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# Bridging the gaps in family businesses

BY MAXINE YONG

Only 12% of family businesses make it to the third generation and a mere 3% make it to the fourth. Clearly, there needs to be a well-communicated plan that takes into account not only the growth of the firm but also the future of the family if the business is to survive and thrive.

Fung Mei Lin, PwC senior executive director and leader of its entrepreneurial and private clients practice, points out that succession planning is a crucial part of the family business' strategic planning.

"Family business owners must have a documented and communicated succession plan in place. They also need to bridge the gaps between the current and the next generation, as well as institute proper conflict management procedures to resolve family conflicts," she says.

According to the PwC Family Business Survey 2016 (The Malaysia Chapter), which was released in January, although 69% of local family businesses have members of the next generation working in the business, only 15% have a robust, documented and communicated succession plan. Some 31% have no succession plan at all.

"In terms of growth, the report survey shows that 19% aim to grow aggressively, 60% to grow steadily and 21% to consolidate the business over the next five years. We think local family businesses are quite optimistic compared with 3% of the global respondents who said they may downsize their business due to the economic downturn," says Fung.

This was the 8th edition of the PwC Family Business Survey. It included interviews with more than 2,800 family businesses in 50 countries that had an annual turnover of US\$5 million to more than US\$1 billion. Of these, 48 respondents were Malaysian family business owners and managers and most of the businesses had an annual turnover of more than US\$50 million.

The report highlighted areas that PwC thinks are the key to ensuring that more family businesses make it to the third generation and beyond, says Fung. Most Malaysian family businesses are still in the second generation. Making sure they survive to the next generation is crucial as they contribute substantially to the country's economic growth.

She says there are three key issues highlighted in the Malaysian Chapter. First, owners need to bridge the gaps between the current and the next generation. Second, they must have a documented and well-communicated succession plan. And the third, they must implement a proper conflict management mechanism.

## ALIGNING EXPECTATIONS

According to PwC's Next Generation Survey, which started in 2014, there are three kinds of gaps between the current and the next generation — communication, expectation and generation. "The latest Next Generation

Survey shows that the communication gap has improved, but there are mismatches in terms of expectations between the two generations. They may not share each other's views in terms of succession or where the business is headed," says Fung.

For example, the Family Business Survey (The Malaysian Chapter) shows that only 40% of the owners plan to pass on the management of the firm to next generation while 38% plan to bring in professional managers and 21% want to sell or float the business. In contrast, 60% of the respondents of the Next Generation Survey said they want to manage the company.

There is also a huge gap between the two generations when it comes to shaping the future of the business. While both generations agree that the business will earn most of its revenue from its current range of products and services, more than half of the younger generation want to diversify their offerings and almost two-thirds want to bring in an experienced non-family professional manager to run the business and enter new geographical markets, says Fung. However, only 50% and 30% respectively of the current generation agree with that.

"It will be difficult to go in a single direction when the succession plan is unclear or if the two generations have different points of view. There will come a time when they have to part ways. We do not want to see that. The current owners need to think about aligning each other's expectations," says Fung.

## PLANNING FOR SUCCESSION

Succession planning is crucial to safeguard a family business, she says. It is very damaging to a business if there is no one to take over when the key decision maker is no longer around.

Even if a family member takes over, will he be adequately equipped to drive the business forward? Will the other family members agree with him?

"Sometimes, the owners do not feel the need to have a fully communicated succession plan — by getting

the buy-in of all the relevant parties such as their children and non-family employees — as they think that since they have done it a certain way, their children will continue to do it that way," says Fung.

"But sometimes, the children may want to pursue other things and may not be interested in managing the business. So, what will the owner do then?"

Who will manage the business after the current owner, or in the interim while the next generation gain experience outside the company? These considerations need to be part and parcel of a succession plan.

"These are the questions a family business owner needs to consider. Family businesses are unique. They are not like non-family businesses where there are no family ties and shareholders can just sell their stakes and move on. But how do you take yourself out of your family business without affecting relationships?" says Fung.

Some owners go about it professionally. They bring in outside expertise, go through a process to select and document a successor and communicate the plan to the rest of the family. Others, however, do not even know where to start.

"All family members must agree that succession planning is important to them and the business. The process normally starts by streamlining the business and shareholding structure, followed by setting a framework for the shareholders. For example, who holds what position in the family business, what values does the business hold, what their roles are in providing strategic direction to the business and so on," says Fung.

"Then, we will decide how new members will come into the business. This part is on family governance. Among other considerations, the family governance system sets out the criteria and process for who becomes shareholders — sons, daughters, spouses or live-in partners of the children — and what their roles are in line with the expectations."

For example, the owner can tell the

next generation that he will accept a RM50,000 mistake. But if they make a more expensive one than that, it will call into question their ability to manage the company. This will help them understand their family and business affairs better.

After that, the owner can formulate a strategic plan that sets out the rules for things like entry, exit and legacy, such as arrangements for family members who do not want to join the business, says Fung. "This is usually a lengthy process. If you can get it done in 12 months, it is considered fast and such a time frame may only be possible if the family is cooperative and agrees on most things. Most of the time, dealing with succession planning is even more difficult than dealing with the business issues."

## MANAGING CONFLICTS

Most of the time, family businesses do not fail because of business reasons but because the members cannot resolve their conflicts. Many families do not communicate properly on matters such as wealth and ownership as it may lead to some members having a false sense of entitlement or expectations that could lead to jealousy and conflicts.

Conflicts are unavoidable as the business grows and more family members join the firm. But they are manageable if the owner puts certain measures in place, says Fung. "There are mechanisms or procedures, such as an appraisal system, incapacity and death arrangements and family councils, to minimise the conflicts."

The owner should make sure that everyone working in the family business is fairly and objectively appraised, especially those in the more senior positions. This is to avoid the cloud of unfair indulgence or "you are well-paid because daddy loves you more", she says.

"Sometimes, it is very hard to tell a family member that he has not met the expected performance — partly because he is a family member and partly because the communication about his roles and key performance indicators was vague. But this needs to be communicated effectively so that it does not turn into a conflict later. That is why these mechanisms are important."

Fung says more and more family business owners are aware of these issues and recognise the importance of addressing them. They, too, are just caught up in the day-to-day operations to deal with the personal, emotional and private matters such as these.

She observes that as more of the next generation decide to pursue their own interests, more of the owners will be open to hiring a professional management team to run the business while their children hold shares in the company.

"I think this is a good idea because children can reap the benefit and dividends and are not locked down by the day-to-day operations. The only caveat is that they must be professional shareholders and owners. They need to know how to set a good vision for the business instead of disrupting the management process," says Fung.



Family business owners must have a documented and communicated succession plan in place.

> **Fung**

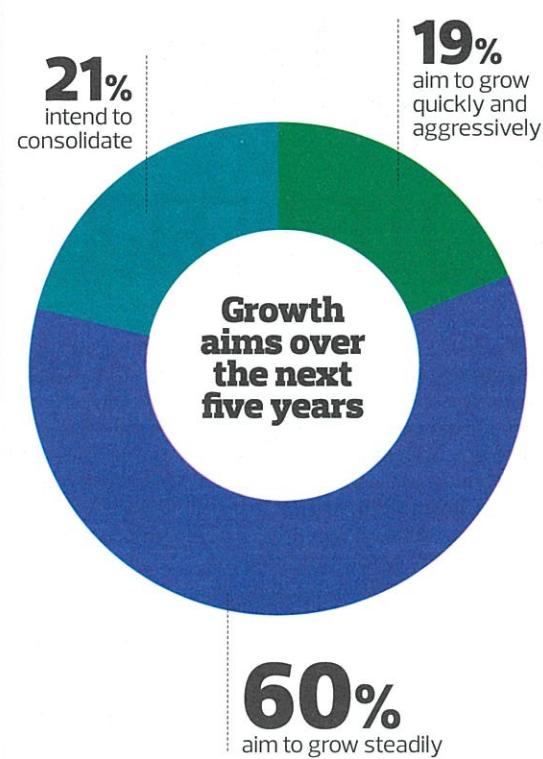


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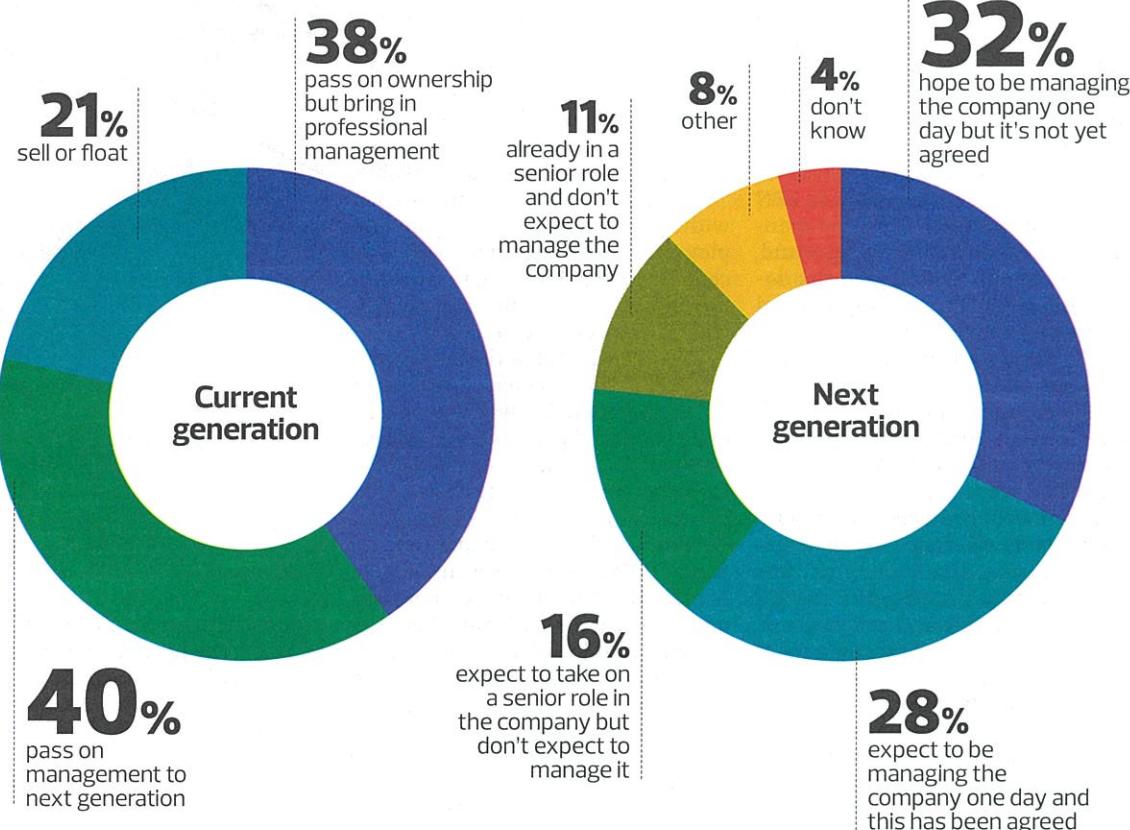
## Succession

**31%** have no succession plan in place

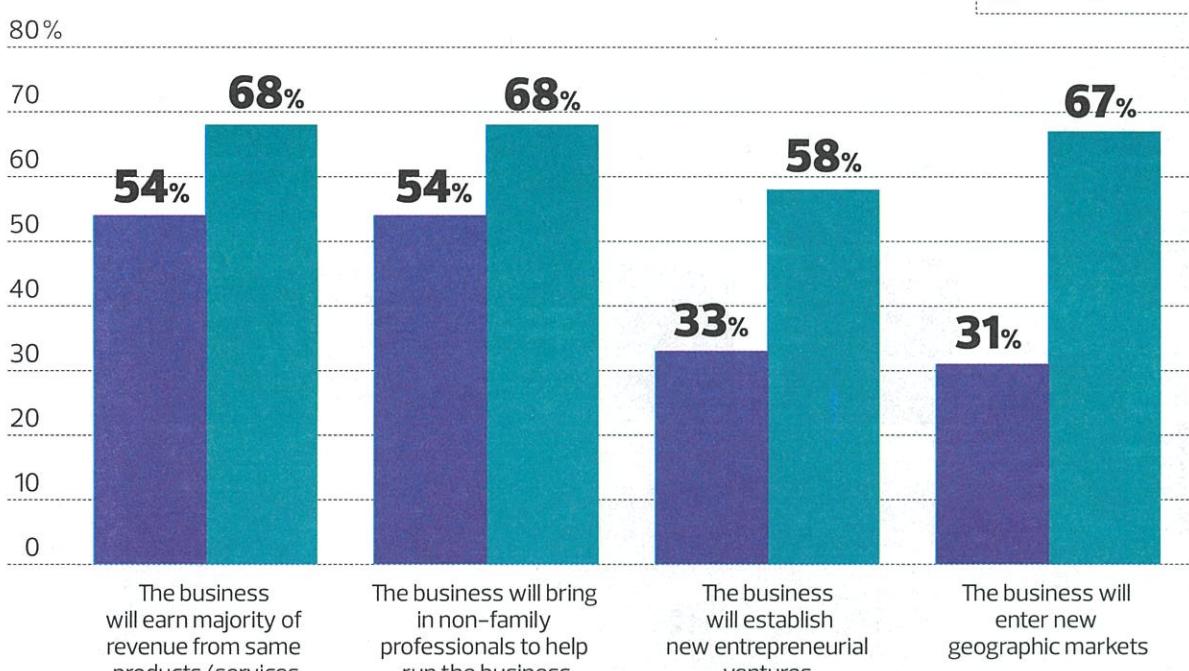
**Only 15%** have a robust, documented and communicated succession plan



## Expectations for the business



## The future of the business



Note: multiple choices; answers do not add up to 100%

## Ten steps to effective strategic planning

### ① It is the "what", not the "how"

A strategic plan is about setting the medium-term goals of the business and deciding the direction of the firm. A business plan is about the specific actions it needs to take in the next 12 months to make the strategic plan a reality. So, having a good business plan is crucial, but it is only half the answer.

### ② Stand in the future and look back

Where do you want to be in three years? In five? Be absolutely clear about what the future looks like and then work out what you need to do to get there, from your products and services to your balance sheet, working culture and organisation.

### ③ Stand in the present and look around

Take a long hard look at the business as it is right now. Do you have a genuine competitive advantage? Are your ambitions realistic? What needs to change? Techniques such as a SWOT (Strengths/Weaknesses/Opportunities/Threats) analysis can help you get an objective view of where you are internally. You can also use PESTLE (Political/Economic/Social/Technological/Legal/Environmental) to analyse the external factors at play in your market. Porter's Five Forces Analysis is another useful way to assess issues such as the threat of new competitors entering your sector or the likelihood of new game-changing products and services.

### ④ Invite input

The CEO needs to drive the strategic plan. But the more people who contribute, the more likely it is to be robust. People are also more committed to something they have helped create. So involve skilled people from across the organisation (and trusted external advisers), including those with a good grasp of how the market is changing. Ask your employees or canvass your customers.

### ⑤ Be prepared for change

A rigorous strategic planning process should challenge the way you are operating today and test its fitness for the next phase. If it does not do that, it is not doing its job. So, be open to different alternatives and new approaches and accept that you may need to adapt your own personal role as well as the way the business operates.

### ⑥ Set a time frame

A good strategic plan is like an itinerary – it is about when you plan to reach the milestones along the way, as well as the final destination.

### ⑦ Assign responsibilities

The CEO and board must take ultimate ownership of the plan, but specific elements need to be owned and driven by appropriate managers, supported by the budget and resources they need to succeed.

### ⑧ Translate the strategic plan into a business plan

Move from the strategic to the tactical by turning the first phase of the plan into a programme of action and implementation over the next 12 months.

### ⑨ Measure, monitor and adapt

As you implement the plan, assess how well it is working and whether it needs to be fine-tuned. Use objective key performance indicators to evaluate progress.

### ⑩ Communicate, communicate, communicate

Do not just share the strategic plan, but the progress you are making against it. This builds a shared sense of commitment, energy and direction.