



Family Businesses & Governance: Lessons Learned

DIFC Knowledge Series 8: Setting up a Family Office

Dr. Nasser Saidi,
Chief Economist, DIFC Authority
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Agenda

Importance of Family Businesses

Performance/ Challenges for World/ GCC Family Firms

Family Businesses & Corporate Governance

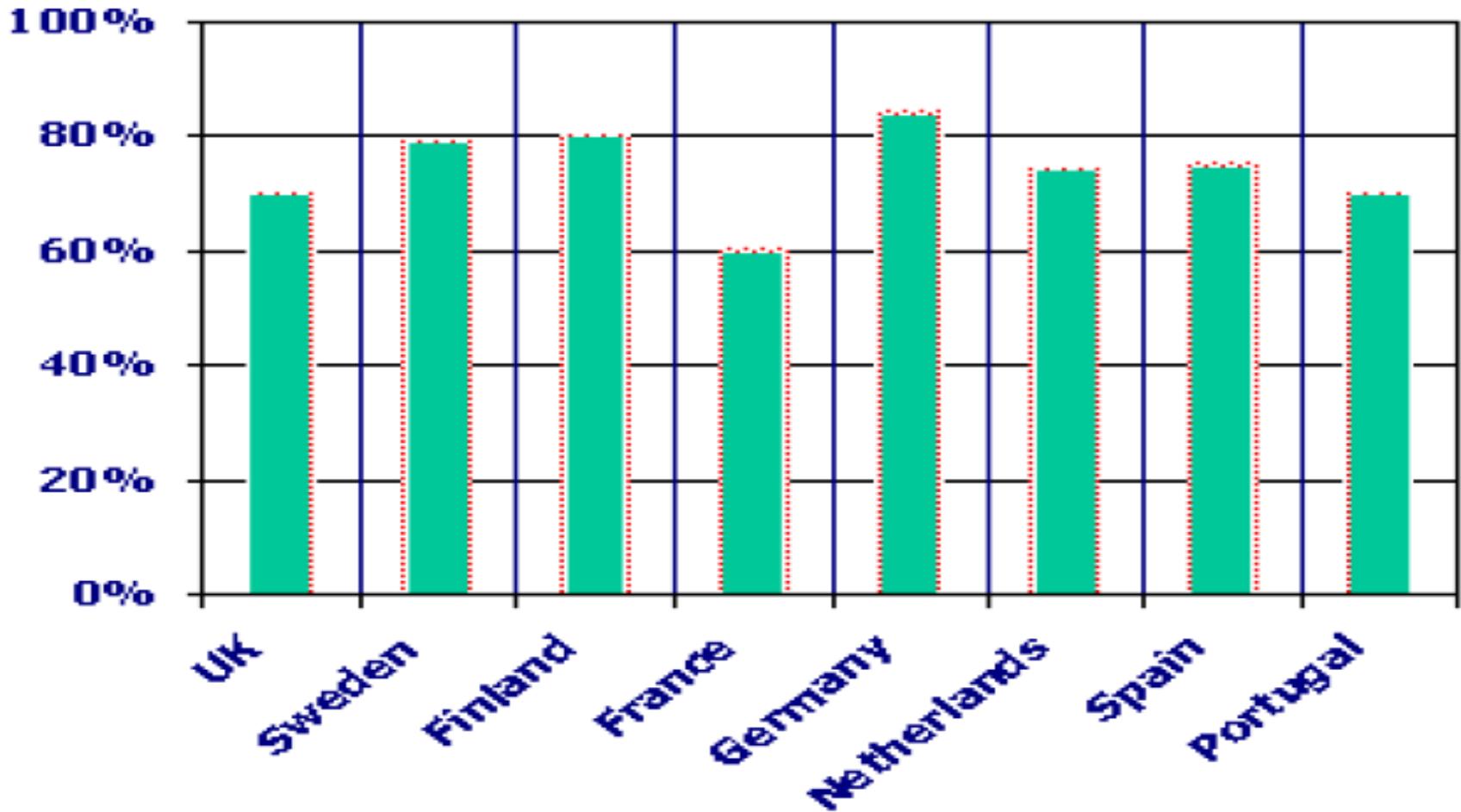
Hawkamah-Mudara & The 'Family Business Forum'

Families are dominant economic units

- **Family Business constitutes world's oldest and most dominant form of business organisation**
- **In many countries, family businesses represent more than 70 % (MENA \geq 90%) of all overall businesses and play a key role in economic growth and workforce employment**
In Spain, for example, about 75 percent of the businesses are family-owned and contribute to 65 percent of the country's GNP on average
- **One-third of all companies in the S&P 500 index and 40% of the 250 largest companies in France and Germany are family businesses**
- **Most family businesses have a very short life span beyond their founder's stage and some 95 percent of family businesses do not survive the third generation of ownership!¹**
- *Entrepreneurial-led Family firms only have an average lifespan of about 24 years ; only 30% survive into the second generation, 10% into the third and a mere 3% into the fourth - David Pistrui of Acumen Dynamics in MEED magazine*

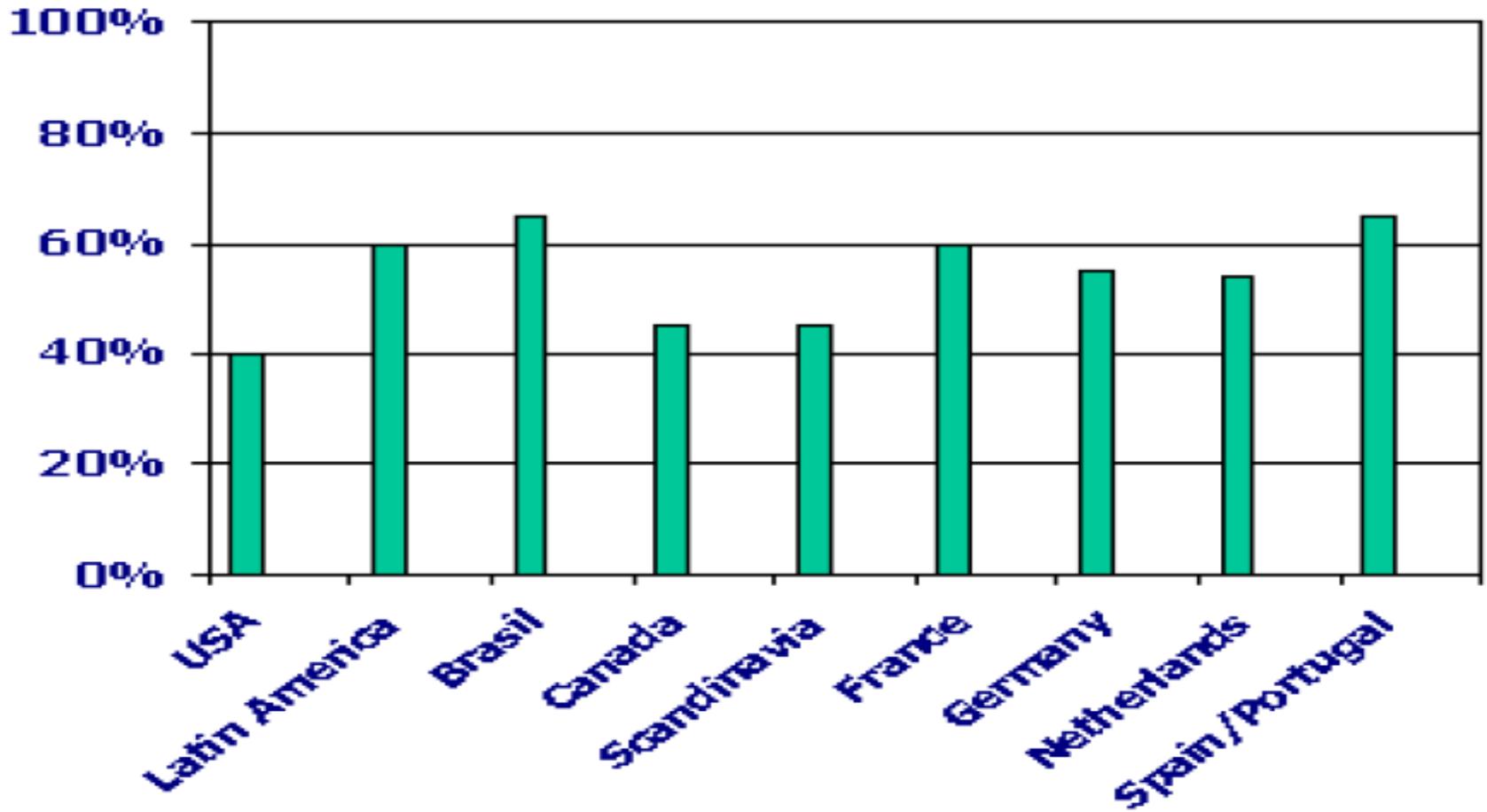
¹Source: The Family Business Network, www.fbn-g/fbn/main.nsf/doclu/facts.

Family Businesses are Dominant: % of all businesses



Source: FBN

Family Businesses are major contributors to GDP

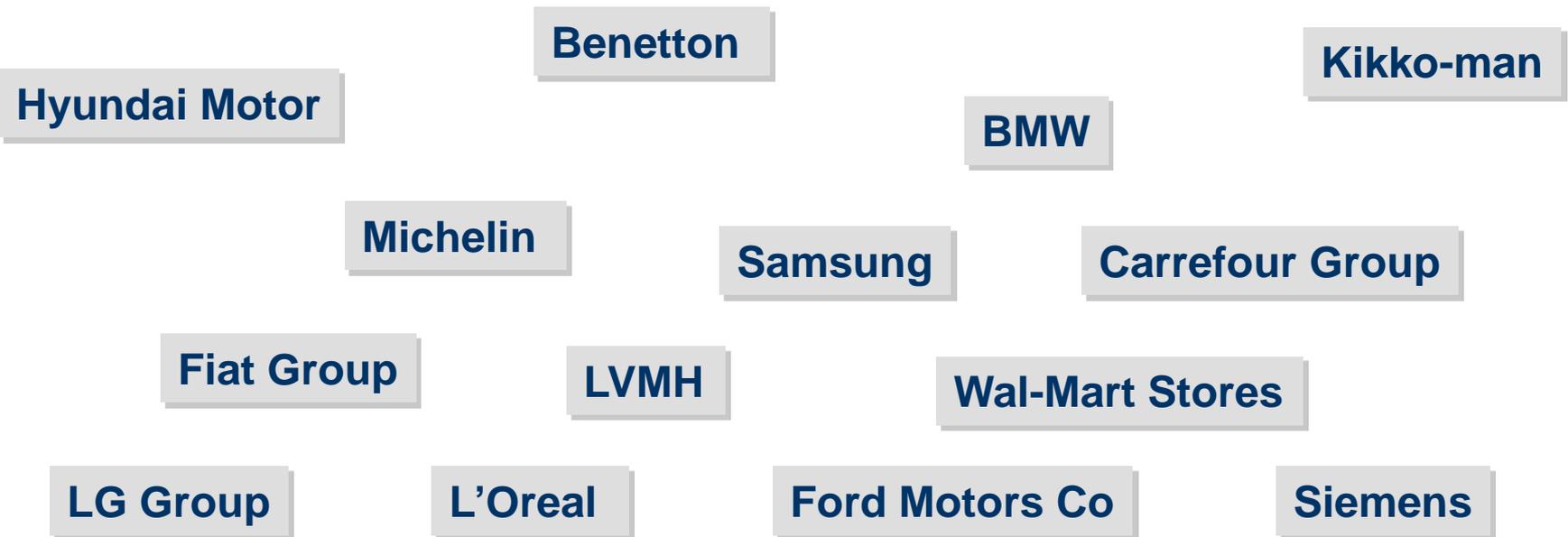


Source: FBN

FOEs are both SMEs and conglomerates

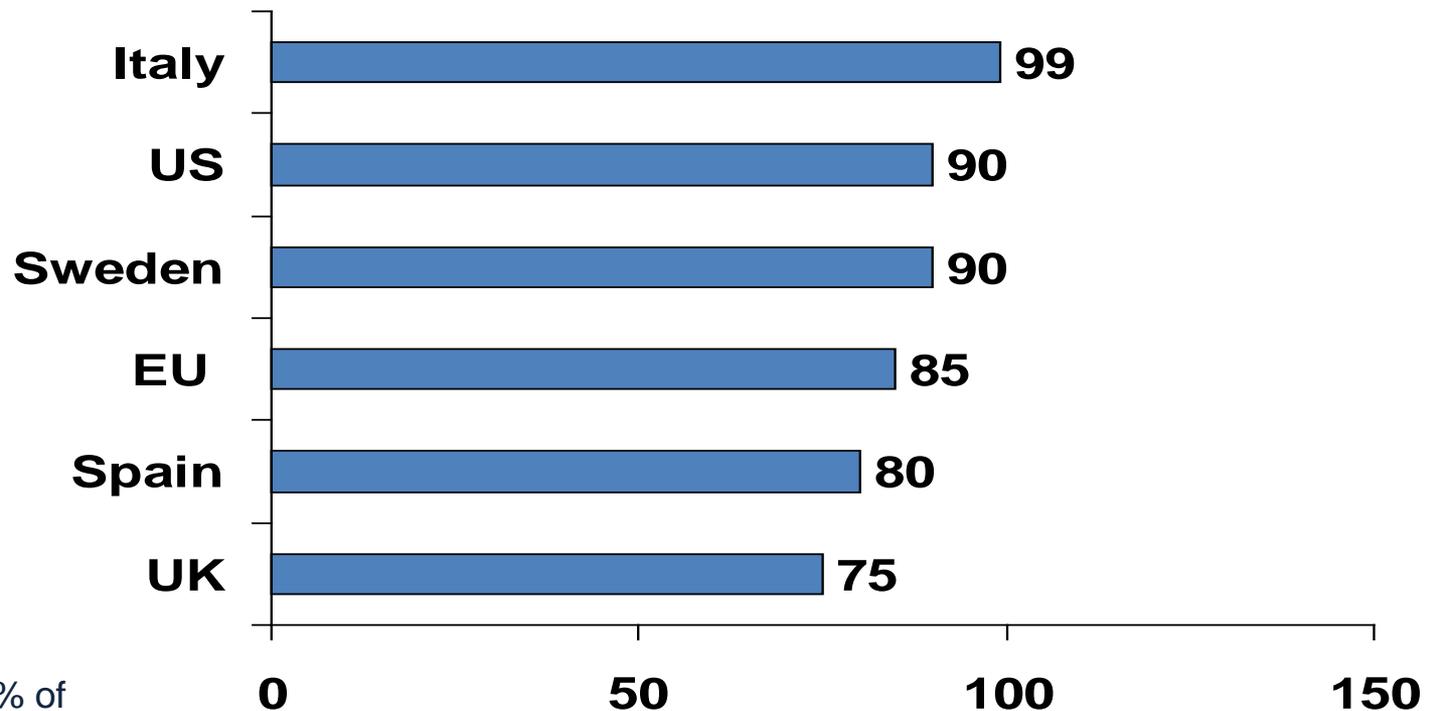
Family Businesses range from small and medium sized companies to large conglomerates that operate in multiple industries and countries

A Few Examples...



Family-run firms predominate in OECD economies

Proportion of OECD Firms That are Family-Run
Percent



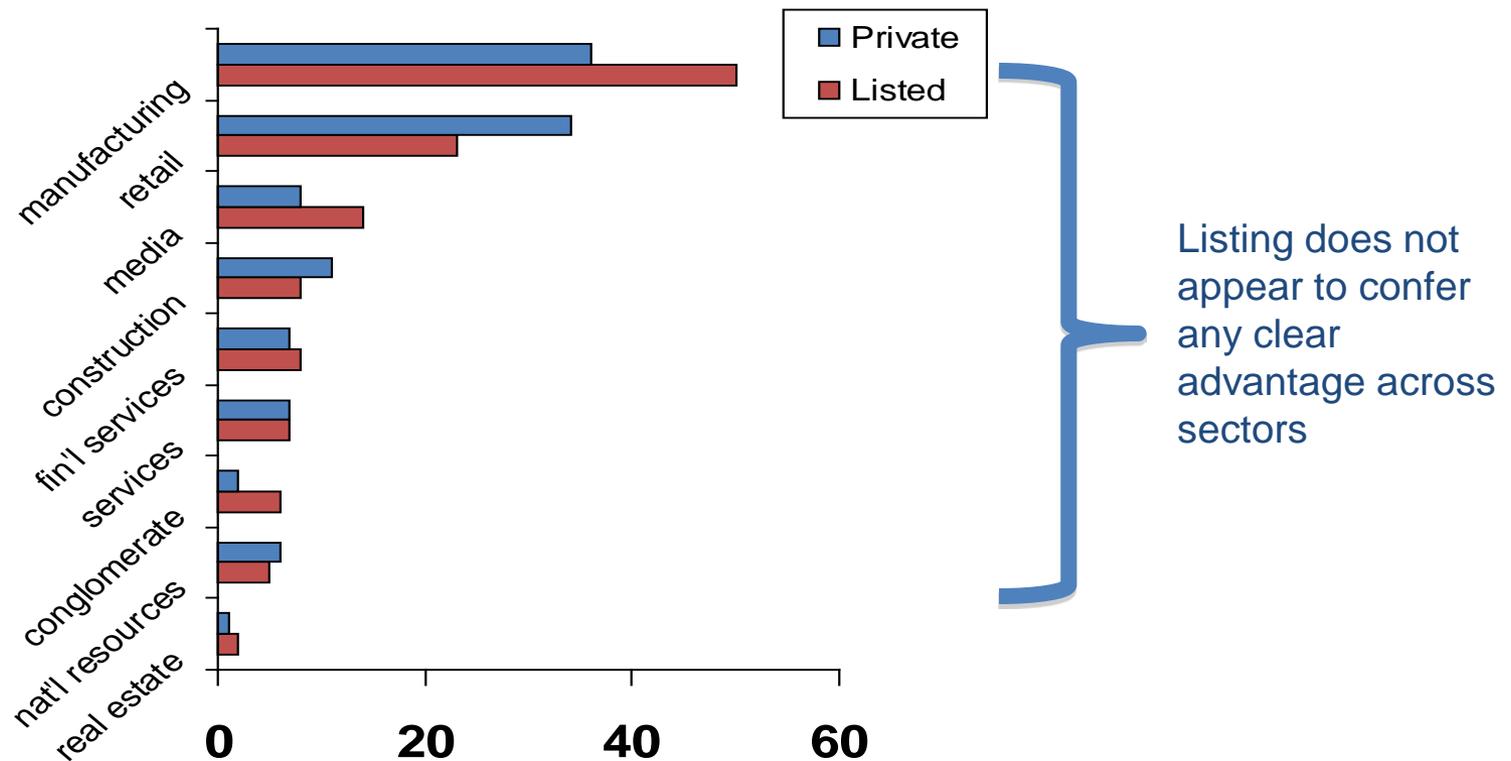
Over 85% of
EU/US
businesses are
family run

Source: Nancy Upton and William Petty, "Venture Capital Investment in Family Business," *Venture Capital*, 2000, Vol. 2, No. 1, pp. 27-39

FOEs are comparably represented across industry sectors

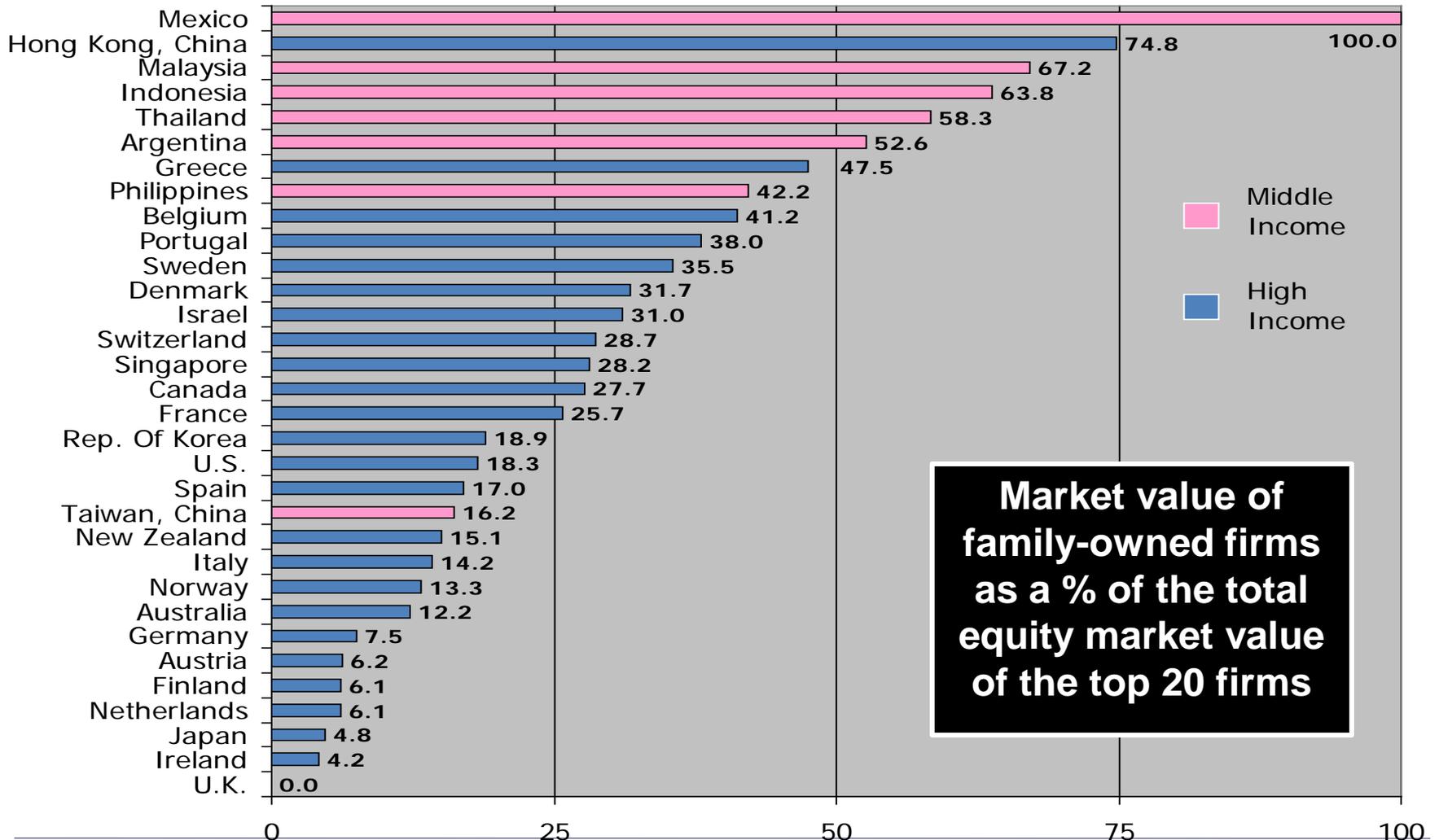
Distribution of Large, Family-Run Firms across Sectors

No. of Firms



Source: Family Business Magazine; OECD Analysis

Family Firms Play an Important Role in Markets (OECD)

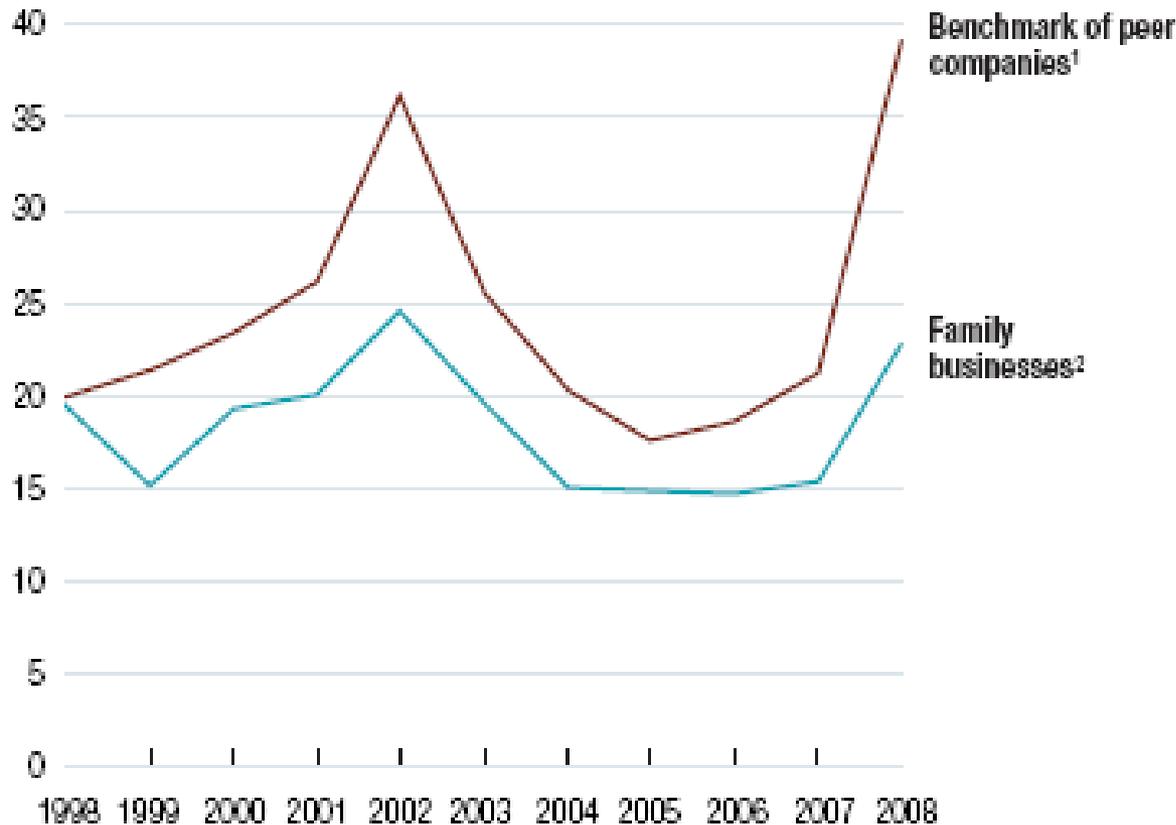


Market value of family-owned firms as a % of the total equity market value of the top 20 firms

Performance of Global Family Businesses (McKinsey)

Lower levels of financial leverage ...

Median debt-to-equity ratio, %



... and a lower cost of debt

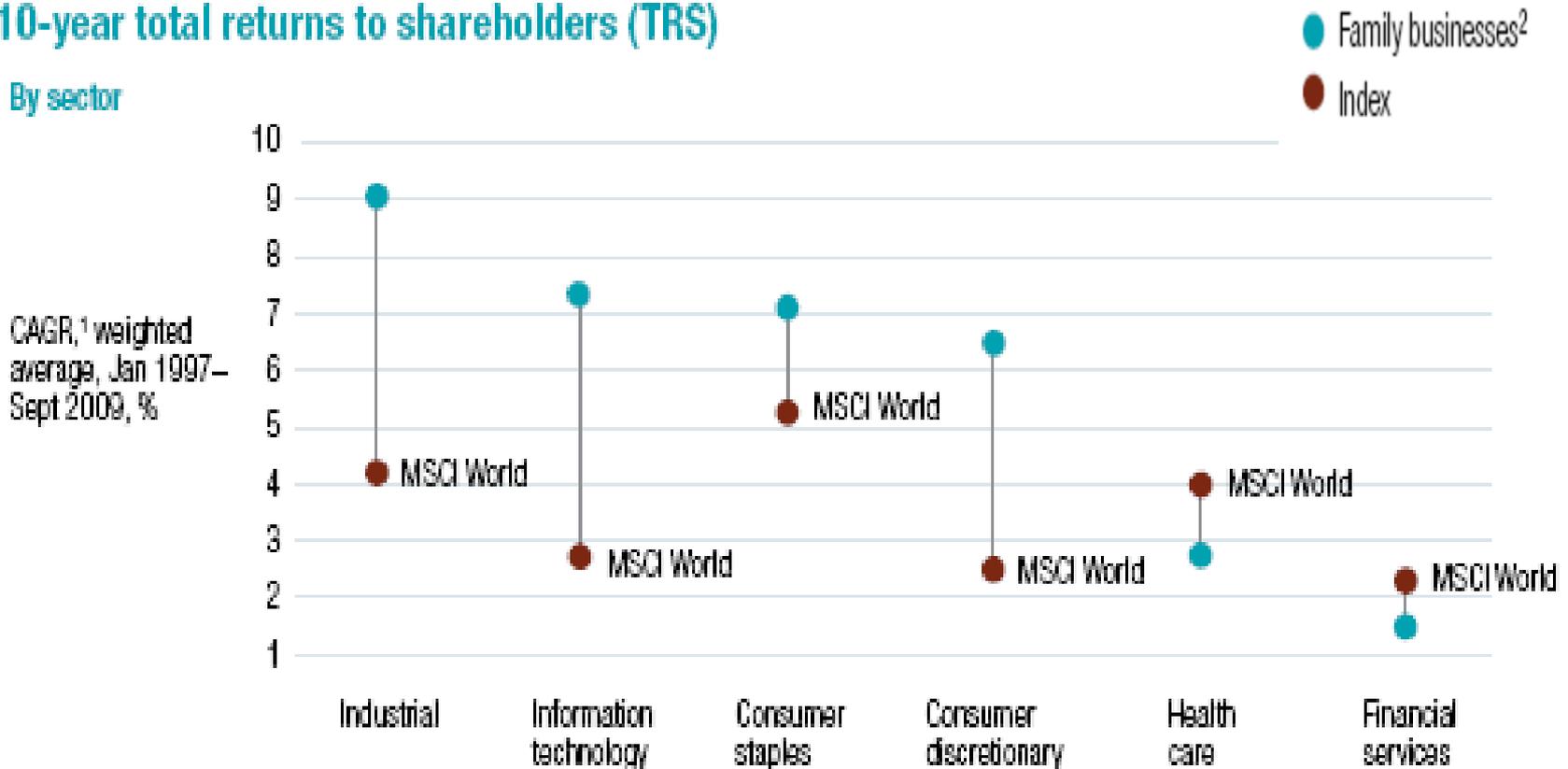
The average yield spread on corporate bonds is 32 basis points lower for family-owned businesses³

Performance of Global Family Businesses II (McKinsey)

Healthy returns over time

10-year total returns to shareholders (TRS)

By sector



Family Business - Strengths

They outperform non-family owned companies in sales, profit, and other growth measures.

Thomson Financial study compared family firms to rivals on the six major indexes in Europe and showed that family companies outperformed their rivals on all of these indexes (2003).

Strengths:

- ✓ **Commitment:**
 - Dedication from family as business owners.
 - Family members willingness to work harder and reinvest profits into the business for long term growth.
- ✓ **Knowledge & Continuity:** Willingness to pass on knowledge and experience to the next generation.
- ✓ **Reliability & Pride:** Family name and pride associated with the business.

Family Business - Weaknesses

Two-thirds to three-quarters collapse or are sold by the founders during their own tenure.

Only 5 to 15 percent continue into the third generation in the hands of the descendents of the founder(s)¹

Weaknesses:

- Informal management structures.
- Ineffective oversight & control mechanisms.
- Non-alignment of incentives among family members/Family Conflicts
- Lack of discipline.

¹Source: Fred Neubauer and Alden G.Lank, *The Family Business: its Governance for Sustainability* (Routledge New York, 1998).

General Challenges to Family Business

Challenges

Access Capital

Diversify wealth

Manage succession

Issues

- ✓ Finance growth
- ✓ Balance debt/equity

- ✓ Manage risk
- ✓ Provide liquidity

- ✓ Appoint competent directors/managers
- ✓ Adjust shareholdings pursuant to inter-generational hand-over
- ✓ Finance share transfers
- ✓ Balance jobs/compensation for family employees with returns to family shareholders

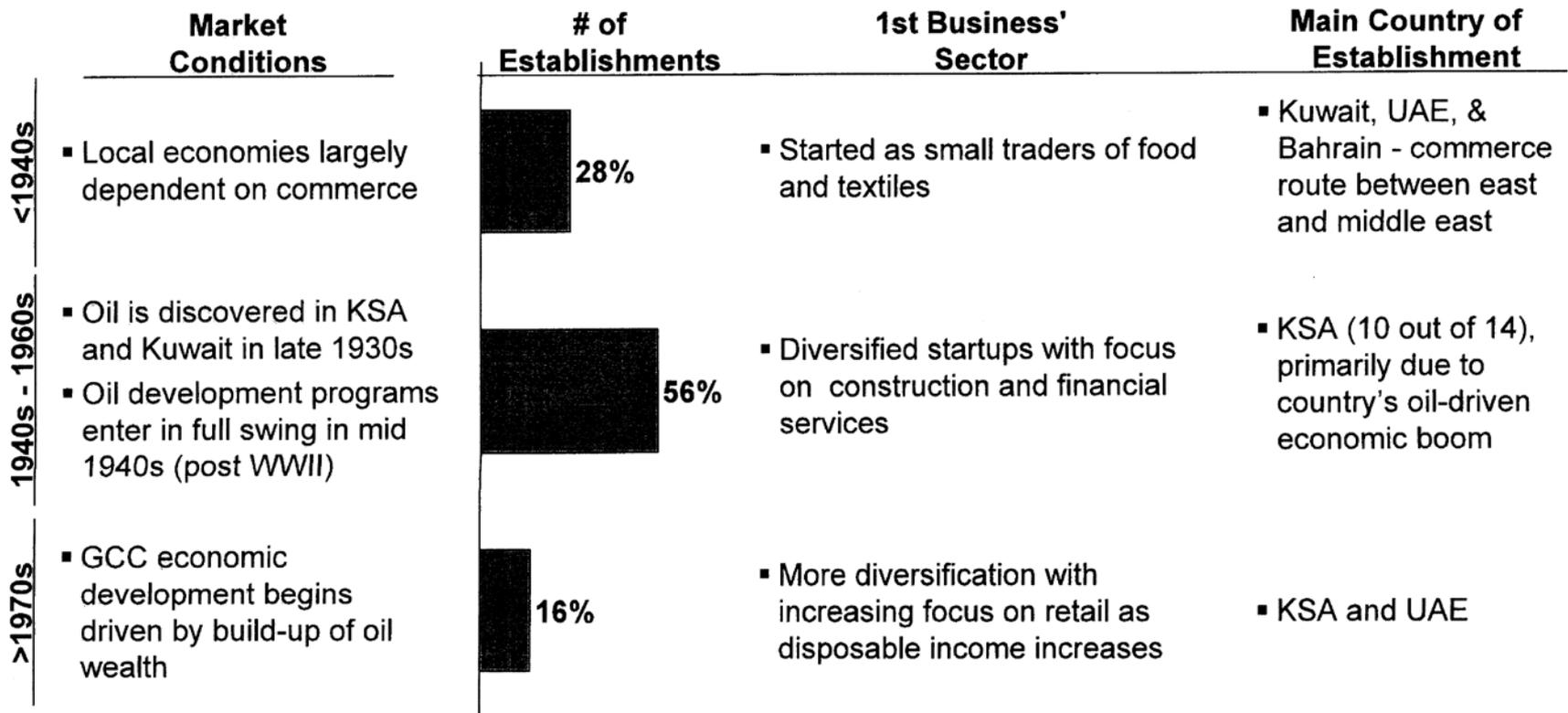
These challenges and issues exist for all closely controlled firms

Family Firms in the GCC

In the GCC, family firms are relatively young...

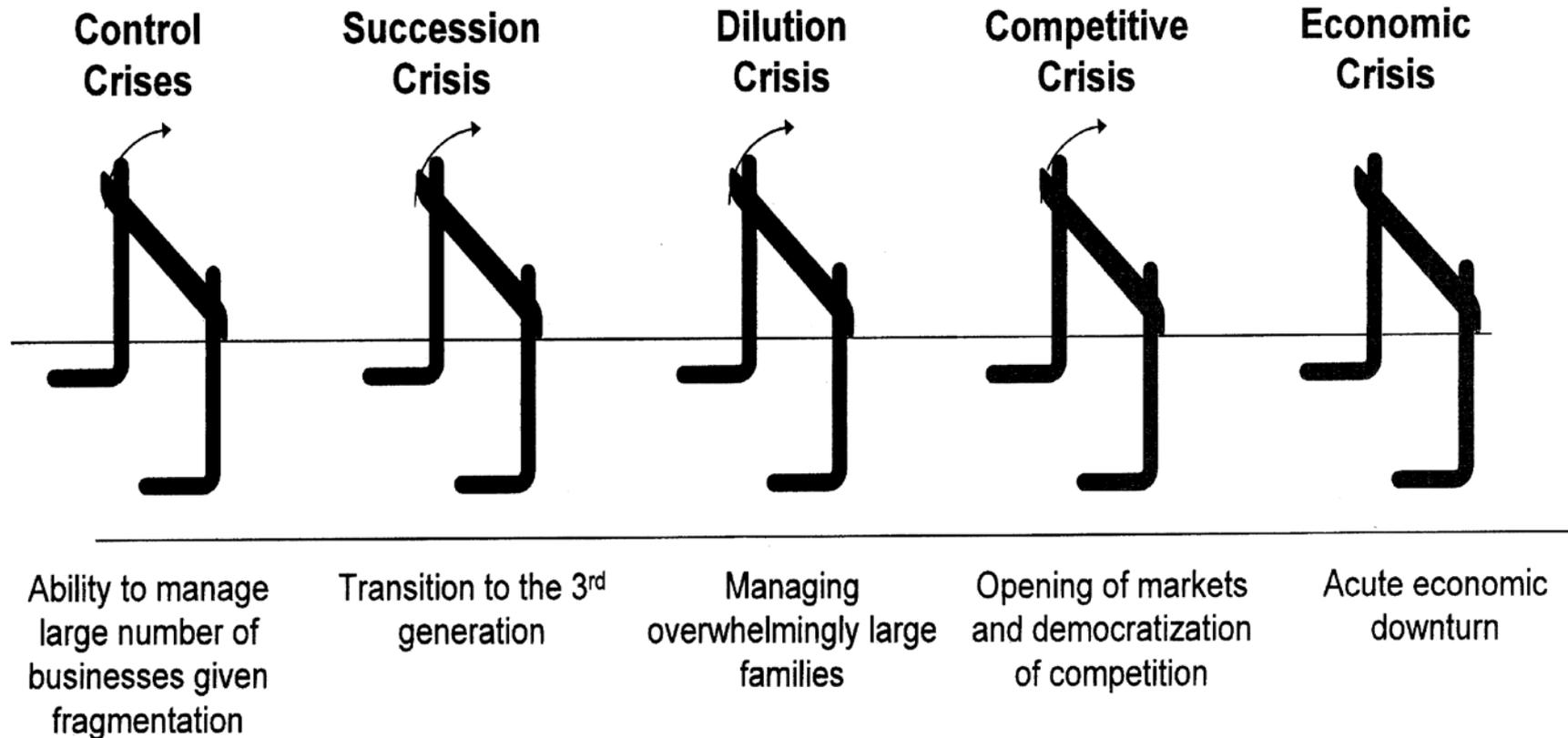
Main Family Business in the GCC⁽¹⁾

- Dates of Establishment and Initial Sectors-



1) Based on a sample of 25 family businesses spanning the GCC
 Source: Literature search and Booz & Company analysis

GCC Family Firms Face Five types of “Crises”



Importance of Corporate Governance

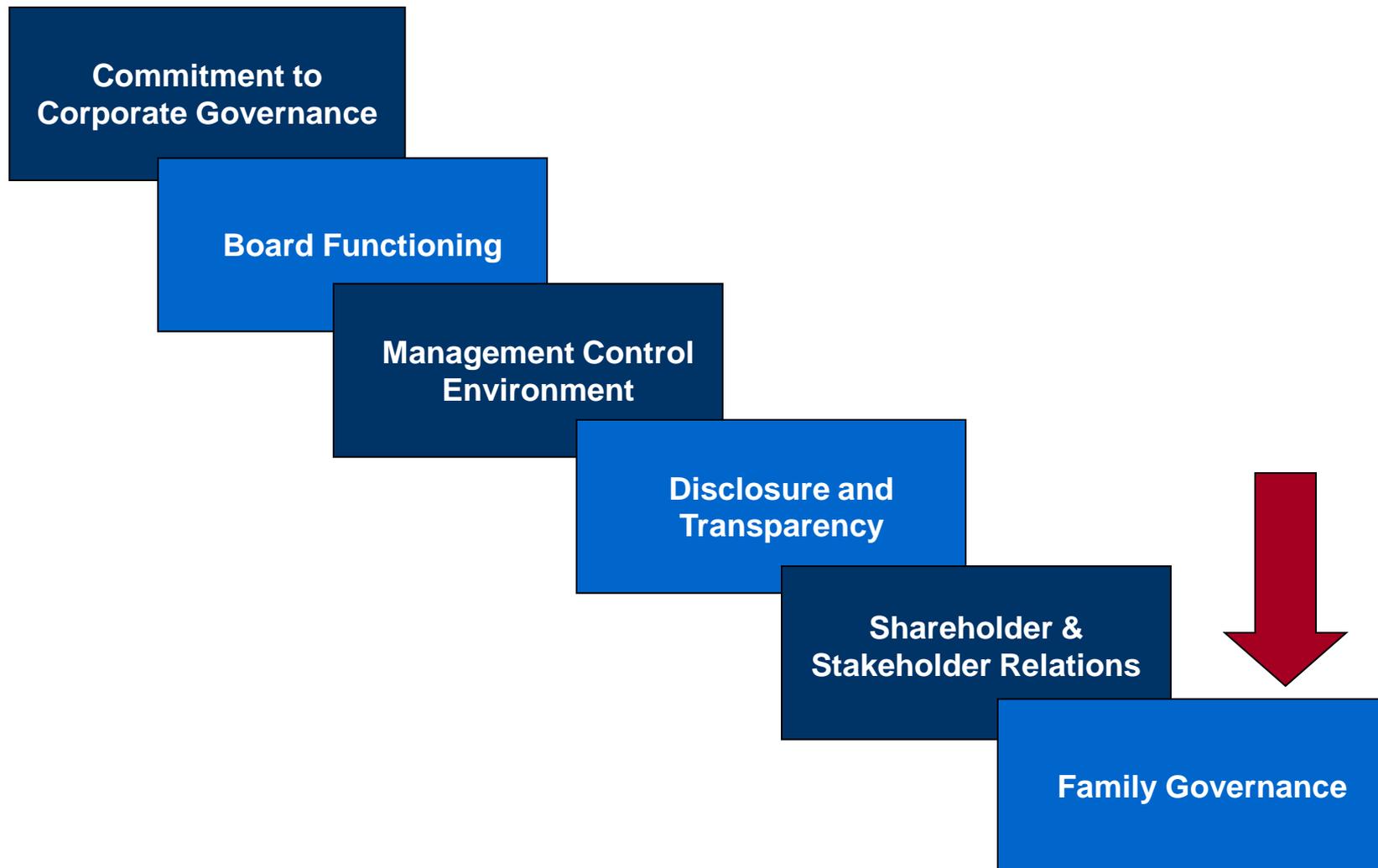
“Good” corporate governance is essential for:

- safeguarding company assets
- maintaining and enhancing investor confidence
- reducing the potential of fraud
- Ensuring sustainability

Companies with “poor” corporate governance

- will find it harder to access external capital
- will face higher financing costs
- will see their credit ratings downgraded
- will have weak investor confidence

Key Dimensions of Corporate Governance



GCC Family Business

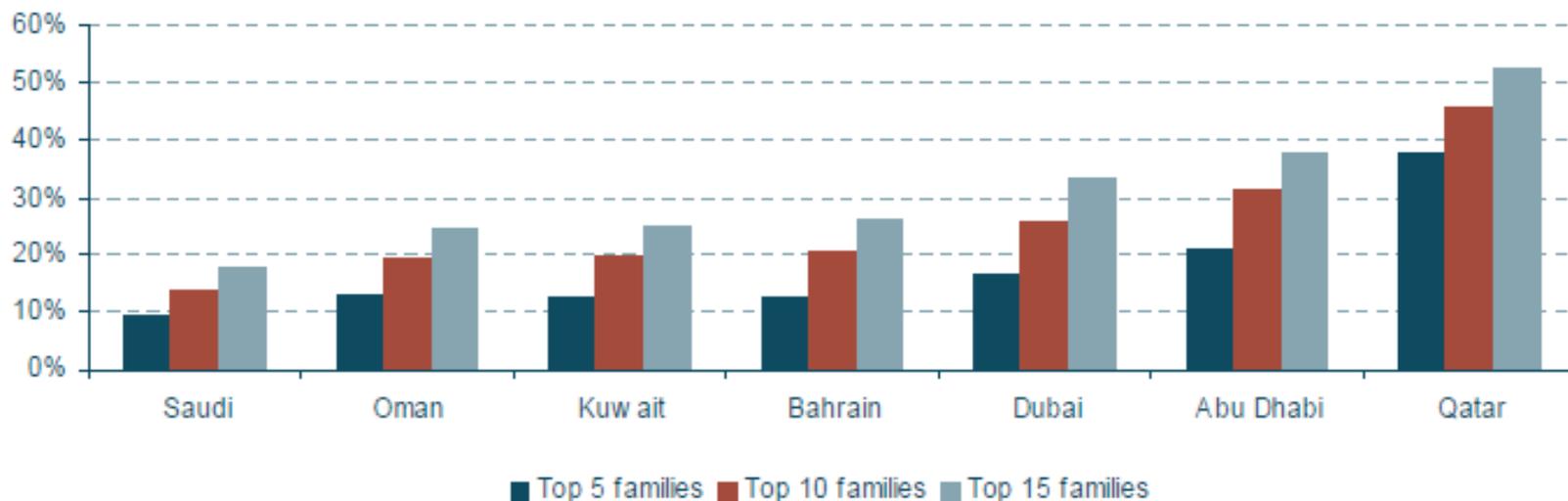
- Within the GCC, **over 90 per cent of all commercial activity** is estimated to be controlled by family firms.
- These firms number **over 5000**, hold combined assets of **more than \$500 billion**, and employ **70 per cent of the workforce**.

Source: Impact of private Equity on GCC Family Business

The Issue: Boards

Family Business Power: Family Rules!

Concentration of family influence - Proportion of total board seats held by most influential families



Sources: Stock market authorities, TNI Investment Research, Company accounts

The region still has ways to go in building more independence in the region's board rooms...

In the UAE listed companies, families are represented on many Boards (257 total seats/37%)

Family name	# of board seats held	% of all board seats	# of seats DFM-listed companies	# of seats ADASM-listed companies
Qassimi	45	6.4%	3	42
Dhahiry	23	3.3%	2	21
Mazrouei	23	3.3%	5	18
Ghurair	16	2.3%	15	1
Suwaidi	15	2.1%	0	15
Shamsi	12	1.7%	1	11
Qubaisi	11	1.6%	0	11
Mansouri	10	1.4%	3	7
Sayegh	9	1.3%	2	7
Muhairi	9	1.3%	0	9
Khoury	8	1.2%	1	7
Yousif	7	1.0%	3	4
Sarri	7	1.0%	5	2
Hosani	6	0.9%	0	6
Badi	6	0.9%	1	5
Essa	6	0.9%	5	1
Jaber	6	0.9%	0	6
Mualla	6	0.9%	0	6
Owais	6	0.9%	4	2
Nahyan	6	0.9%	5	1
Darmaki	5	0.7%	0	5
Lootah	5	0.7%	5	0
Mulla	5	0.7%	5	0
Zaabi	5	0.7%	1	4

Source: ADASM, DFM, TNI Investment Research, Company accounts

Multiple Family Members on the Board of Same Company

Table 10: Multiple family members on the board of the same company

Market	# of companies	0 directors from same family	2 directors from same family	3 directors from same family	4 directors from same family	5 directors from same family
ADSM	59	44.1%	42.4%	11.9%	1.7%	1.7%
DFM	34	58.8%	26.5%	14.7%	0.0%	2.9%
UAE-listed	93	49.5%	36.6%	12.9%	1.1%	2.2%

Table 11: Multiple family members on the board of the same company

Location	# of companies	0 directors from same family	2 directors from same family	3 directors from same family	4 directors from same family	5 directors from same family
Abu Dhabi	29	44.8%	51.7%	3.4%	0.0%	0.0%
Ajman	1	0.0%	100.0%	0.0%	0.0%	0.0%
Dubai	27	55.6%	25.9%	14.8%	0.0%	3.7%
Foreign-based	12	66.7%	33.3%	8.3%	0.0%	0.0%
Fujairah	2	100.0%	0.0%	0.0%	0.0%	0.0%
RAK	11	45.5%	18.2%	27.3%	9.1%	0.0%
Sharjah	9	33.3%	33.3%	22.2%	0.0%	11.1%
Umm Al Qaiwain	2	0.0%	100.0%	50.0%	0.0%	0.0%

National

Emirate by Emirate

Hawkamah – IFC Initiative

- Provide **Corporate Governance Assessments** and **Corporate Governance Advisory Services** for Families in Business and **Families going for IPO.**
- The initiative is being rolled through a **regional road show program** aiming at providing families in business in the region to create and manage a family governance system that will work across generations. The road shows also provides family businesses practical solutions for a range of governance, succession and IPO issues.

Hawkamah Family Business Forum

- Hawkamah, in association with Mudara and Shoora has created a **Family Business Forum** to provide second and third generation members of regional business families with an interactive forum to share, analyse and discuss key business and governance issues affecting their businesses.
- Aim is to promote the long term interests of family businesses in the GCC and MENA regions at family, local, national and regional level
- Seeks to identify challenges faced by the region's family businesses through research, workshops and seminars, and support the development of a regionally-relevant framework to institutionalize families
- Activities will include:
 - Commissioning regionally relevant research
 - Facilitating dialogue among regional families to share and learn from experiences of other markets
 - Housing a library on family business issues.
- The Family Business Forum is a joint initiative between the Hawkamah Institute for Corporate Governance, the Mudara Institute of Directors and SHOORA - Family Business Advisors LLC



Thank You!