Economy Next

Technological and market shifts can wipe out your business model overnight. But in addition to the threats, there are new opportunities—and your next generation may have exactly what's needed to capitalize on them.

BY RICHARD A. MORRIS AND GREG MCCANN

In the past 50 years, many family businesses in a variety of industries have become extinct, or at least endangered species. The odds of a family business lasting three generations have always been long, but the rate of product adoption and obsolescence today makes this dream even less likely. For example, it took 50 years for the telephone and the automobile, introduced in the late 1800s, to gain 50 million users worldwide. Compare that with the cell phone, introduced in 1973, and Skype Internet calling, which debuted in 2003. These technologies took only 11 years and two years, respectively, to gain 50 million users. With few exceptions, product life cycles have been condensed from decades down to years.

How family businesses have changed

Waste management firms, automotive parts businesses, retailers of music and books, and video rental stores were all predominantly family-owned 50 years ago. Today, these industries are dominated by non-family corporations.

In the waste management field, which for more than 100 years consisted primarily of family businesses, the change was a result of industry consolidation. This is not a new phenomenon, but in this case it happened very fast. Waste Management Company was founded in 1968 and became the largest trash service in North America in the 1980s.

A similar consolidation took place among manufacturers, distributors and retailers of automotive replacement parts, starting with the manufacturing area in the 1980s and then spreading to the entire auto industry. By 1998 most of the industry had consolidated. What would be the fate of your business if consolidation occurred even more quickly in your industry?

Family-owned video stores began to disappear within five years after the debut of Blockbuster and similar corporate competitors. But these large competitors didn't last long, either. After just 30 years, the retail video store concept has been eradicated by the confluence of video vending machines, streaming video and discs by mail. Blockbuster declared bankruptcy last year.

The music industry was also affected by consolidation followed by a shift in distribution channels. Family-owned music retailers were run out of business by big-box stores. Then came the Apple iTunes store, which opened in April 2003. Five years later, the iTunes store had surpassed Best Buy and Wal-Mart to become the U.S.'s biggest music seller. The bookselling business changed in a similar way, with superstores replacing independent retailers and then finding themselves displaced by Internet bookseller Amazon. Today, with the advent of e-readers and tablet computers, the industry is changing again.

These are just a few examples that represent a wide range of businesses. Having a large company is no guarantee of survival or success. Only 13% of the companies that were on the *Fortune* 500 list in 1955 remained there in 2010.

In many of these industries, the dramatic shifts weren't caused just by technological advances in product design. Technological innovations also affected production, manufacturing and distribution and, more important, all the companies that support these functions. What will technological progress and new distribution channels do to your business in the next decade—or sooner?

The new normal

Technology isn't the only factor affecting family businesses. Here are some other key trends:

• **Population growth** will slow in this century, and it's possible that population levels may even start to decline. The birth rate is declining in most developed countries, with growth generated through immigration.

• **Real GNP growth** in the U.S. (growth of all sales less inflation) over the past 50 years has been trending downward. Over the past decade, U.S. GNP growth averaged 1.7% per year, compared with an average growth rate of more than 4% per year in the 1960s.

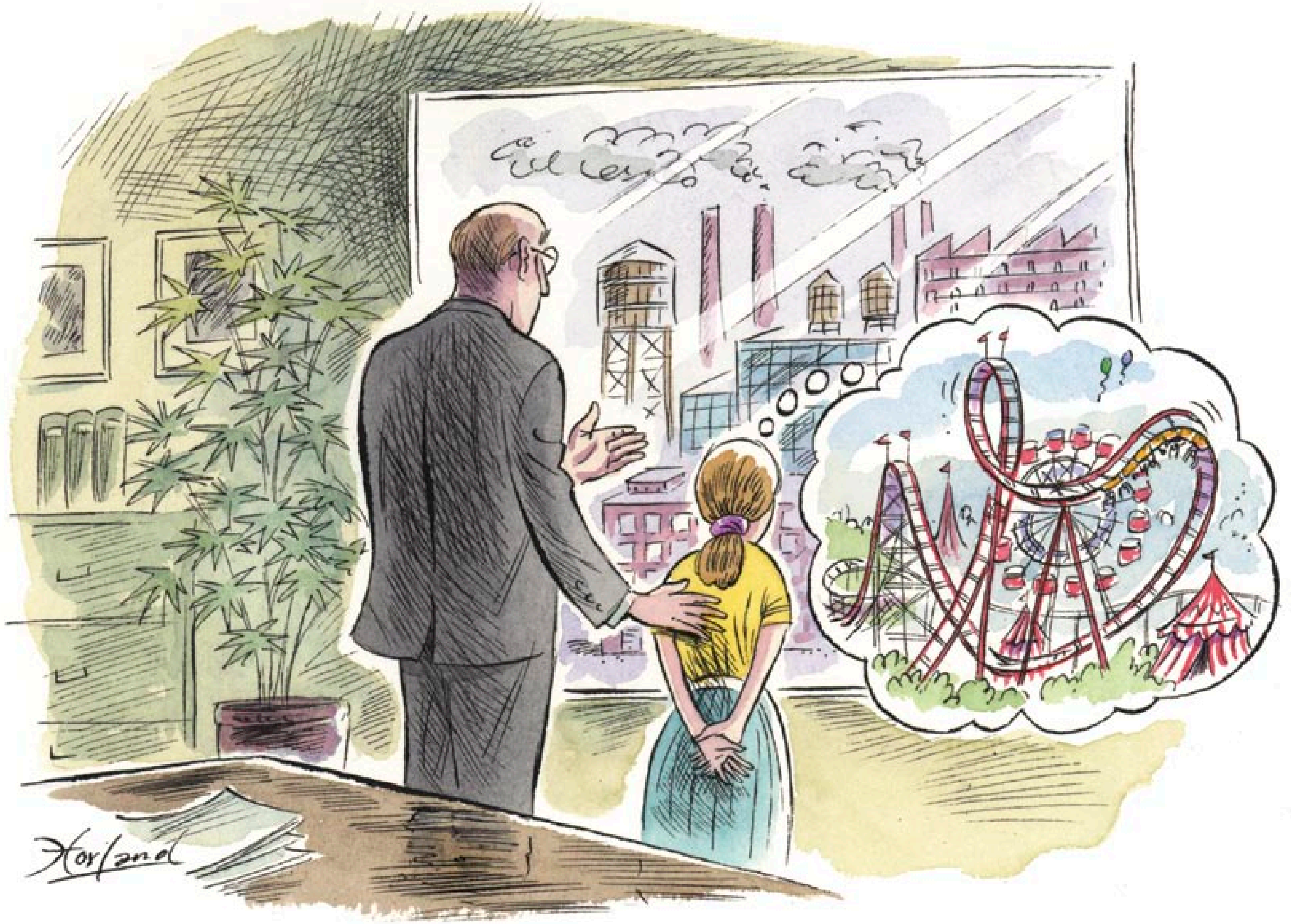
• **Productivity improvements** have exceeded real GNP growth in the past decade, making unemployment a part of our new reality.

These economic themes, fueled by technology, will:

• Increase industry roll-ups.

• Compel businesses to find customers through different and new channels of distribution.

• Force companies to focus on growing market share from current or reinvented products within their industry, or to develop products to take market share from outside



their industry. Total GNP growth in developed countries will likely be reduced to a trickle in the next decade.

Implications for your family business

Reframing our thinking about family business is the place to start. Traditionally, family enterprise has been thought of as three generations operating one business. In today's marketplace, it's wise to think about three business concepts for each generation to come. The Family Firm Institute–Goodman Longevity Study, released last year, suggests that family business leaders, advisers and academics "reframe the dialogue on succession and longevity."

In virtually every culture, there is some variation of the maxim "shirtsleeves to shirtsleeves in three generations," implying that the third generation "kills the business." Indeed, research conducted by Professor John Ward in 1987 found that only 13% of family enterprises are still viable in the third generation. But if a family business doesn't survive, is it the third generation's fault?

In light of the structural economic changes noted above, is it wise to continue down your current business path?

Opportunities in Economy Next

In an ever-shifting economic climate, no business model should be considered permanent. The business leaders of today are likely ill-equipped to train the leaders of tomorrow. Here are four areas where rethinking is warranted:

1. Reframe innovation as a necessity.

Reinvent the business to fit the new economy. In the examples described above, the emerging businesses took advantage of new economic themes. Don't focus narrowly on reinventing your product (i.e., incremental innovation). You must redefine your entire business model (i.e., breakthrough innovation) to better serve the needs of your current customers—and the customers of the future.

Go global: Family companies tend to think of themselves as tied to the community where they're based. But according to the U.S. Small Business Administration website, more than 90% of U.S. businesses that export are small businesses. Is your family business interacting internationally?

Incorporate technology: Even if your business is not a technology company, you are not immune to the realities of the information age. Can technology help you improve the way your product or service is promoted, the way you communicate with customers or your distribution channels? Your next-generation members may be best equipped to help you make the shift effectively and creatively.

Look outside your industry: Companies in other industries might have business models that could be adapted to fit

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your situation. If your firm can't grow organically or acquire new businesses, you will need to find an innovative way to truly differentiate your offerings.

2. Reframe your view of the competition.

When a market shifts and new distribution systems become dominant, a business that was your longtime rival can become a key ally, actually helping your company to stay relevant and independent.

Adam Schwartz, vice president of public affairs and member services at the National Cooperative Business Association, can cite hundreds of industries where competitors have joined forces under a cooperative structure to make each party a stronger individual business. "True Value Hardware is an example in which individual owners have joined a cooperative that affords them the buying power of their big-box competitors, such as Home Depot," Schwartz says. "They also save money on cooperative marketing and distribution, and share best practices." Without the cooperative, he notes, these local family hardware stores —formerly each other's competitors—would not be able to compete effectively against the big-box stores.

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Ask yourself if there is a way for your company to reinvent how you do business by working cooperatively with other businesses—even competitors.

3. Reframe how you cultivate the next generation.

The next generation has always been the engine that either maintains or kills the business. Rather than "grooming" your Generation Next, think about forming a true partnership with them. Identify what each generation can offer the other.

• The senior generation offers business knowledge, a long-term perspective and control of the current business and its cash flow.

• Generation Next is living the future now and can be a great source of ideas and market research. They offer passion and dreams, and a perspective on what is needed to perpetuate the business. They may be far more comfortable with exponential change than the more senior generations.

Consider the following as you work with Generation Next:

• It's important to instill a sense of entrepreneurship. Passive invested wealth is generally not sustainable.

• Encourage the next generation to be independent and free from a sense of entitlement. Stress the idea of establishing credibility and marketability.

• Inculcate a sense of stewardship. The family's capital should be viewed as an investment that can be redeployed —it isn't there just to provide for today's family and business needs.

4. Reframe your definition of successful business succession.

Imagine a family business whose founders, from the outset, proclaimed that the *enterprise* might not be passed on to the next generation. Instead, they would focus on passing on the *capital* that resulted from the enterprise. There are several different types of capital:

• **Values capital:** Your family's values system, including how business should be conducted; how you treat family, employees and vendors; and your contributions to the community and charitable causes.

• **Knowledge capital:** The business experience gained in running the enterprise.

• **Professional capital:** The professional team of company managers, board members and trusted advisers. The recognition that the current business, and any others in which the family might invest in the future, require a professional structure.

• **Financial capital:** The family's financial assets, which may include cash, stock in the current business and other holdings.

• **Family capital:** Each family member's abilities and dreams for a happy life. Many founders convey to their children—overtly or by implication—the hope that they will take over the business. What if there were a new family business model—one that supported family members' career dreams instead of the legacy business? What if the next generation's career dreams *became* the new family business?

Long-term thinking

When assessing future possibilities, try not to think of your business as a set-in-stone entity. It might even be wise to consider selling the business and putting the assets into a family office until your family identifies its next venture.

In today's world, an enterprising family must proactively prepare for rapid change. The concept of "transition" must go beyond the shift from generation to generation; it must also incorporate the notion of an evolution from one business concept to the next. FB

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