

The Special Role of Strategic Planning for Family Businesses

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Most family-owned businesses struggle to survive beyond a single generation. Strategic planning—for both business and family—can help to strengthen the family enterprise and extend its lifespan.

Strategic planning for family-owned businesses differs from planning for other types of companies largely because the family firm must incorporate family issues into its thinking.

Family concerns and preferences can influence the choice of business strategy and often make the family reluctant to embrace more formal goal-oriented discussions and decisions. Further, family considerations can limit the strategic aggressiveness of the family firm.

While our research revealed several reasons for this hesitation among family businesses, it also pointed to the critical need for strategic planning and the special benefits to those who undertake it.

That research consisted of three studies of strategy in family firms. Ward (1987) has detailed information on this research. In the first study, 200 privately owned firms that were at least five years old and that employed at least twenty people in 1924 were selected at random from the *Illinois Manufacturers Directory*. (The year 1924 was selected because 1919 was the earliest date of meaningful data.) Interviews at the surviving firms in 1984 documented the family ownership and leadership succession patterns and the evolution of the companies' strategies.

The second study compared the strategies and results of firms that were closely held or family-controlled with the strategies and results of public firms not controlled by families. For this study, we subdivided the PIMS data base (Strategic Planning Institute, Cambridge, Massachusetts) into 300 business units of privately controlled firms and 1,500 units of publicly held firms not controlled by families and studied their strategic profiles to determine the extent to which private companies selected different strategies, competed in different environments, and obtained different results. We explored hypotheses on the long-term orientation of private and family-controlled companies, the emphasis on quality, and so on.

In the third study, we recruited twenty family firms to apply the strategic planning framework to their own businesses. Each business assessed its industry, market, and environmental threats and opportunities. Each firm also assessed its strengths and weaknesses. As a result of these assessments, the businesses selected strategic alternatives that were most appropriate to their situations. Then, they

described their current strategies. In nearly every case, their current strategies were less aggressive than their self-determined strategic potential. Last, each family identified the factors that it believed to have contributed to the conservativeness of its choices. The explanations included questions bearing on estate tax and personal financial liquidity and uncertainty over the eventual success of future family leaders.

With this paper, I hope to stimulate research exploring the special role of strategic planning in the family firm; to provide professionals who serve family businesses with some insights on how families in business approach strategic planning; and, most important, to outline a strategic planning framework for the family business. I want to encourage a formal approach to strategic planning. Many contend that strategic planning is merely one quick vehicle to "strategic thinking"—conscious regular attention to key issues affecting the future of the business. They argue that formal planning is not necessary if "strategic thinking" is present, especially for smaller firms. I prescribe a formal process for three reasons: First, not all family businesses are small. Second, for most family businesses, strategic planning is the necessary groundwork for active "strategic thinking." Third, formal planning meetings and review help to promote the healthy, open, shared decision making so often needed in the family enterprise. Brandt (1981) and Steiner (1969) are two good references on formal strategic planning.

This paper begins with an argument urging strategic planning in family businesses. Then, I define this process for families and identify the particular questions they must address. Next, I illustrate how family issues often influence the choice of business strategy, and I outline a strategic planning framework integrating family and business. I then suggest several unique competitive characteristics of family companies that can influence the choice of business strategy. I conclude by noting the reasons that I believe explain the reluctance of family business owners to plan and the additional benefits of planning specific to family businesses.

The Need for Strategic Planning

A family that perpetuates its company from generation to generation is rare. The study of 200 family-owned Illinois manufacturing firms found that only 13 percent lasted through the third generation. Of these, just a small minority—3 percent ($N = 3$)—actually prospered, as evidenced by an increase of 10 percent or more in their employee base over the sixty years between 1924 and 1984. The results of this study are summarized in Figure 1.

There are several possible explanations for the high failure rate. First, many family businesses are small and

Figure 1. Life Expectancy of 200 Successful Privately Owned Manufacturing Firms, 1924–1984

No longer surviving	80%
Same name still surviving as independent companies	20%
Of the 20% still independent:	
Sold to outsiders	5%
Went public and no longer controlled by the founding family	2%
Still owned by the same family as in 1924	13%
Of the 13% still owned by the same family:	
Grew significantly	3%
Did not grow	3%
Declined	7%
Of the 80% that did not survive:	
Ceased when 0 to 29 years old	33%
Ceased when 30 to 59 years old	36%
Ceased when 60 to 89 years old	16%
Ceased when 90 years old and over	15%

lack the staff and financial strength of larger companies. Second, the family itself can become a stumbling block as the rigors of business sharpen such problems as sibling rivalry and generational succession. Relatedly, the funding of family estate planning, retirement, divorce, and other personal projects often tempts business owners to harvest the company's profit rather than to reinvest it in additional business growth. Third and most important, many owners of family businesses lack a conceptual framework for assessing their company and planning for its future. They often do not take advantage of modern analytical tools that can help them to conquer the challenges of family business continuity. The most critical of these tools is planning—to guide both the company and the family.

My research noted one important pattern among the family firms that had not only survived but prospered: These firms had renewed or regenerated their business strategies several times over the sixty years studied. They added new strategies to their past ways of doing business as market and competitive pressures required response. For example, one food service distributor began in the early 1900s with its founder selling fresh fish to restaurants from a seaport's docks. With the advent of refrigeration technology, the company began using coolers to store and truck fresh and frozen fish and frozen vegetables. Next, the company enlarged its geographic range and added warehouse space for dry goods in order to compete more effectively. Now, the firm is exploring national markets and even export opportunities. Another successful firm began as a stationery supplier to businesses. Then, the firm added furniture to its line, which also moved the business into interior design services. Now, the company is opening multiple outlets for retail stationery, gifts, and cards, and it is considering the

acquisition of a discount office furniture retail store. The key point from these examples is that prospering firms plan actively and add new strategies to their businesses as their environments change. The successful firms in our research pursued change continually.

The research noted another important pattern that was related to the family: Often, the new business strategies came about as a result of changing family influences. In some cases, the new directions were an expression of a successor's interests. In other cases, the plans provided sibling partners with opportunities to "do their own thing" or to obtain some "healthy distance" from each other.

I believe that the best way both of addressing the changing environment and of coping with shifting family circumstances and needs is through a strategic planning process that incorporates both.

What Is Planning?

The term *strategic planning* typically refers to the process of developing a business strategy for profitable growth. It is designed to create insights into the company and the environment in which the company operates. It provides a systematic way of asking key business questions.

Such an inquiry challenges past business practices and opens the way for choosing new alternatives. The result should be a well-prepared strategic plan—usually a written document—that spells out specific steps to improve customer satisfaction, increase profit, and revitalize and prepare the company for the next generation. The plan also states the chosen mission of the business, identifies the direction of future growth, and describes programs that can help to achieve that growth. It thus indicates ways in which the business can compete more effectively.

This approach to strategic planning does not assume that business growth occurs automatically. Instead, it assumes that growth occurs only if specific steps are taken to encourage it. The purpose of the planning process is to determine these steps by asking three questions: In what markets do we want to compete? How can we compete effectively in those markets? and How aggressively do we want to reinvest our corporate and family resources?

The approach advocated here is similar to the sort of strategic planning practiced by most companies. However, the family business must consider the other dimension: the preparation not only of a business strategic plan but of a family strategic plan. The family plan spells out long-term personal and professional goals for family members. It also establishes a process whereby family goals and issues can be explored at regular intervals.

Family strategic planning addresses four questions: First, why is the family committed to perpetuating the business? For example, why not sell the company? What benefits does the family see in keeping the business? Second, how does the family see itself and the company in the years ahead? Does the family envision that many family members will be active in the firm, or will they be passive owners? Does the family see the business creating spin-off ventures for family members? Third, how will the family build or maintain strong relationships, resolve conflicts and work for harmony? How will the family and the business resolve questions of family compensation? Fourth, what are the specific steps required to accomplish the family's personal and professional goals each year? Is this the year to discuss and establish rules, such as expecting outside work experience? Will the family begin regular "family fun" activities, such as group vacations?

Answers to these questions are important, because in a family enterprise they shape business strategy in ways that other companies do not need to consider. Should family members in the company work together in one business and location or apart in separate businesses and locations? How much money does the family need from the company? Are older family members confident that their sons and daughters can run the company well? In its strategy, the company's plan must reflect these considerations.

This weaving together of business and family plans represents a special challenge for the family business, because it means that the business and the family plans are highly interdependent. The business plan requires the family to determine the extent of its commitment to the company. That commitment depends on the prospects for the business that the planning process reveals. As a result, the family cannot separate strategic business planning from family strategic planning. It must undertake both in a connected and simultaneous way.

Realizing the Company's Full Potential

Some owners resist the idea of combining family with business. They believe that business decisions are best and most cleanly made when the decision makers ignore the personal interests of the family. But, those who subscribe

to this school of thought should consider the following: In 1982, we studied twenty family concerns representing a variety of industries and locales that were willing to share their planning process with us. The owners were asked to assess their companies through a comprehensive, strategic planning process. Much to their surprise, the majority of the business owners discovered that they were performing below their strategic potential. That is, they were pursuing strategies less ambitious than their own business assessments would justify.

For example, a company supplying food vending machines and products to businesses was the leader in its market. It was very profitable, and it faced no particular competitive or technological threats. Yet, for several years the firm had been plodding along doing nothing different except refining operational procedures, such as developing sales commission systems and computer programs that provided more detailed information on delivery and repairs. Although the opportunities for growth—in new cities, in cafeteria food service, in new product lines, and other areas—were bountiful, the company did not have a vision. The stagnation came from wanting to limit the possibility of dispute among the three brother owners, to wait until the plans and capabilities of the next generation were clear, and to avoid a business spending commitment while their own personal financial plans were unaddressed.

Owners offered two explanations for the disparity between their strategic potential and their actual—less ambitious—strategic choices. First, they were unsure of the way in which family members might influence their businesses. For example, they did not know whether all members would want to work together under a single roof or whether they would prefer to work apart in autonomous business divisions. They did not know whether those in the business would have to provide financially for those outside the business. They did not know whether they as parents might wish to set cash aside for the new ventures of entrepreneurially minded offspring.

Second, owners were unsure of their own commitment to the company's future. They were unsure because they had not explored or settled such key issues as the amount of money available for new projects or the amount of managerial talent that potential successors possessed. As a result of these uncertainties—all related to their families—the owners selected more cautious, conservative business strategies. They did this despite self-avowed confidence in the underlying strengths of their companies.

This study demonstrates that family issues strongly influence the choice of business strategy in a family business. Family issues shape business judgment whether the fact that they do is formally recognized or not.

How Planning Begins

When a family business faces almost any setback, a specialist in strategic planning may well be called in. The problem can be characterized in such terms as these: "We're not as innovative as we should be." "We're losing profitability."

“We’re wasting a lot of energy debating where we should be going.” The first efforts of the planner, as he or she begins to intervene, are usually to profile the current situation, using financial analysis or competitive analysis or customer analysis, and to interview the senior managers on what they see as the key strategic issues facing the firm.

The first entry into the business can offer insights on its health and aggressiveness. The interviews often uncover all sorts of family business issues, such as uncertainty about succession, rivalries among family members, and discrepancies between position and performance.

In any case, the planner or consultant looks for opportunities to generate enthusiasm about the planning process. The hesitancy to undertake strategic planning often results from fear that it is an unfamiliar process and that it may reveal confidential data, expose weak management communication practices, and surface past errors and current family issues. The planner is asked to propose a process that gets strategic planning going.

Step One: The Commitment of Family

In a family business, the ideal starting point for the planning process is the family itself. The first step is for the family to establish its level of commitment to the future of the business and to planning as a way of securing that future. Is the family willing to sacrifice short-term material gains in order to invest money in the company? Will family members spend the time it takes to build a business? Can they work together? Do offspring have the necessary qualities of leadership? Are parents willing to let go of the company when the time comes?

If family members reach a consensus on these issues, they can write a preliminary statement of commitment. Such a

statement might say, “We are fundamentally interested in the long-term future of this business. We want this business to last forever. And, we will do what it takes to accomplish that!” Whatever the resolve and rationale, the family’s statement of commitment is a necessary first step. As Figure 2 shows, the rest of the planning process flows from this commitment.

Step Two: Assessing the Firm’s Business Health

Next to the family’s commitment, the foundation for planning lies in a financial and market analysis of the business. Such an analysis is common in firms that practice strategic planning. It shows whether the company is gaining or losing market share, using cash efficiently or inefficiently, and increasing or decreasing its productivity. Such analysis has an additional significance for the family business. Among other uses, it reveals whether the family is reinvesting sufficiently in the business to help ensure a vital future or whether it is financing personal needs at the expense of the company.

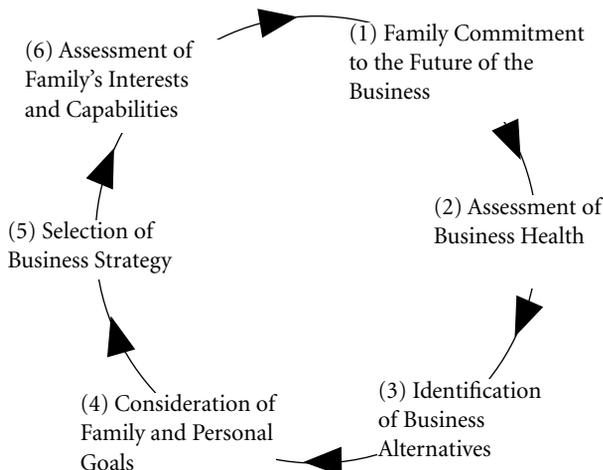
Natural forces within the family business probably encourage dis-investment from the business over time. So-called excess cash from the business is often used to reward the family for years of sacrifice with an improved standard of living. Or, it is used to meet such perceived needs as retirement and inheritances or to retire debt or reward loyal employees.

Most successful families are unaware of the damage done by these financial “harvesting” practices. They assume that all is well if profit is strong and sales are rising. They think they can afford high levels of personal spending. Yet, successful businesses must have a certain amount of reinvestment if they are to continue to grow. In fact, the longer family members want the business to live and the more prosperity they want to enjoy in the years ahead, the higher their rate of current reinvestment must be. Families that spend the company’s profit elsewhere set in motion forces that silently weaken the firm, often in ways that will not show up on the bottom line for years. At that point, it may be too late to reinvest and turn the company around.

Financial analyses uncover potential soft spots. They illustrate just how much money is going into such areas as family bonuses and how much is being plowed back into the enterprise. The most important of these analyses figures the rate of reinvestment in the business.

Approaches to the calculation of rate of reinvestment range from figuring debt-to-equity ratios to judging the number of strategic experiments under way. One of the most useful approaches compares the return to the owner with the return to the business. This approach figures family salaries, bonuses, and perquisites as a percentage of the total sum available for future business opportunities. That sum is typically measured by net income before taxes. To figure the percentage, owners divide family salaries plus perquisites by that sum. Family salary and perquisites should usually be no more than 33 percent to 50 percent of operating income

Figure 2. The Interdependence of Family and Business Planning



for midsize companies with more than twenty employees. If the figure is significantly higher, the family is milking the business for short-term gain. It is withdrawing more funds than public companies typically pay out in dividends to their shareholders.

To be sure, milking or harvesting the business may be desirable for some families. Perhaps a family has concluded that the future of the company is dim or even hopeless for reasons beyond its control. If that is the case and the family still wants to find a long-term, prosperous role for itself in business, the family should harvest profit and seek other ventures in which its members can invest. But, if the family has concluded that its firm is a satisfactory investment, the harvesting of profit clearly compromises the future vitality of the family business.

Step Three: Identification of Business Alternatives

The next step is to identify possible business alternatives: enter new geographical areas, increase the quality of service, hire strong managers to generate sales or improve productivity, and so on. At this stage, family businesses can consider some of their possible uniquenesses or advantages.

Truly clever strategies capitalize on market insights and the relative competitive strengths that the individual business enjoys. Good family businesses will share some strengths by the very fact that they are family businesses. The following insights were supported by the study that compared the strategies and performance of nearly 300 family companies with the strategies and performance of 1,500 public companies.

Many family firms enjoy the benefits of a long-term orientation. They rarely have outside shareholders to whom they must justify quarterly performance in sales and earnings; no stock market will judge them harshly if they increase expenses for worthwhile strategies. They can afford to focus their vision on the future. They also tend to have a flexible organization, with fewer bureaucratic layers that can stall a needed market response. The company's motivation for quality, born of having the family's own name on the door or in the board room, often produces quick service and top-notch products. The company is adaptable to smaller markets. It is often willing to invest in people. And, if the family provides a unified culture at the top of the organization, it becomes easier to establish business direction and to get everyone pulling together in that direction. Clear direction increases a company's chances of success.

The strengths just listed have clear implications for the strategic direction of any family business. The strategies that are suitable to these particular strengths include exploiting smaller markets, market niches, ethnic or regional markets, declining or more mature markets that yield profit through personal effort, and emerging markets. Smaller companies can also emphasize craftsmanship or customized services or products.

These strategic directions suggest that the smaller family business does best by seeking out the "hidden customer"—

the buyer whom others have somehow overlooked or ignored. Of course, big and small companies alike desire that customer. But, the family business has some specific advantages that can help it to win even when it competes with companies that have larger staffs, more financial clout, or both. Its very smallness gives it the ability to respond quickly. The personal involvement of the owner tends to seal the loyalty of employees and customers alike. And, if it is physically close to its market, there is the potential for such extra services as emergency delivery and personal tracking of customers' tastes.

These possibilities also suggest some relative weaknesses of the smaller family business, such as limited access to large amounts of capital, naiveté of management, or inattention to cost-cutting measures. In the business strategic planning process, I encourage attention to the relative strengths and weaknesses of family ownership. Explicit recognition of these characteristics should improve the choice of strategy.

Reluctance of Family Business Owners to Plan

The planning process outlined in this paper often seems threatening to business owners. Many think of planning as a straitjacket that will constrain their instinctive survival skills and limit business flexibility. The nature of the planning process also requires these independently minded business owners to share decisions—and private financial statements—with others in the company. These statements represent power and information that many owners would rather keep to themselves.

Others object to planning because they think the future is too uncertain to make the effort worthwhile. Rapidly changing markets, an unpredictable economy, and the unclear career interests of offspring are just a few of the unsettled issues that they foresee.

Perhaps the greatest threat is the association of planning with change. This association seems to create nearly unresolvable dilemmas, because change requires compromises. For example, satisfying the demands of customers for a new product may require the business to divert money from successful projects that have a guaranteed return to experimental activities whose return is unknown. Executing the changes suggested by planning also often requires business owners to tailor their products to specific customers in specific markets. Such tailoring destroys the Be All Things to All Customers principle that guides so many businesses in their early years, a principle that is especially attractive to the business owner who sees a variety of customers and products as a way of diversifying risk from any one category of product or customer.

Executives in nonfamily businesses are often exposed to more businesses over time, and they may have more experience with sophisticated planning systems. More important, they are less likely to see the stability of the business as critical to the preservation of their own family wealth and well-being. In any case, my experience suggests that a mature business owner who owes his personal wealth

and life-style to a strategy that he or she has built or designed is reluctant to change the successful formula.

Benefits of Planning

As we have seen, formal planning helps to prevent family businesses from “undershooting” their strategic potential by articulating assumptions and perceptions. Planning encourages commitment from family members as a part of the process. It provides techniques that help managers to assess the company’s rate of reinvestment and assure that the business is retaining sufficient cash for a solid future.

The very nature of planning requires a variety of people to be involved. Those who report directly to the chief executive will contribute to the business plan. Members of the immediate and, often, the extended family will be involved in the family strategic plan. As a result, the planning process increases business knowledge throughout the company and the family and provides outstanding training for offspring, who are the successors and future leaders of the company.

Planning provides one other key benefit. Because it requires the participants to answer tough questions about competition and reinvestment, the planning process helps all managers and family members to develop a common understanding—that is, the same assumptions—about the world in which the company operates. Consequently, at the very least, business planning should encompass everyone who reports to the business owner and every family member with a key management role in the present or future.

Such a common understanding is critical, because conflict in family businesses is often caused by differences in basic assumptions or values, especially among family members involved in guiding the business’s direction. For example, consider the father and son who are arguing about whether to install up-to-date manufacturing equipment. The argument may be less about the value of technology than it is about the relative value of change and consistency. The young often argue for change; the old, for the status quo. Typically, they will not attempt a straightforward resolution of such underlying differences. Instead, they may begin to argue about personalities or management styles. Such discussions can easily cause emotional pain. The original objective—to decide whether or not to install new equipment—is forgotten.

The Special Role of Personal Values and Family Communications

Even within families, values are bound to vary. They shape the choice of goals, modify the ability to tolerate risk, and influence ideas about teaching and learning. They show up in family decisions that in turn mold business strategies and the approach to strategic planning. How much money does the family need for security? The answer to this question affects the level of investment in a business strategy. To what degree should family differences be openly discussed and tolerated? The answer to this question affects the ability to debate business facts and perceptions. How close should family relationships be? The answer to this question affects

decisions on geographic expansion.

All these questions are critical examples of how family factors influence the choice of strategy in a family business. Answering these questions can lead to conflict. Understanding that there is no absolute right or wrong in many of these issues is one step toward compromise. Strategic planning is a valuable tool that helps to build such qualities as the ability to work toward consensus, team management, and shared decision making. It identifies the fundamental business and family assumptions in a constructive way.

Strategic planning strengthens the ability to share decisions and value orientations. Both are critical requirements for success in perpetuating the family business. So, in addition to providing a framework for evaluation and choice of a business direction and family goals, strategic planning is a process that prompts healthy communication on critical family business issues.

Conclusion

To keep a family business moving forward requires a spirit of reinvestment: a confident eagerness to commit funds for the sake of future family benefits. Motivating the family requires a compelling vision—a commitment to a family dream—that everyone shares. When such a commitment has been made, the family can aggressively invest family funds in a business strategy.

There are many challenges to sustaining a family’s emotional investment in an enterprise from generation to generation. Deliberate strategic planning is one key to success. It helps to create motivation that can sustain the family and business through inevitable differences in individual perspectives. Good planning releases energy that the family can use to fulfill the dream of many family businesses: creating and sustaining a healthy family enterprise for the next generation.

The insights gained from the three studies outlined at the start of this paper and from personal experience suggest how strategic planning in the family business differs from planning in nonfamily business. It is clear that business and family strategic planning promote continuity in family businesses.

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