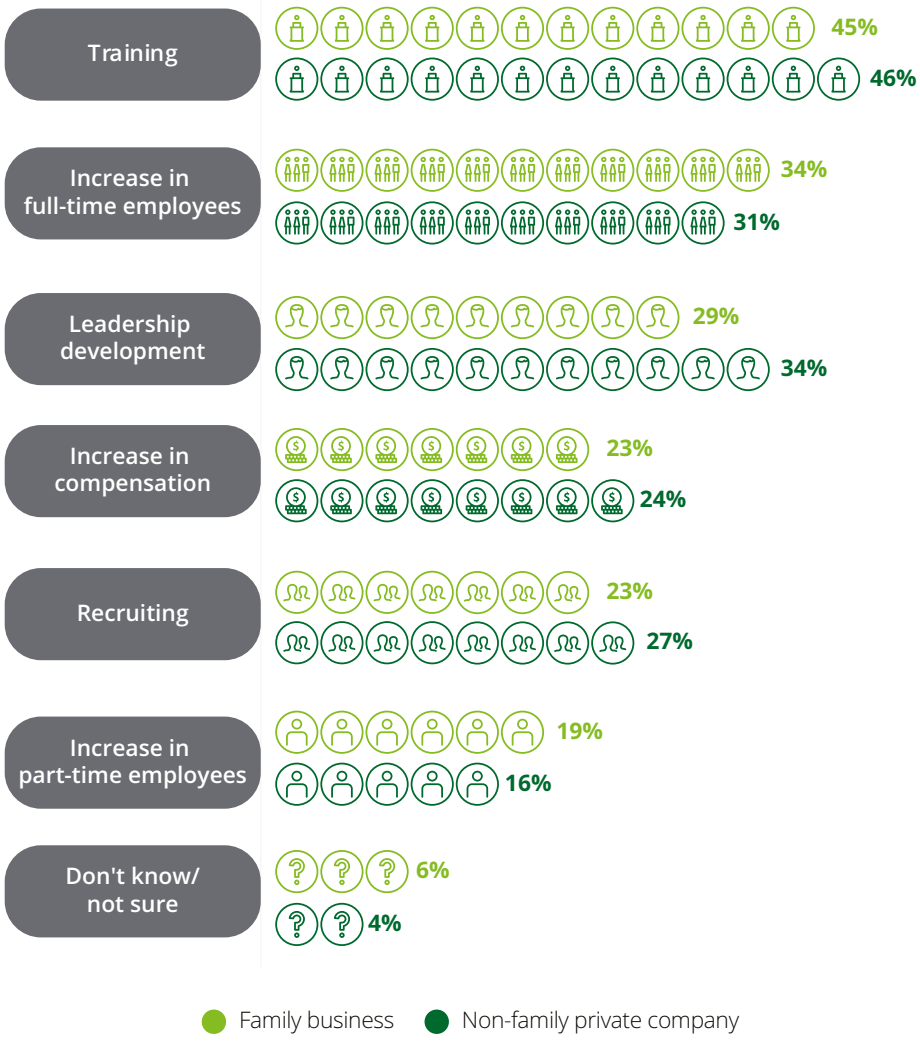
Almost 45 per cent plan to focus on training and development over the next 12 months whilst around a third expect to hire more full-time employees. These results hardly differ very little from those of non-family private companies.

Some 29 per cent of family business leaders indicate that their companies are going to invest in leadership development, five percentage points less than non-family private companies so a lower priority.

Leadership development is critical to success, especially when a company wants to grow in a rapidly-changing business environment. In a family business, the leaders are more than just the executive management team. They also include family stakeholders who might not sit on the board, but nevertheless influence the company's strategy and the balance it seeks between business and family needs.

Given the special importance of leadership succession in family businesses, they need to consider how they develop the next generation of leaders, both family members and non-family.

Figure 12. Which investments in talent is your family business most likely to make in the next 12 months?



Technology driving disruption

Around half of family businesses expect to be disrupted by a non-traditional competitor in the next 2-3 years

Disruption means radical change. Most often, a change in the broader environment, outside a company's control, serves as an early indicator of disruption. The change precedes any action by the company itself.

For many business leaders, disruption is associated with technological innovation. Family businesses expect technological advances, and access to content through different platforms, to have the most positive impact on their business.

Changes in regulation and macroeconomic market conditions are expected to have the most negative impact.

48 per cent of our respondents believe it is likely (or very likely) that their family business will be disrupted by a non-traditional competitor over the next two to three years. This is consistent with the findings of our study *Next generation family businesses – leading a family business in a disruptive environment* (2017), where 47 per cent of the next generation of family business leaders expected disruption.

When respondents were asked which technology trends are likely to have a significant impact on their family business, the five top-ranked areas were:

1. Mobile devices
2. Social media / social business
3. Information security / cyber security
4. Internet of Things
5. Legacy (core) system modernization.

Figure 13. How likely is it that your family business will be disrupted by a non-traditional competitor over the next 2-3 years?

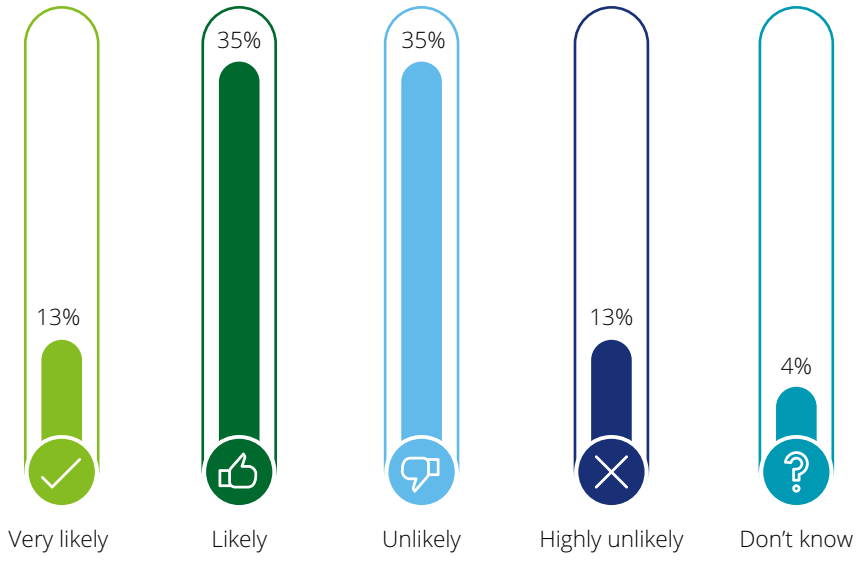
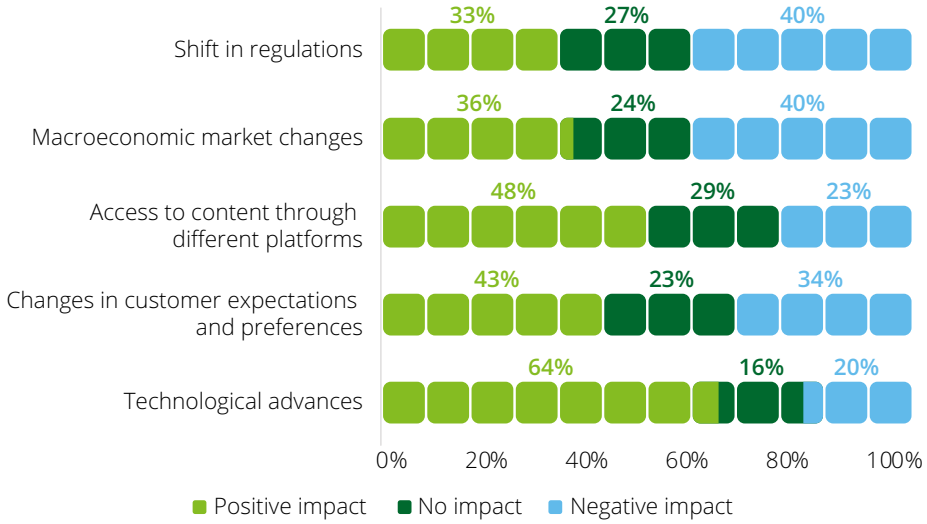


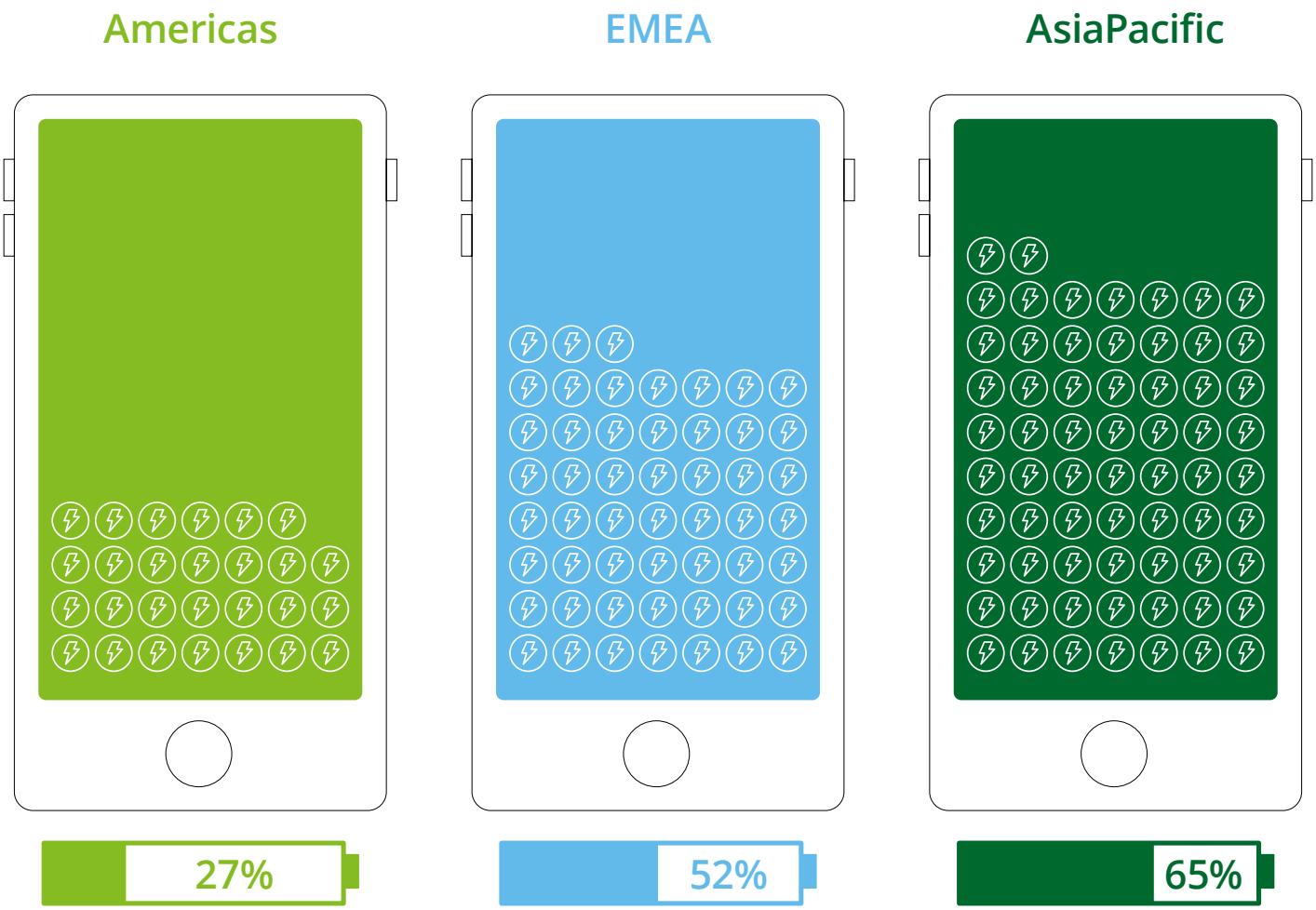
Figure 14. Please rate the impact of the following drivers of change in your market.



Technology driving disruption – international comparison

The majority of AsiaPacific-based family businesses expect to be disrupted, compared to only a quarter of family business in the Americas

Figure 15. How likely is it that your family business will be disrupted by a non-traditional competitor over the next 2-3 years?
(Percentage of respondents who answered 'likely' or very likely.')



Conclusion

Tough questions

Although 53 per cent of the 394 family business executives in our survey believe that uncertainty in their home country is (much) greater than one year ago, they also express optimism about the future. They expect their businesses to grow, which gives them confidence to invest in their workforce and new technologies.

Their long-term planning horizon, their agility and their sound financial structures enable family businesses to maintain their family culture and values while also adapting and progressing the business in response to a rapidly changing business environment.

Even so, family businesses need to consider a number of tough questions:

- How to deal with business leaders, both family members and non-family?
- How to retain employees, especially non-family senior managers, if giving them equity is not an option?
- How to grow via acquisitions, instead of being taken over?
- How to finance growth, and whether to rely on internal funding or whether to seek external funding?
- How to anticipate disruption, and benefit from it?
- What will be the impact of emerging technologies, not only on the business but also on the family system?

For some family businesses the answers to these questions will confirm that they are on the right track. For others, some of the answers could give a gentle nudge in a new direction.

More family business insights

Next-generation family businesses – evolution – keeping family values alive (2016)

https://www2.deloitte.com/global/en/pages/strategy/articles/emea-family-business-initiative.html

Next-generation family businesses – leading a family business in a disruptive environment (2017)

https://www2.deloitte.com/global/en/pages/strategy/articles/2017-nextgen-survey.html

Global perspectives for private companies – plans, priorities and, expectations (2018)

https://www2.deloitte.com/content/dam/Deloitte/at/Documents/about-deloitte/deloitte-private-global-perspectives-2017.pdf

Purpose, place & profit in the family business – a framework for dialogue and discussion (2017)

https://www2.deloitte.com/uk/en/pages/private-markets/articles/purpose-place-n-profit-in-the-family-business.html

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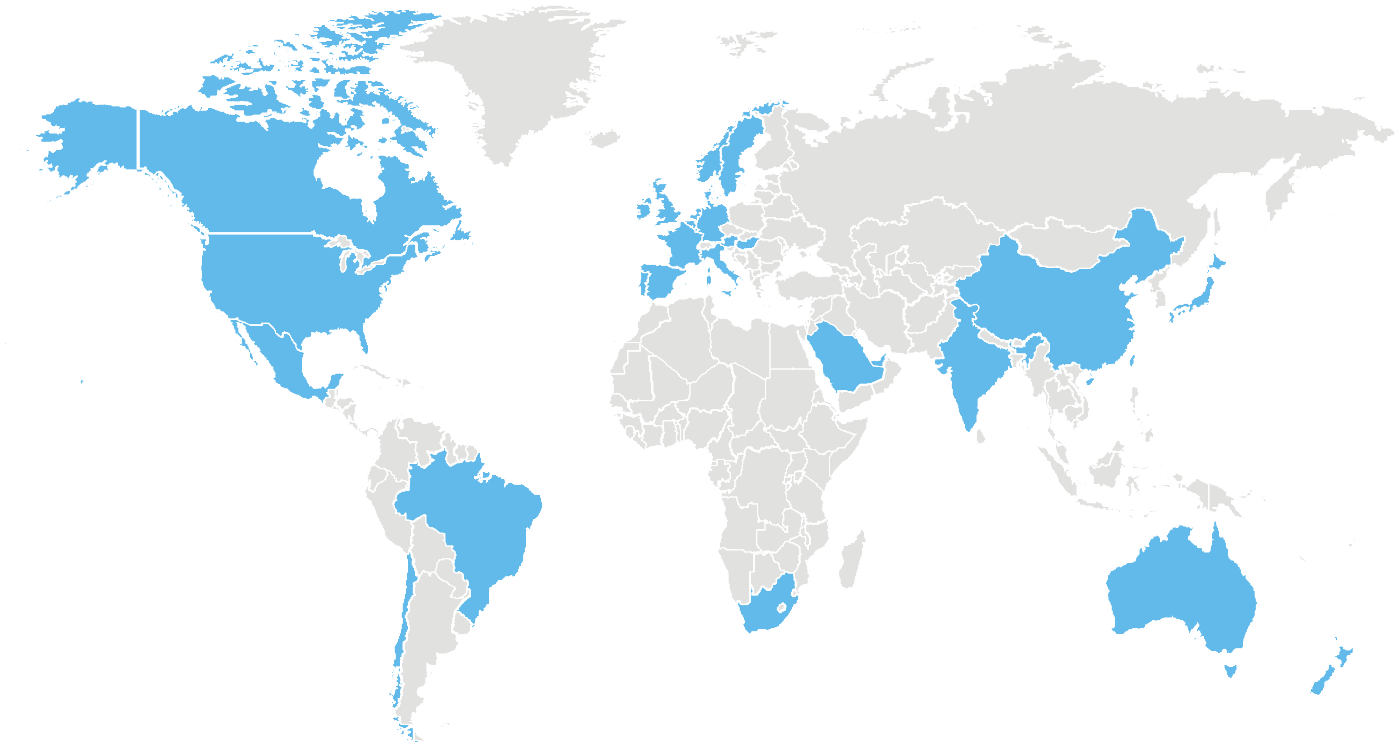
About the survey

From August 14 to September 18, 2017, a Deloitte survey conducted by OnResearch, a market research firm, polled 394 executives at global, mid-sized family companies about their expectations, experiences and plans for becoming more competitive in the current economic environment. Respondents were limited to executives at companies with annual revenues between $10 million and $1 billion.

Some 55 per cent of respondents were owners, board members, or C-suite executives. The remainder included vice-presidents, department or business line heads, or managers.

Some percentages in the charts throughout this report may not add to 100 percent due to rounding, or for questions where survey participants had the option to choose multiple responses.



Deloitte Family Business Centre

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