CEO & CIO Interview of Professor John Davis and Florence Tsai

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CEO & CIO: Some studies show that the success of family businesses is in large part due to their core values. Based on your case study research on successful Western family businesses, have you reached the same conclusion? Could you share your perspectives on this?

John Davis: We have also noticed that the success of multi-generational family businesses is in large part due to their core values. Most of the emphasis on core values comes from the family business leaders. They view core values as an important anchor. Good business leaders will take every opportunity to talk about core values in their roles as guardians of the culture at the companies they lead. All enduring companies we studied have strong core values and well defined corporate cultures. They serve as rudders during periods of change and uncertainty, both of which are accelerating at unprecedented rates.

Florence Tsai: And there are many cases where core values have steered family companies through huge disruptions in their industries. Take the U.S. telecom giant Cox Enterprises, led by third generation family CEO, Jim Kennedy. Today Cox reports sales of $17 billion. But like many U.S. media companies, it could have collapsed during the 1990s and early 2000s. That's when the Internet was driving many traditional media and publishing companies out of business.

Cox's owners refused to panic. They remained patient and accepted low to modest returns on their investment, true to their core values to focus on the long term. This allowed them to save up a war chest of capital, take their public company private again, and rebuild a strong balance sheet so they could diversify from newspapers, TV and radio into telecom. Much of their steady growth now comes from delivering high speed Internet service, and the company is diversifying into growth industries like home health care.

As reported in Forbes, the family's core values of humility and thrift are explicitly stated in the founder's Will that passed ownership of the business to the next generation. So Cox is a great example of how strong core values helped steer a family company through massive change in its industry—and then transform it.

John Davis: Developing strong core values is only part of the recipe for success in family companies. There's a lot more to it, if you want to achieve the enduring advantage that high performing family companies have over non-family competitors. Our field research over 30 years indicates that there are six other factors that go even farther to explain superior performance. To list them:

1. Long-term perspective and investments, known as "patient capital,"
2. Strong loyalty with customers, suppliers, and the community,
3. A loyal employee group,
4. A contributing family,
5. Focus on excellence and ethics, and
6. A stable, committed ownership group and business leadership that demonstrates persistence, resilience and a sense of duty.

These are the key factors in achieving multi-generational family business success. Do well in all six dimensions, and you have a good chance at defying the Three Generation Rule, "富不过三代. " Fail in one or two, and it's usually "game over" by the third generation.

For more learning about how to create successful multi-generational family business enterprises, perhaps you can join the short education program offered by the Harvard Business School entitled *Leading and Transforming Family Businesses in China* that will be taught in three week-long modules. The first will take place in March 2016 at Beijing University; the second in May 2016 at Oxford University; and the third in July 2016 at the Harvard Business School.

Are there any successful cases of Western family businesses fostering their successors that you think might provide a valuable reference for Chinese family businesses? Are there any specific approaches you think are worth sharing?

John Davis: Developing capable and talented successors is critical for family businesses around the world. How to cultivate skilled and motivated successors is increasingly weighing on the mind of first generation Chinese entrepreneurs. The issue is especially dire in China because many business families here have only one child. Moreover, China has not yet developed the broad talent pool of professional managers that entrepreneurs feel they can entrust with the family companies they have built.

During my thirty-plus years of working with leading business families globally and advising my students at the Harvard Business School who are thinking about joining their own family companies, I am often asked whether it is better for the successor to work outside of the company first or start early inside the family company and work their way up the ranks.

I have seen successful examples of both ways of training next generation family members. Both methods set clear guidelines around what qualifies an incoming leader, so that the next generation clearly understands that meritocracy is the standard. The next generation needs to know that being a family member does not entitle them to leadership positions or decision making authority within the family company. They have to meet the performance standards.

Florence Tsai: Whitney MacMillan of Cargill and Axel Dumas of Hermès are good examples of successful Family CEOs who prepared for becoming the family business leader by working their way up inside the company. Each man followed the norms of his generation in developing skills and experience; neither leader built his career outside the family company.

At Cargill, Whitney MacMillan had never worked outside the company when he joined Cargill as a commodities trader and patiently learned the business from the inside, working internationally before becoming the CEO at the age of 47 in 1976. He focused on two main goals as the family CEO: strengthening the family ownership group and diversifying the international food conglomerate. During his tenure, Cargill tripled its revenues.

Born in 1970, Axel Dumas' career had developed along the traditional path of summer internships, university education and a Harvard MBA, followed by eight years of international banking experience at leading financial institutions, before he joined the company. After joining Hermes, Axel spent ten years gaining operating experience by directing the leather goods business that generates half the company's sales. This is a common path for many capable next-generation family executives being groomed for business leadership today. When Axel Dumas succeeded Non Family Insider Patrick Thomas as CEO of Hermès at 43 in 2013, the 176-year-old luxury goods retailer was profitable but in crisis. Axel's first job was to defend the company from a hostile takeover by its chief competitor, LVMH. Fire-tested immediately, Axel proved ready to lead, showing that his development path had been a successful one.

Even so, it is a good idea to plan for a period of overlap between the outgoing business leader and the incoming CEO, just in case the incoming leader needs to take over in a crisis. There's no question that Axel Dumas benefitted from a two-year transition period, serving alongside Patrick Thomas as co-CEO.

John Davis: One other important thing to note about developing successors is that it is helpful for the senior generation to provide opportunities to the next generation, but refrain from planning their future for them. I founded the Families in Business Executive Education Program at the Harvard Business School, which I have chaired since the mid-1990s. One of the exercises we do every year is a cross-generational dialogue, where we ask the senior generation what they think they can do to help the junior generation. We also ask the junior generation how the senior generation can help them.

The junior generation overwhelmingly expresses a critical need of incoming family business leaders. While they really appreciate the senior generation giving them career opportunities within their business network or in the family company, it is important to let the next generation have the freedom to make their own decisions about their future. You can read about these compelling conversations in *Next Generation Success,* published by the Cambridge Family Enterprise Group.

What's important for success is finding the right development path for the next generation, especially identifying what roles suit the talents and interests of every family member. In today's world, it is no longer possible to lead in business simply by virtue of seniority. Yesterday's skills and experience may not necessarily help with tomorrow's challenges. Change is now happening too fast. The senior generation cannot dictate what the next generation should do. That approach is no longer very effective.

A key question facing China's emerging high-net worth families, who produced the first generation of successful start-ups, is how to pass on their entrepreneurial spirit and flair to the new "rich generation". As Chinese society continues to develop and transform rapidly, a key concern is how to achieve a smooth transition in terms of power, values, and governance and leadership. What's your perspective on this issue?

John Davis: Entrepreneurial spirit and flair are both quite difficult to pass onto the next generation—but not impossible. Business families that succeed usually make room for the next generation to experiment with their own ideas. They make room for this inside family company, or else they support innovation outside the family business. Innovation is a necessity for any company's survival. Technology changes impact traditional businesses. Changing business models and industry practices also impact a company's competitiveness.

Next generation executives, both family and non-family, often spot new trends more quickly, while the senior generation brings more industry experience to any new business challenge. Often, the best way to develop effective strategy is for the two generations to consider both perspectives. In fact, Florence and I do a lot of work with family companies helping them reach consensus on strategy across generations.

Florence Tsai: A good example of constant innovation is the Reidel family from Austria. They make fine crystal and wineglasses. Some generations of the family have led innovations in technology; others, like Claus Riedel after WWII, have revolutionized product design.

The company was originally founded in 1756. The Riedels have developed family business leaders for 11 generations, and the company has innovated almost every generation through wars, economic recessions, and changing political boundaries in Europe. What enabled them to survive is passion for the work they do, glass making, and equal passion for innovation in their field. As the products have changed from glass windows to decorative glass to wine glasses, the legacy was passed down through a successful business, but each generation took up the torch of leadership and made it their own by interpreting successful leadership in their own way.

The Reidels actually lost their business during World War II, when all their assets were confiscated by the Czech government and the eighth generation family business leader was captured by the Russians, spending many years in Russian gulag (prison). When the eighth generation father Walter was finally reunited with his ninth generation son Claus, they were able to restart Reidel by buying a bankrupt glass stemware company with the financial help of the Swarovski family makers of decorative glass. (Today, Swarovski is famous for its crystal jewelry.) So they were back in the glass business, but what should they produce? The father, Walter Riedel, wanted to focus on products with high volume sales. And the son, Claus Riedel, wanted to focus on glass stemware, reasoning that after the destructions of war, consumers were trying to rebuild satisfying lives. Claus argued that changing consumer lifestyle would transform their industry. People across Europe now needed wine glasses to share a drink with friends and family on a regular basis. Walter Riedel decided to let his son pursue his particular passion in glass making.

It was Claus, the ninth generation Riedel CEO, who created the egg-shaped wine glass that is so popular today. He also introduced the idea that the glass in which the wine is served impacts the taste and balance of the wine, moving wine connoisseurship to a more sophisticated level.

As Claus Riedel tells his family today, "Stoke the fire, don't save the ashes." You can read more about constant innovators like Claus Riedel in Family Spirit: Stories and Insights from Leading Family-Owned Enterprises (San Francisco: William Grant & Sons and Chronicle Books, 2015).

John Davis: Too often, the senior generation family business leader tries to shape the successor into a carbon copy of himself. A patriarch often thinks that unless the successor is exactly like himself, the incoming leader is not good enough—and will never be. It's a common error. Take Marriott, for example. Marriott Hotels was led by two family CEOs—father and son—before the Non-Family Insider Arne Sorenson recently took over after the retirement of Bill Marriott, Jr.

Bill's father, Bill Marriott senior, had a flamboyant personality. He was a brilliant marketer. His son, with a quieter personality, focused on operations. Early on in his career at the family company, Bill Jr. became almost obsessed with details like standardizing the housekeeping. He wanted to make sure that every single hotel room was pristine. Not just pristine, but consistently clean and consistently furnished, so that the business traveler could rest assured of a hotel room that met expectations every time. Bill Marriott also demanded excellent management of the hotel staff. He knew this was core to customer satisfaction, and instinct told him that customer satisfaction would be key to growth.

Because Bill junior was different from Bill senior, the father did not have confidence in his son's abilities. It took a close advisor and friend of the father to point out junior's talents and to encourage the father to give company leadership to the son. Turns out, it was the best bet the patriarch ever made. Bill Marriott Jr. is considered one of the great scalers among 20th century business leaders.

After taking the helm at Marriott, Bill junior subsequently went on to design and implement many innovations in the hotel industry that are now common practice. He introduced the industry concept of revenue management and diversified brand holdings starting less expensive, no-frills budget hotels. Under his leadership, the company's annual revenue grew from US$100 million when he took over to over US$1.6 billion when he retired.

As you can see from this example, both the father and son had entrepreneurial flair. But they had different kinds of flair. And both were successful. The Marriott story shows how, when the time comes for an incoming leader to succeed an outgoing patriarch, the senior generation should be ready

to take on the role of advisor. Develop next generation family members to take on the roles best suited to their talents and ambitions. Prepare incoming leaders well. Plan to pass the torch not when the outgoing leader is ready to leave, but when the incoming successor is ready to lead. If this is challenging, seek a trusted advisor to help you in making the transition. Then give the next generation the space to lead the family company. The success of a business leader is defined, not only by what he builds, but also what he is able to pass on to the next generation.

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For over thirty years, John A. Davis has served as an academic, advisor, writer and speaker in the family enterprise field. He is a leading authority globally on family business, family wealth, leadership and succession. To learn about his professional activities, visit johndavis.com and follow him on twitter @ProfJohnDavis.

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About Cambridge Institute for Family Enterprise

The Cambridge Institute for Family Enterprise is a global research and education institute dedicated to the real issues facing family enterprises. It is a place where progressive members of family enterprises come to learn, exchange ideas, develop themselves and position their enterprises to be not only successful, but sustainable over generations. Learn about our conferences, education programs, writing and research at cambridge-institute.org and on twitter @CambridgeFE.