

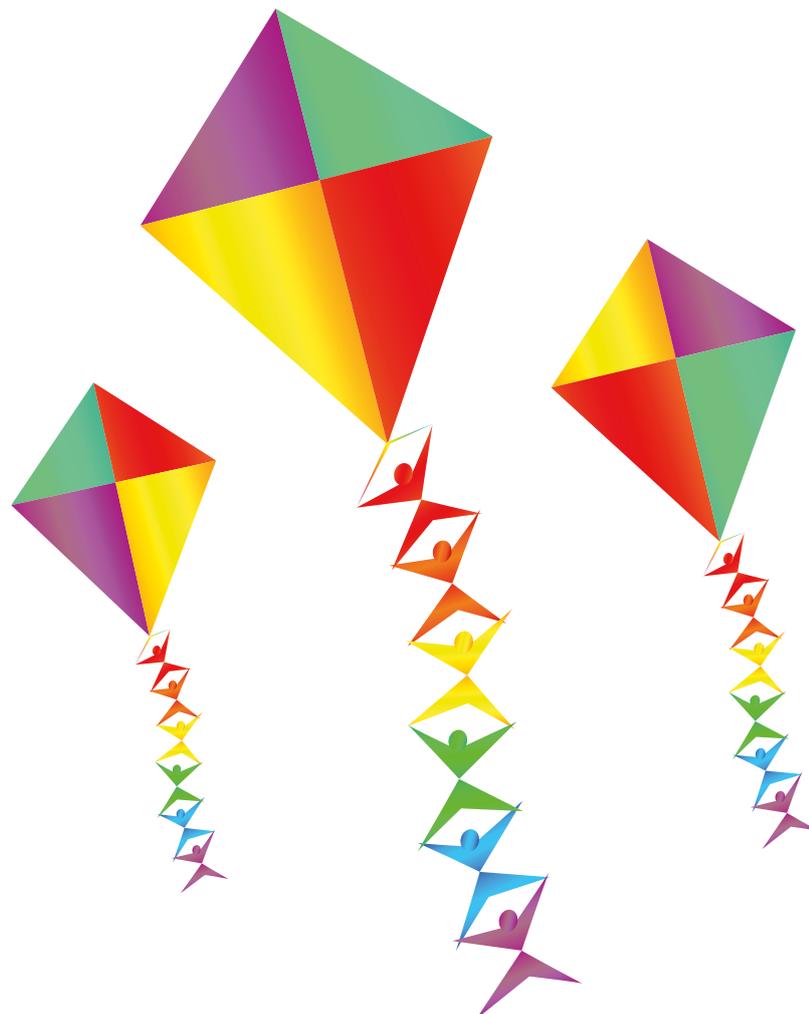


Institute for
Family Business

Family Business Entrepreneurship

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An IFB Research Foundation Report

Foreword



The purpose of this report, commissioned by the IFB Research Foundation, is to increase understanding of the depth and nature of family business entrepreneurship. The study also highlights good practices that will help family firms to continue to innovate and to ensure their business constantly adapts to changing market needs.

The report shows that high entrepreneurial orientation improves financial performance. The family, its history and its own collective mindset can have a strong influence on the management team and the interrelationship is important in determining the company's ability to ensure a sustainable future. From a personal point of view it is also encouraging to see that the report finds that a family CEO can be beneficial for stimulating innovation in a business, when balanced with good governance including non-family directors.

In order to carry out the study, the Foundation commissioned a team of experts from three of the UK's leading business schools – Imperial College Business School, Durham University Business School and Lancaster University Management School. The authors find that family firms report a strong orientation towards creativity and experimenting with new products, services and processes. Another key insight is that the family's involvement in entrepreneurship and innovation is a positive factor and helps to support risk-taking.

All businesses, family or non-family owned, are buffeted on a daily basis by changes in markets and the shifting needs of customers. This IFB Research Foundation report offers readers valuable insights into strategies that will help to ensure that family businesses maintain a strong culture of entrepreneurship and innovation, driving success across generations.

I hope that you enjoy the read and find the outcomes useful in developing your business.

Sir Michael Bibby

Chairman, IFB Research Foundation



**Research
Foundation**

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Executive summary

This report sets out the findings and recommendations from new research into the entrepreneurial orientation of private family firms in the UK, the drivers of this orientation, and the impact this has on innovation activity and financial performance. The project has been funded by the IFB Research Foundation and conducted by researchers from three UK business schools – Imperial College Business School, Durham University Business School and Lancaster University Management School.

The project findings draw upon the first large-scale survey of UK family companies to examine their entrepreneurial orientation, innovation and performance. The study questionnaire was sent to 2,854 family firms sourced from the FAME database and the IFB membership, and there was an excellent 12 per cent response rate.

Key findings and recommendations

The study findings offer important insights into the active role of families in directing the entrepreneurial orientation of family firms and point to important factors that can help to increase the entrepreneurial orientation of these firms. The research ultimately indicates that family businesses must carefully align their goals, structure and governance to support entrepreneurship and innovation. They must also consider the involvement of non-family directors and employees, and think about how next-generation family members can drive innovation.

Summarising the study findings, to achieve higher performance through entrepreneurial orientation family businesses need to:

- **Align the entrepreneurial orientation of the firm with the entrepreneurship of the family.** The family firm is unique because it has two entrepreneurial orientations – that of the family and that of the firm. Families have a separate family entrepreneurial orientation distinct from their firm’s entrepreneurial orientation. Importantly, the family entrepreneurial orientation supports that of the firm. Family firms report a strong orientation towards creativity and experimenting with new ideas for products, services and processes, thereby initiating changes to which competitors react. But at the same time, they are less likely to engage in high-risk projects despite the prospect of high return. Firm entrepreneurial orientation is only slightly higher than family entrepreneurial orientation for creativity, initiating changes and the tendency towards taking high risk. But family entrepreneurial orientation supports the entrepreneurship of the firm with a high willingness to change and an above-average keenness to create new business because it has the success of future generations in mind. So involving the family to ensure that entrepreneurship and innovation are at the heart of the family business is crucial.
- **Involve the next generation to increase entrepreneurship and innovation.** Over 60 per cent of family firms want their next CEO to be a family member but the next generation is rarely involved in strategic decision-making and strategic activities of the firm, such as innovation and entrepreneurship.

- **Involve non-family employees to increase entrepreneurship and innovation.** While families commonly dominate and strictly manage key strategic decisions, they also allow greater autonomy and flexibility to non-family managers and employees on less strategic matters. This should be extended to entrepreneurship and innovation.

- **Prioritise non-family-centred goals to become more entrepreneurial.** Family businesses should increase the number of innovation goals and the diversity of these goals. Despite their entrepreneurial orientation, family businesses surveyed tend to adopt an incremental approach to innovation. Most innovation activity is oriented toward improving existing products, particularly quality, as well as opening new markets and extending the range of products offered. Entering new technological fields is not a high priority of innovation in UK family firms. This risks stagnation of the business in the face of more aggressive competition.

- **Put entrepreneurship and innovation front and centre.** New products account for more than 10 per cent of sales in the majority of our sample of family businesses, and only 7 per cent do not obtain any significant sales benefit from innovation. Family firms should examine opportunities for securing competitive advantage through registering patents.

- **Reshape the board of directors to have more non-family members.** Diversity of board membership is important in sparking entrepreneurship and innovation. For family businesses, the traditional control role of the board of directors is less important than strategy initiation. Family firm boards should capitalise on their lower need to monitor managers, and should assist managers to develop effective strategic plans for entrepreneurship and innovation.

- **Retain a family CEO in order to become more entrepreneurial.** Some 85 per cent of family firms are open to appointing a non-family CEO in the future but this could undermine family business entrepreneurship. When the CEO of the firm is a family member, family-level entrepreneurial orientation is significantly greater and this is positively associated with firm performance.

- **Involve women on the board to increase profitability.** The presence rather than the number of females on a board is associated with a higher profit margin. Promoting board gender diversity can support increased entrepreneurship and innovation.

- **Consider establishing an operations board in addition to the main board of directors.** Only around a third (36 per cent) of family firms have operations boards and only a small proportion of these (19 per cent of the 36 per cent) specifically discuss innovation on their agenda. This is a wasted opportunity because operations boards are important in developing innovative new products and improving existing products.

1 Introduction

Previous studies on family firms have looked in particular at performance (usually versus non-family firms or the performance of publicly listed versus private family firms) and at inter-generational succession, but few have examined entrepreneurship and innovation in family firms. Understanding entrepreneurship and innovation in the context of family business is highly relevant from a practical point of view because there is a growing body of evidence showing that family firms use entrepreneurship and innovation to nurture their competitive advantage and to overcome economic and financial downturns. Research indicates that entrepreneurial and innovative companies typically outperform their competitors and innovation is widely acknowledged as an important determinant of sustained superior performance. Thus many family firms are gaining from their entrepreneurial orientation.

This study begins to address this gap in our knowledge of family firms, aiming to assess the entrepreneurial orientation of private family firms in the UK, the drivers of this orientation, and the impact this has on innovation activity and financial performance.

In order to do this the researchers asked a random selection of 338 family firms from 17 industrial sectors in the UK questions on their family involvement, governance, entrepreneurial orientation, innovation, the family's influence on the firm and the firm's goals. Face-to-face interviews were also conducted with five family firms in order to provide on-the-ground insights into the drivers and processes of entrepreneurial and innovative activity.¹ The responses from the sample are presented in this report.

Entrepreneurial orientation and the family firm

Entrepreneurship and the firm

The entrepreneurship of any business depends on its senior managers. The entrepreneurial orientation (EO) of a firm is defined by “the methods, practices, and decision-making styles *managers use* to act entrepreneurially”.² A combination of behaviours contribute to a company becoming more entrepreneurial.³ Senior managers have to practise innovativeness, proactiveness and risk-taking. Innovativeness is an emphasis on idea generation and novelty; proactiveness is a “hands-on mentality” in which the firm takes the initiative and tries to beat competitors to the punch; and risk-taking is tolerating and being willing to commit the resources of the firm to projects that have an uncertain outcome, but a potentially high reward. Crucially, EO comes from the idea that, over time, firms become reflections of their senior or owner-managers.⁴

1. Further details on the methodology employed in this study and supplementary data tables are set out in Wright et al. (2016).

2. Lumpkin and Dess (1996).

3. Zellweger, Nason and Nordqvist (2011).

4. Covin and Miller (2014).

Firm entrepreneurship is an antidote to the paralysis of inertia and “business-as-usual”. Without it, companies are destined for mediocrity. Entrepreneurial orientation is particularly important when a firm operates in a so-called high-velocity environment, where changes happens regularly and competitors are fierce in chasing customers whose needs and wants often change.

It is not just the firm that can have an entrepreneurial orientation. So can the family, through its own wider attitude to entrepreneurship.

Entrepreneurship and the family

In family firms, the family has its own view of entrepreneurship, forged by the entrepreneurial mindset, attitudes and goals of the family. This has been termed “family entrepreneurial orientation”.⁵ The attitudes, mindsets and goals of family members shape the wider governance of the firm,⁶ which in turn shapes its willingness and ability to engage in entrepreneurship and innovation activity, and how it views, prioritises or constrains these activities. “Firm EO” and “Family EO” have the potential to spark entrepreneurship and innovation, as shown in Figure 1.

- **Firm EO** concerns behaviours of the firm itself and how risk-taking, innovativeness and proactiveness are present in strategic decisions, the management of resource availability and how the firm is developed over time.
- **Family EO** concerns family behaviours geared towards expressing the wider attitudes and mindset of the family. These typically include its own view of risk-taking, innovativeness and proactiveness, but also focus on security and control (of family assets), stability (versus growth and a willingness to change) and long-term view (stewardship of the firm for the long term and being conscious about the next generation).

Figure 1: Firm and family entrepreneurial orientation



5. Zellweger, Nason and Nordqvist (2011).

6. Kotlar and De Massis (2013).

While Firm EO and Family EO *embed* a mindset towards entrepreneurship and innovation into the firm, the extent to which entrepreneurship and innovation is *enabled* relies on how the family owners exercise their decision-making authority and their commitment towards entrepreneurship and innovation goals.

Family owners' decision-making authority and commitment

Family owners' decision-making authority and commitment potentially play important roles in a family firm's innovative activities.⁷ Decision-making authority refers to the family owners' power to direct, allocate or dispose of a firm's resources. It includes discretion in selecting the goals of the organisation and in choosing from among a range of feasible strategic, structural and tactical options. Commitment concerns the disposition of the family owners to engage in distinctive entrepreneurial and innovative behaviour based on the goals, intentions and motivations that drive these owners to influence the firm's behaviour in directions diverging from those of non-family firms.⁸ For example, family owners may gain non-financial returns – or what is termed “socioemotional wealth”⁹ – through their ownership and involvement in a firm, and the extent to which such benefits influence their decisions is a cause of some of the differences between family and non-family firms.

Enabling entrepreneurship and innovation to happen can lead to several performance outcomes including increased financial performance, radical (radically new products, processes and markets) and incremental forms of innovation, all fuelled by a continuous pursuit of new opportunities. Entrepreneurship and innovation can then create risks that the family firm must evaluate and manage through effective governance.

The family firm and governance

The governance of a family business defines how power and decision-making authority are distributed among family members, which will have important implications for the family firm's entrepreneurial orientation. The focus here is on two main elements of governance, namely boards (the board of directors and the operations board) and trustees.

The effect of a “professional” board might be quite different compared with a “family” board. A family board will be made up of mainly family members but a professional board will be more likely to have outsider representation in the form of non-executive directors and possibly a non-family CEO. Outsiders can have quite different mindsets and can bring in new ideas, skills and capabilities required to increase entrepreneurship. Similarly, women on the board will have a different mindset and may help to deal with disagreements and friction. Having a diverse board should have a positive effect on the entrepreneurial orientation of family firms. Operations boards (also termed management boards) can provide a venue for discussing operational aspects of the business, generally not debated in detail at main board level. An operations board can then be a productive way to foster entrepreneurship in these businesses, especially if innovation is specifically on the agenda at these boards.

7. Chrisman et al. (2015).

8. De Massis, Di Minin and Frattini (2015).

9. Gomez-Mejia et al. (2007).

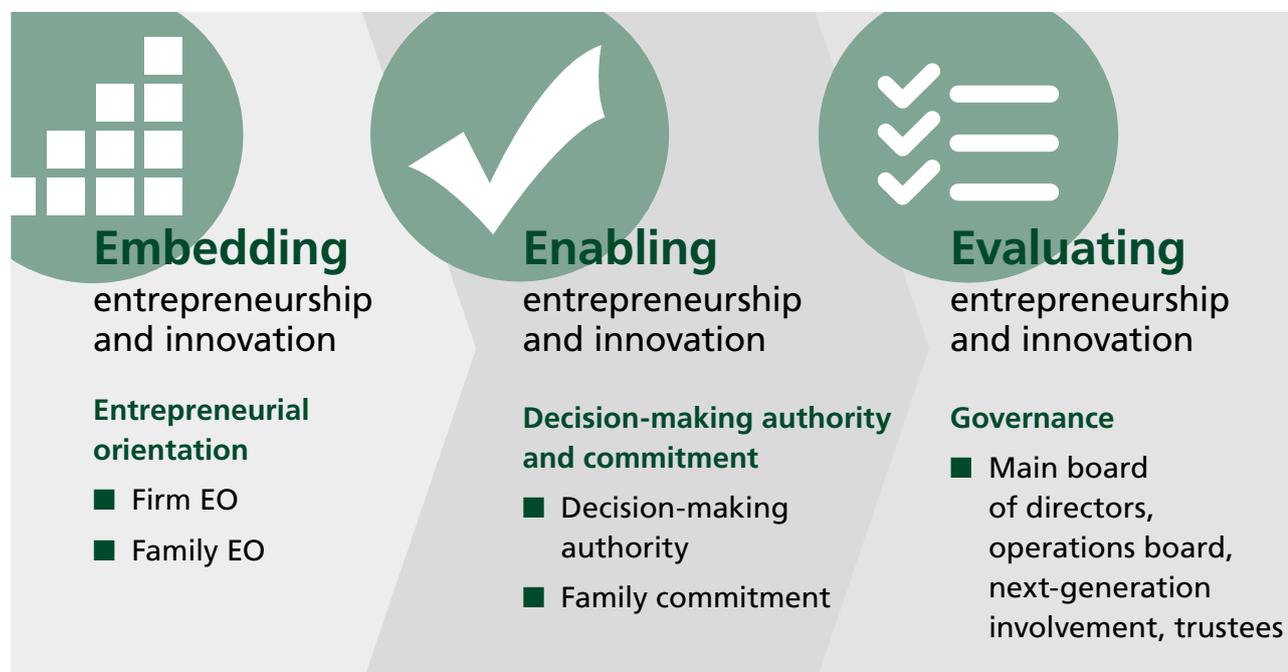
The setting up of a family firm trust is also an important aspect of governance. Trustees might simply be acting on behalf of their beneficiaries, or they might become more involved in the business through the board of directors or other avenues. If trustees become more involved they could be classed as “quasi directors” with influence at board level^{10,11} and they could have a bearing on the entrepreneurial orientation of the firm.

Embedding, enabling and evaluating entrepreneurship and innovation

Building a culture of entrepreneurship and innovation in the family firm relies on three core practices – embedding, enabling and evaluating (see Figure 2). These three concepts provide a framework for understanding entrepreneurship and innovation in family firms:

- **Embedding concerns how entrepreneurship and innovation activities are established in family businesses.** Entrepreneurship and innovation within the family firm depend on the extent to which Firm EO and Family EO are present. The entrepreneurship of the family business is established by increasing risk tolerance, innovativeness and proactiveness at the firm level. This entrepreneurship is also established through risk tolerance, innovativeness, proactiveness, a transgenerational outlook, emphasis on growth and a willingness to change at the family level. While these *embed* a pro-entrepreneurship and pro-innovation mindset in the family, they are not enough to enable entrepreneurship and innovation activities to take hold in the family firm.

Figure 2: Building a culture of entrepreneurship and innovation in the family firm



10. “[as a trustee] my job is to hold the shares for the benefit of the family and leave the running of the company to the board. But the fact is that if I am a trustee, I am acting for the benefit of the beneficiaries, so I have to have some sort of understanding of that business, how it works. Trustees are absolutely key ... can have a huge impact ... can control the board.” Helen Tavroges, Partner at Bond Dickinson, interviewed during the course of this study.

11. Scholes and Wilson (2014).

- **Enabling concerns the ways in which family businesses encourage entrepreneurship and innovation to take place.** Entrepreneurship and innovation depend on how the family's decision-making authority influences business decisions (and whether others outside the family management team have the authority to act and take decisions), and the family's commitment to engage in entrepreneurship and innovation based on the goals, intentions and motivations that drive family owners. These factors *enable* entrepreneurship and innovation to take place in the family firm. However, entrepreneurship and innovation activity creates risks that must be evaluated and managed.

- **Evaluating concerns the governance mechanisms that family businesses develop to address the risks associated with entrepreneurship and innovation.** The governance of family firms is complex and includes aspects such as the role of the main board of directors, the role of operations boards, whether the next generation is involved in running the business and whether the family has set up a trust to manage the family's wealth and interests as part of the business. Inappropriate governance mechanisms can dampen risk-taking, placing a stranglehold on entrepreneurship and innovation; getting this right should lead to improved family firm performance through entrepreneurship and innovation.

Based on this framework, the study findings discussed in this report address the following four questions:

1. **Embedding entrepreneurship and innovation:** What is the nature of entrepreneurial orientation in family businesses?¹²
2. **Enabling entrepreneurship and innovation:** How does family firms' decision-making authority and commitment influence innovation and business performance?¹³
3. **Evaluating and managing the risks of entrepreneurship and innovation:** What is the effect of boards of directors and boards of trustees on the entrepreneurial orientation and business performance of family firms?¹⁴
4. **The performance outcomes of entrepreneurship and innovation:** Does entrepreneurial orientation at both the business and the family level influence business performance?

12. Established measures of EO are used, based on Zellweger, Nason and Nordqvist (2011).

13. The measures used are based on De Massis, Kotlar, Chua and Chrisman (2014).

14. New measures are used to assess the effect of boards and trusts.

2 Embedding entrepreneurship and innovation

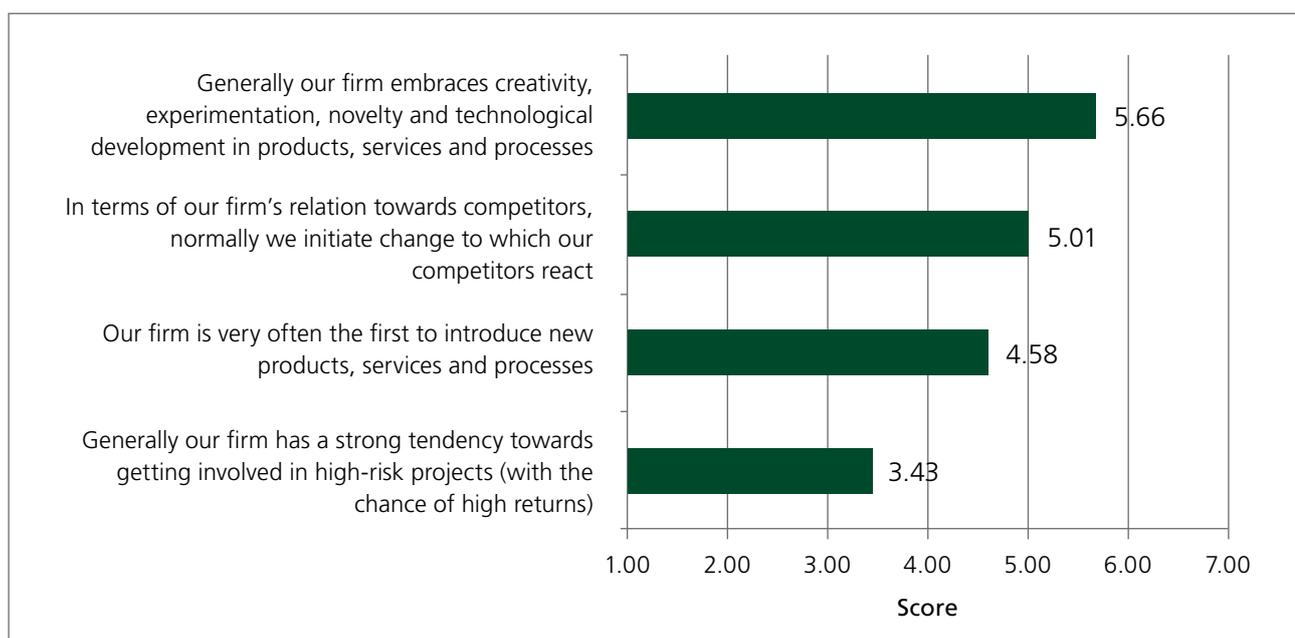
Embedding concerns how entrepreneurship and innovation strategies are formulated and established in family businesses.

Entrepreneurial orientation and the objectives of the firm

How entrepreneurship is approached by the firm and by the family are distinguished in this report as two different but related forms of entrepreneurial orientation (EO). How the firm behaves is defined by its senior managers, but the family, its history and its own collective mindset can also have a strong influence on firm behaviour. The family businesses surveyed in this research have various dimensions to their EO.

At the firm level the results suggest that the family companies in the research sample embrace creativity and experimentation and see themselves as change initiators relative to their competition. They have a more balanced approach to introducing new products, services and processes. Finally, they have a much lower tendency to engage in high-risk projects with the prospect of high return (see Figure 3). The example of HMG Paints (see Case study 1) demonstrates the desire to minimise risk through the use of ring-fencing of finance for new initiatives, while the case of Howarth Timber (Case study 2) illustrates how some companies adapt to competitors' moves. HMG Paints competes mostly through moderate product and process innovation in the specialty paints segment of the market, in the face of low-cost foreign producers who have squeezed out domestic volume producers. Howarth Timber has adopted a follower innovation strategy involving reverse engineering – the extraction of knowledge, technology or design information from competitors' products, processes and services – and enhancing what competitors are doing.

Figure 3: Firm-level entrepreneurial orientation

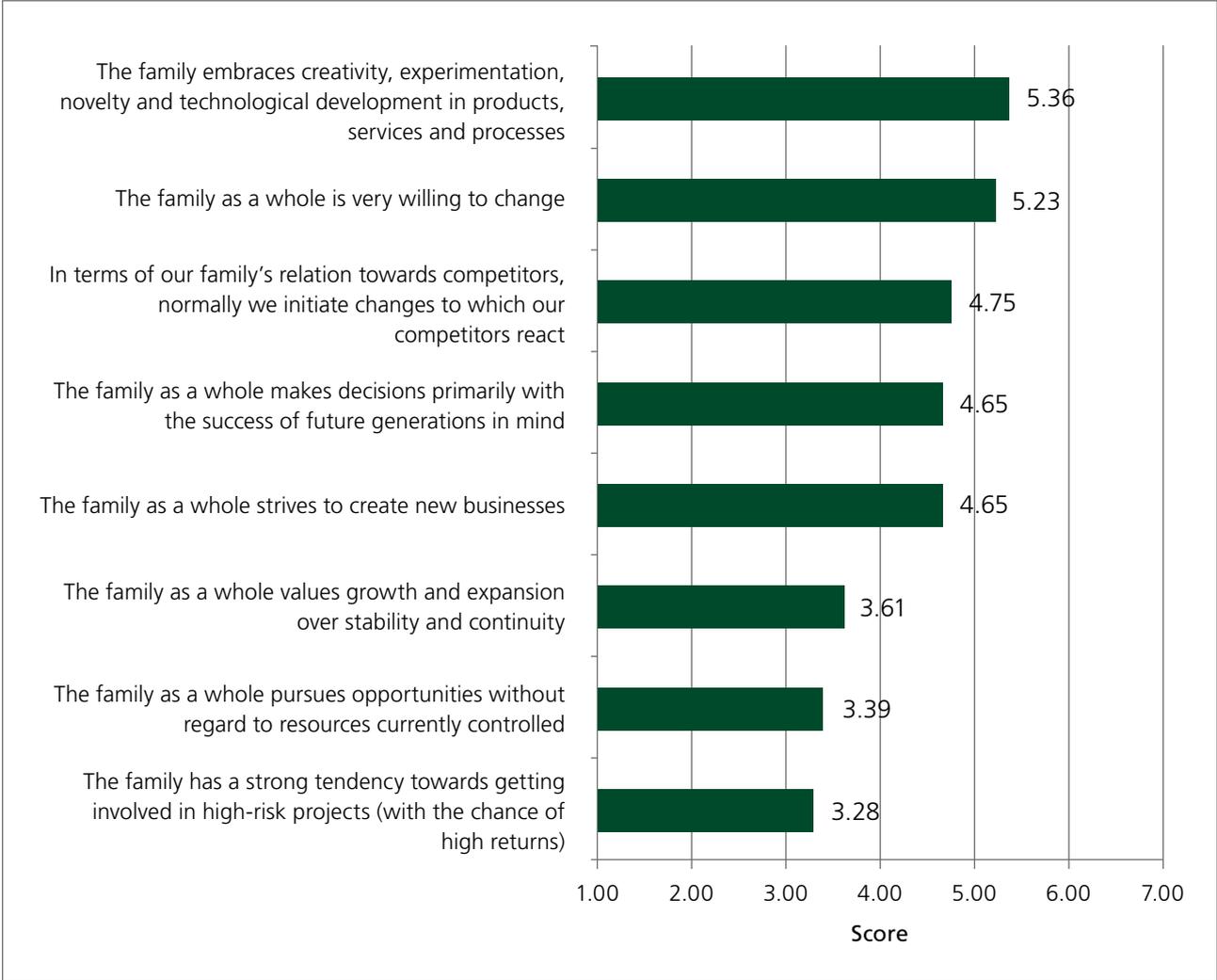


Scoring: 1 = fully disagree to 7 = fully agree.

At the family level, a slightly different approach to entrepreneurship is indicated, but one that appears to be complementary to the firm EO. In particular, families embrace creativity and experimentation, and are very willing to change; they also tend to initiate change to which competitors react. They have a low propensity towards risk (see Figure 4). Families also engage actively in creating new businesses, and also have in mind the importance of entrepreneurship decisions for the success of future generations. However, the entrepreneurial actions of the family are not always oriented towards growing the existing businesses. Rather, most family firms display a particular attention toward sustainability, so that entrepreneurship is seen as a means to ensure stability and continuity for the business. For example, HMG Paints adopts a conservative approach to entrepreneurship by developing organically within the core business and ring-fencing riskier innovations that could be big if they are successful. In the case of Howarth Timber, the company did not engage in innovation for many years but has come to recognise the importance of innovation for sustaining the business. Oversight mechanisms are in place to ensure that innovations do not put pressure on their conservative approach to financing.

EO is displayed by the research sample of family firms at the firm and family levels, but how it is then reflected in the innovation objectives, activities and outputs of these businesses is mixed. As shown in Figure 5, most innovation activity is oriented towards improving existing products, particularly quality

Figure 4: Family-level entrepreneurial orientation



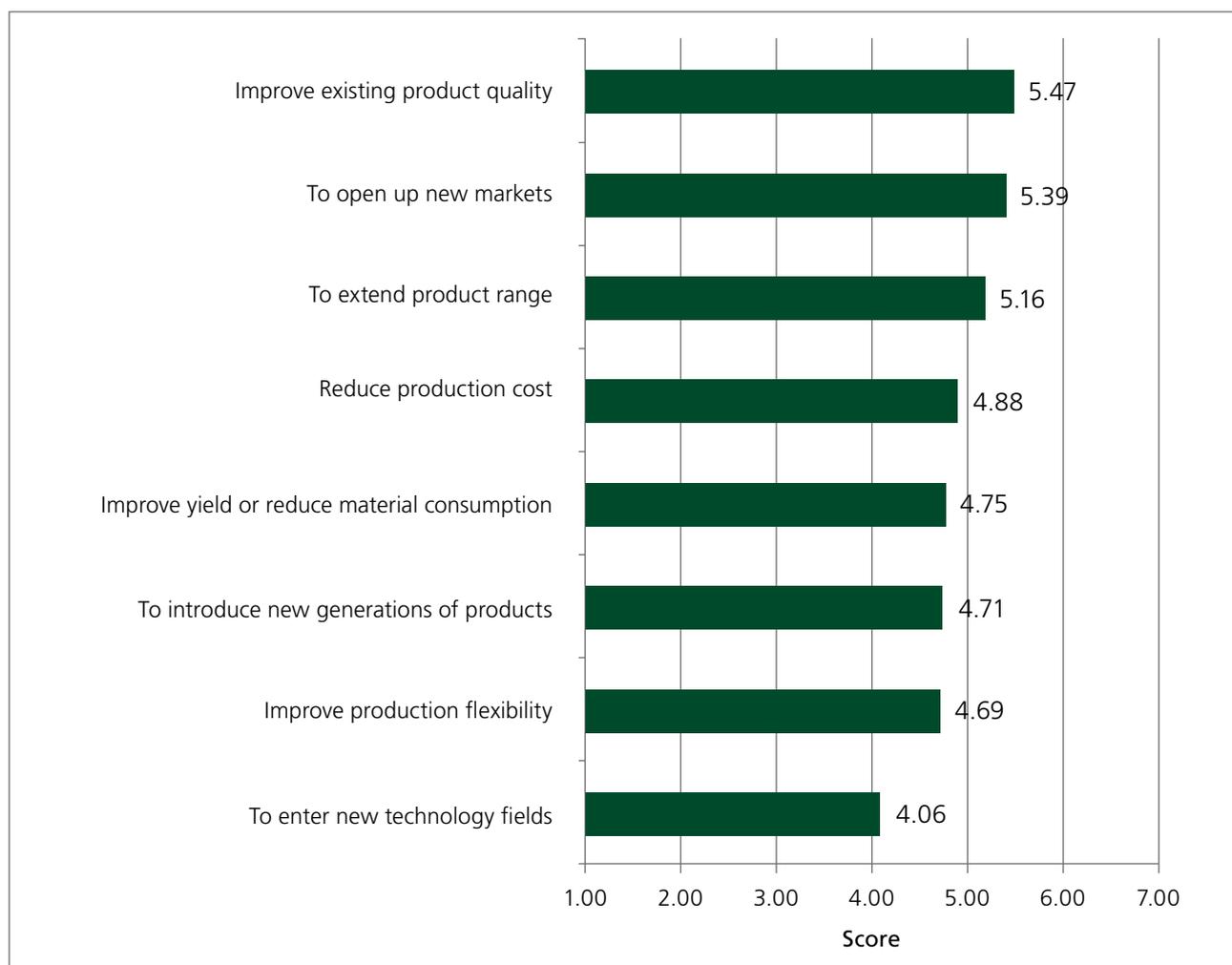
Scoring: 1 = fully disagree to 7 = fully agree.

(ranked #1), closely followed by reducing cost and improving yield (#4 and #5). These are typically “safe” innovation strategies. Sandwiched between these are innovation objectives concerned with opening up new markets (#2) and extending product range (#3). However, objectives relating to truly breakthrough activities, such as introducing new generations of products and entering new technology fields, are only ranked #6 and #8 (of 8) respectively. This suggests there are some barriers to how EO can encourage truly novel or breakthrough innovation activities over and above more gradual and safe incremental innovation activities.

The survey results indicate that great emphasis is placed on incremental innovation within the boundaries of the existing business and technological domains as compared with breakthrough or radical innovations. In fact, the results make clear that entering new technological fields is the lowest innovation priority in this sample of UK family firms, whereas greater emphasis is placed on reducing production costs, improving services and improving production flexibility (ranked #7). The EYMS Group case study illustrates these dimensions of innovation (see Case study 3). These observations are in contrast with how respondents defined their firm and family EO.

However, firms and families with a higher EO are consistently significantly more innovative across all of the innovation categories shown in Figure 5. A greater proportion of firms are involved in

Figure 5: Innovation objectives



Scoring: 1 = fully disagree to 7 = fully agree.

improving existing product quality (79 per cent) compared with entering new technology fields (45 per cent).

Analysing respondents based on the life cycle stage of the family firm, splitting them between first or second/later generation ownership, there is no difference in the importance of improving existing product quality. But there is a difference regarding “entering new technology fields” between first generation firms (53 per cent view this as important) versus second/later generations (41 per cent view this as important), indicating that mature family firms can be more conservative in terms of innovation.

Case study 1

HMG Paints



Specialist product and process innovation while ring-fencing more radical innovations

HMG Paints was founded in 1930 and is now third generation owned and managed. The company, which employs 170 people, manufactures speciality paints and is based in Manchester. HMG operates in a location and sector where many volume paint manufacturers have been squeezed out by low-cost foreign producers, and it competes mostly through moderate product and process innovation in the specialty paints segment of the market. Product innovations include biocidal anti-fouling for boats, flexible paint for commercial truck sides, PVC finishes for architectural coatings, temporary grass markings for sports grounds and anti-graffiti coatings for buildings.

The fourth generation is given challenging projects, including working overseas, and currently involving developing an online marketing business to bring the firm’s products to a wider consumer audience. Apprenticeships encourage children of non-family employees to be involved from an early stage in maintaining the family culture; they also reduce outsider domination. This creates a culture in which there are powerful reciprocal loyalties among the family and its staff. The company boosts its reputation by supporting local community enterprises. Networking with other producers is difficult as competition for intellectual property is fierce. Rather, social capital is mainly focused on that derived from close networks with distributors, some of them other family firms. The company refuses to recruit outside non-executive directors to avoid constraints that might compromise innovative initiatives. However, it has an operations board made up of non-family and family employees, with the expertise of non-family employees who are the most senior people in the company and who had been “born” or “weaned” in the company, being drawn upon by having them closely involved in developing innovation activities.

The company’s approach to innovation and entrepreneurship is quite conservative as it seeks to protect the future of its employees. As such the company seeks to pursue organic growth within the core business and to carry out a few ring-fenced “outer edge” projects that could either be very big

and exciting or fail. Although the brother of the current CEO is on the board of HMG, he has also established a separate spin-off business in the chemicals sector, Byotrol, which is now listed on the Alternative Investment Market. This arrangement provides security for the main company by avoiding exposing it to the unusual risks involved in Byotrol. At the same time, the family is open to benefit from the opportunities for riskier innovative initiatives in a growing niche of the chemicals sector.

Case study 2

Howarth Timber Group



***A follower strategy
devolving innovation to
the business units***

Howarth Timber Group is a family business with 175 years of experience employing over

1,000 people. It is the UK's largest privately owned timber company, and its origins can be traced back to 1840.

Howarth Timber produces a range of timber products across five activities. They operate an integrated manufacturing and distribution supply chain to serve customers, most of whom operate in the construction industry. The company imports, treats and machines timber. It is also a leading lean manufacturer of timber windows and door, and also timber structural roof and flooring products. In addition the firm has a chain of timber and builders merchants.

Innovation is mainly focused on operational and customer services aspects. In the timber and building supplies area, Howarth Timber has innovated by introducing an online training academy. The company actively monitors market and competitor developments, and much of its innovation arises out of a follower strategy, reverse engineering and enhancing what competitors are doing.

With respect to manufacturing activities, the company is engaged in the manufacture of high-performance timber doors and currently has a patent application for a sliding sash window enabling easier operation.

The company does not have a dedicated R&D team but empowers the management and operations teams in each division to take innovation initiatives that reduce waste and improve processes. Senior managers for its divisions are recruited who have a management style that allows scope for bottom-up innovation initiatives.

The company is currently run by the two sixth generation brothers. The seventh generation have

recently been introduced into the business in training roles following university, much as the previous generation. Seventh generation members are learning the business by working in each of the divisions. They are not yet involved in running the business but initial steps have been taken to introduce them to the company's trustees. No other family members are involved in the business.

For the first 125 years of the firm's existence there was little innovation. Innovation only began about 50 years ago with the fifth generation. At that time the family only owned 15 per cent of the business and the current owners' father set about buying out the other shareholders to enable more control and scope for innovation. Following the premature death of their father, the two brothers have run the business jointly since 1988. Over this time, markets and technology have changed and the brothers are able to do more modelling and forecasting than before.

Innovation initiatives are devolved to divisional managers who come up with a three-year plan and a one-year budget regarding new developments. The brothers participate in setting and reviewing objectives for the divisions. Where possible, they also look to achieve synergies and economies of scale across the group. As long as divisional managers put forward a good business case, the brothers will support it subject to the overall cash flow and gearing position of the group. The treasury function is at group level and the company is not averse to borrowing to fund investment as long as gearing is maintained at fairly conservative levels.

The company identified one innovation initiative that was not fully successful. This involved the acquisition of a loss-making business that would enable innovation through transforming the manufacture of timber-framed houses into the manufacture of retail stores using the same techniques, enabling off-site manufacture of retail stores and speedier construction. However, the acquired business did not perform in line with expectations. Much of its market disappeared and the core family business was left to salvage the profitable elements while closing the unprofitable parts, which involved redundancies for about half the workforce in that subsidiary. The remaining activity is now deemed to be successful.

In the last two years turnover has increased through organic growth by over 25 per cent, from £126 million to £159 million. Looking to the future, in the words of the CEO, Nick Howarth, the group intends to "maintain its flexible management structures and be responsive to the evolving needs of customers. We will continue to grow by having a respected, empowered, motivated and trained workforce, and through our capital investment programme, which will be over £14 million this year."

Effects of innovation

The family firms surveyed report very positive results from their innovation activities, suggesting that their distinctive approach to innovation is effective. In particular, new products account for more than 10 per cent of sales in the majority of the sample, and only 7 per cent do not obtain any significant sales benefit from innovation (see Figure 6). The survey indicates a tendency towards incremental innovation practices being common in family firms. This pattern is associated with limited creation of knowledge-based assets in the form of patents: the majority of firms (86 per cent) have never filed

a patent (see Figure 7). Howarth Timber, for example, adopts a follower innovation strategy, mainly focused on improving operations and customer service. Similarly, the bus company EYMS Group (Case study 3) has engaged in operational innovations, but has also been innovative in developing driver training activities that it now sells as a service to other companies.

Figure 6: Innovation performance – percentage of sales from new products

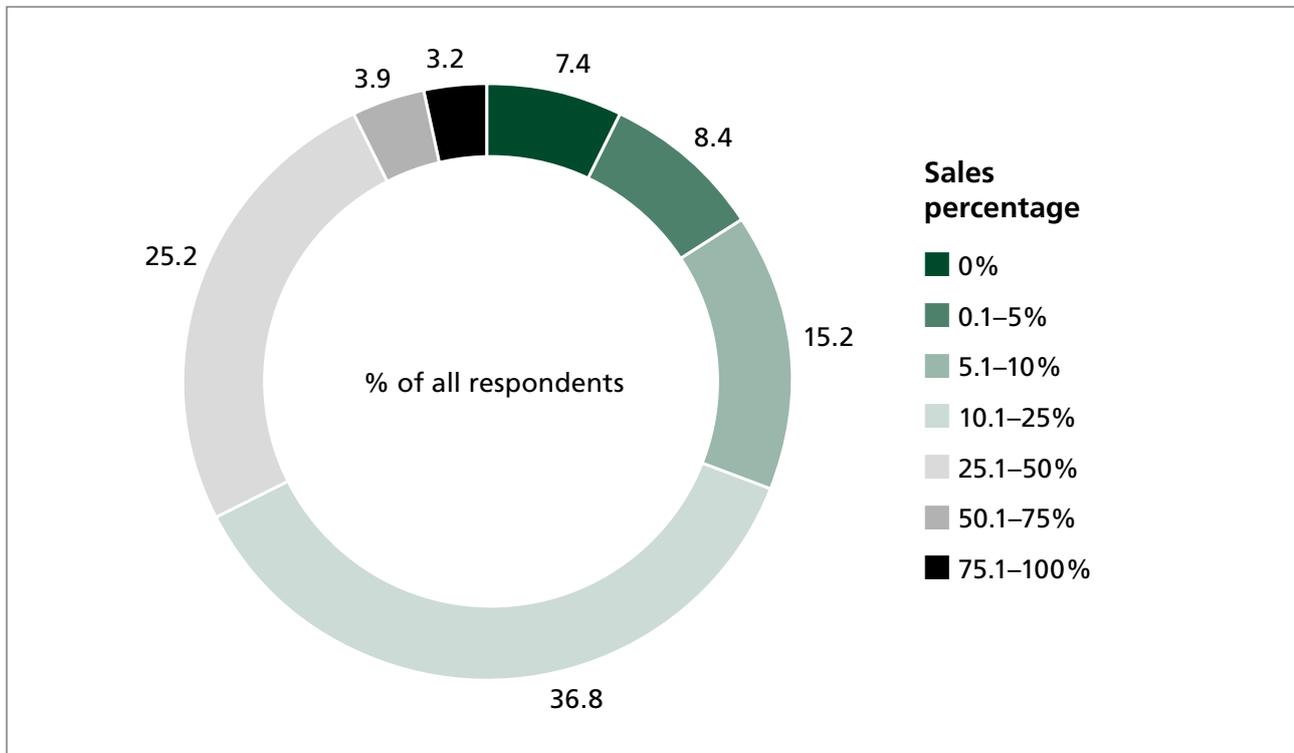
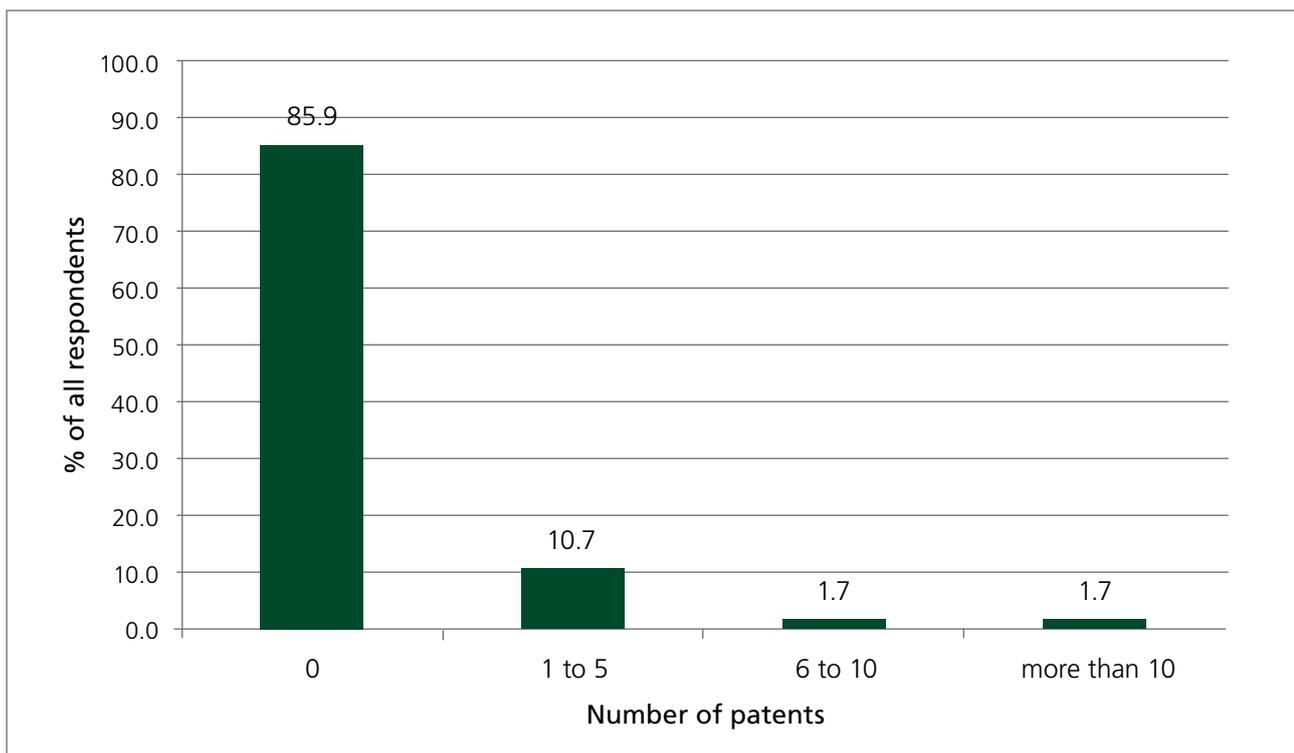


Figure 7: Innovation performance – patents filed



EYMS Group



An informal approach to innovation involving family and non-family members

East Yorkshire Motor Services (EYMS) is the largest family-owned bus company in the UK. EYMS itself was founded in 1926, becoming part of the National Bus Company in 1969.

EYMS Group was established in February 1987 by a team of senior managers employed by East Yorkshire Motor Services Limited in order to buy the company from the government as part of its bus industry privatisation programme.

After the management buy-out, EYMS Group continued to grow, by acquisition and by expansion of its routes and services. In September 1997 the business interests of the two remaining members of the buy-out team were demerged, leading to the main coach holiday business, National Holidays Limited, becoming an entirely separate company, leaving Peter Shipp as the sole owner of EYMS Group. Following further restructuring, the business now has 700 employees and an annual turnover of about £30 million, earned chiefly on local bus services but with substantial contributions from school contracts, National Express contracted routes, private coach charter and holiday tours, plus revenue from on-bus advertising and its design studio.

CEO Peter Shipp, as the sole owner of the company, gave some company shares to his wife and three children and the “family firm” was born. His wife takes no active part in the business and does not want to; the daughter worked with them for a while as secretary/PA but left to do other things; and the two sons joined the firm. There was no pressure from the parents for any of the children to join the business, and Peter Shipp stated that “if my kids wanted to come into the company they would have to show what they were made of”. The children started working elsewhere first and then joined the company at the bottom and worked their way up. The youngest son (David) joined in 1990 as a builders’ labourer, and the eldest son (Jonathan) joined in 1996 as a bus driver. David showed aptitude for business and became Assistant Operations Manager, and then General Manager of Whittle Coach & Bus Limited, but was unable to resolve their financial difficulties. Whittles was sold and David returned to EYMS as Group Performance/Business Development Manager, a senior position but without line management responsibilities. Jonathan became a Depot Supervisor in the village where the family live and is happy with this role.

The board consists of Peter Shipp as CEO and Chair, plus the Finance Director who has a 5 per cent share option (should the company be sold). They have several very informal board meetings a year, mainly to sign off the accounts. The CEO encourages ideas from all staff, is always “kept in the loop” in terms of operations, but does not generally get involved in day-to-day decisions unless they involve capital expenditure.

In terms of innovative changes to operations – for example bus services and service planning –

David, as Group Performance/Business Development Manager, will often be involved. However, the main input comes from non-family senior managers such as the company accountant, chief engineer, commercial manager, and operations managers who are responsible for any changes. No formal innovation or operations board exists. The group used to have general management meetings attended by all senior managers to discuss improvements and changes, but this was abandoned in favour of more focused topic-related meetings – for example, the theme of accident reduction would involve a meeting with only those senior managers affected. The CEO sometimes attends these meetings. Innovations, mostly in operations or services, can be led either by the family or by non-family. A significant innovation was the development and extension of driver training, which was led by a non-family Training Manager with the support of the CEO. The company now also sells these services outside of its own organisation.

The family has been very innovative in relation to its PR activities. For example, it has set up the “Big Bus Day”, which is a one-off event at the local Street Life museum in Hull. The idea behind the event is to engage the local community by displaying buses from the past and present, and in doing so the company raises money for the NSPCC. In the words of the CEO, “a lot of people come, they all enjoy it ... we meet a lot of our customers ... [and] it demonstrates and helps our position in the community”.

The CEO does not see the next generation as currently having a great influence on the firm as the sons are not in senior positions (yet), but he himself is very influential and innovative. Also David, the Group Performance/Business Development Manager, with his wide-ranging role has the potential to be influential because he is able to oversee all aspects of the company including performance, compliance, service reliability and business development.

3 Enabling entrepreneurship and innovation

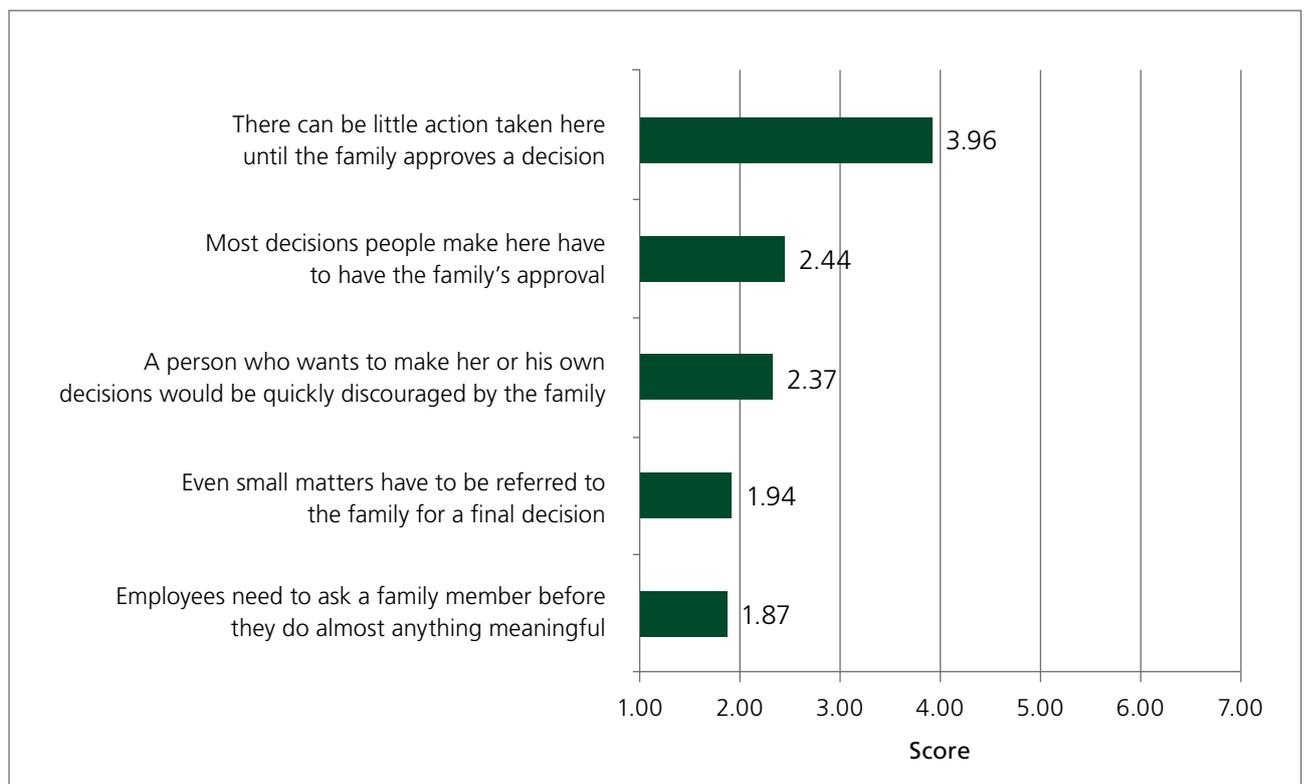
Enabling concerns the ways in which family businesses implement their strategies regarding entrepreneurship and innovation.

Family decision-making authority, commitment and goals

This research throws light on how family owners and managers influence firm behaviour and the goals that are promoted through their influence. The study examined the diversity of family firms along two main dimensions of family influence: the concentration of decision authority in the hands of the family and family commitment to the firm.

There is a generally held view that decision-making in family firms is concentrated in the hands of family members, but this survey shows that this is not so clear cut. Respondents neither agreed nor disagreed that little action can be taken without approval from the family (see Figure 8). In addition, respondents disagreed quite strongly on a further three statements indicating that family firms do not get overly involved in the decision-making process. This is evidence that while families may still dominate and strictly manage key strategic decisions (especially where capital expenditure is concerned) they are allowing autonomy and flexibility to non-family managers and employees on less strategic operational matters. This influence of non-family managers is illustrated in the case studies, where divisional

Figure 8: Decision-making authority



Scoring: 1 = fully disagree to 7 = fully agree.

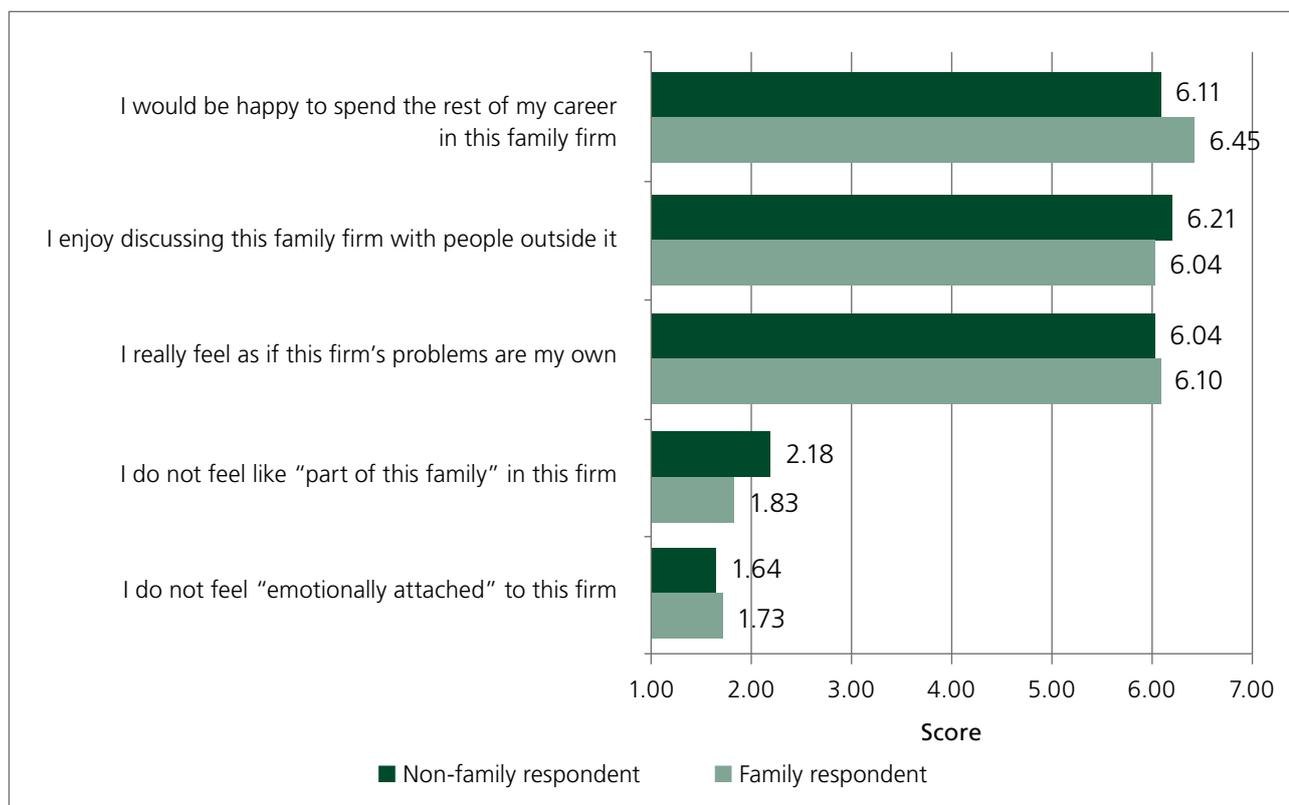
managers at Howarth Timber are responsible for bringing innovations to family senior managers for approval (Case study 2) and EYMS Group, whose family CEO does not get involved in day-to-day decisions unless they involve capital expenditure (Case study 3).

Family firms benefit from a very strong commitment from family owners and managers. The survey reinforces findings from other studies that indicate a strong intention from family and non-family employees to continue their career within the family firm, feeling emotionally involved in the company and enjoying talking publicly about it (see Figure 9).¹⁵

The concentration of decision-making authority within the family does not influence the firm-level or family-level entrepreneurial orientation (EO). In fact, the Howarth Timber and EYMS Group cases both demonstrate that decision-making authority in these family firms (including decisions about innovation) has been devolved to non-family managers. However, family commitment emerges as an important determinant of EO where family firms with a higher level of commitment¹⁶ are indeed more entrepreneurial at the firm level.

The family firms surveyed are dealing with multiple goals. As illustrated in Figure 10, non-family-centred economic goals (such as improving growth and profits) are the most important class of goals for family firms,

Figure 9: Commitment to the family firm

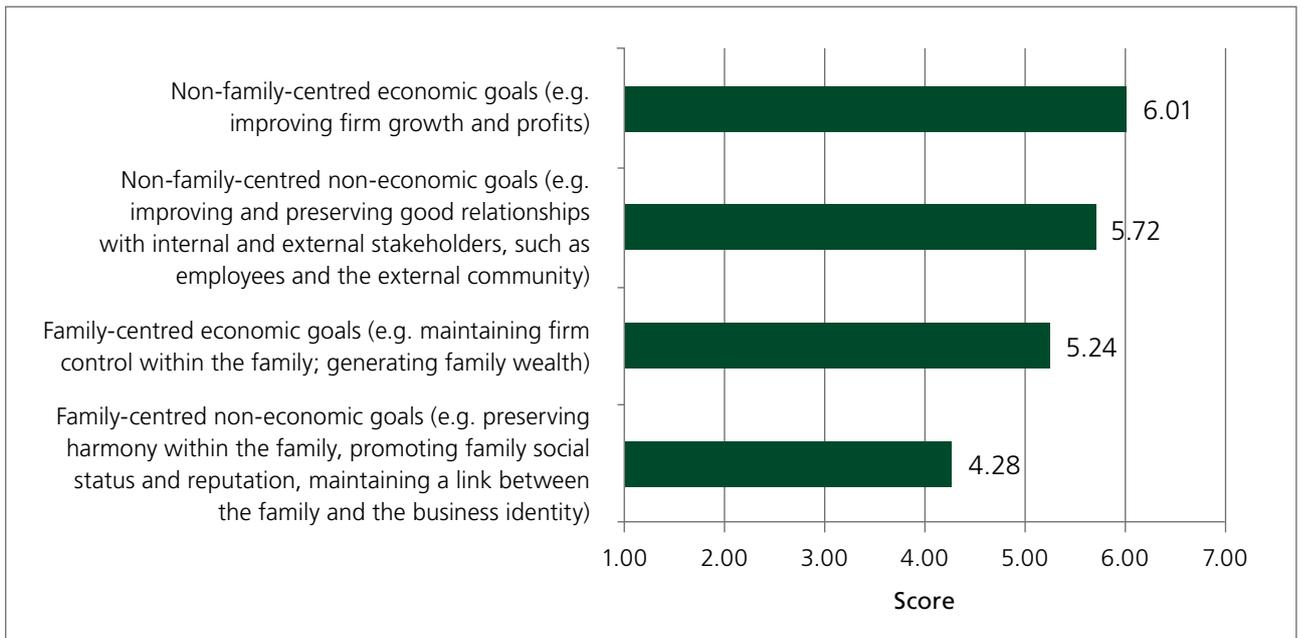


Scoring: 1 = fully disagree to 7 = fully agree.

15. Bacon, Hoque and Siebert (2013).

16. High-level commitment is defined as a score of six or more on the scale shown in Figure 9 for the first three questions, chosen in order to have enough data points for analysis.

Figure 10: Firm goals

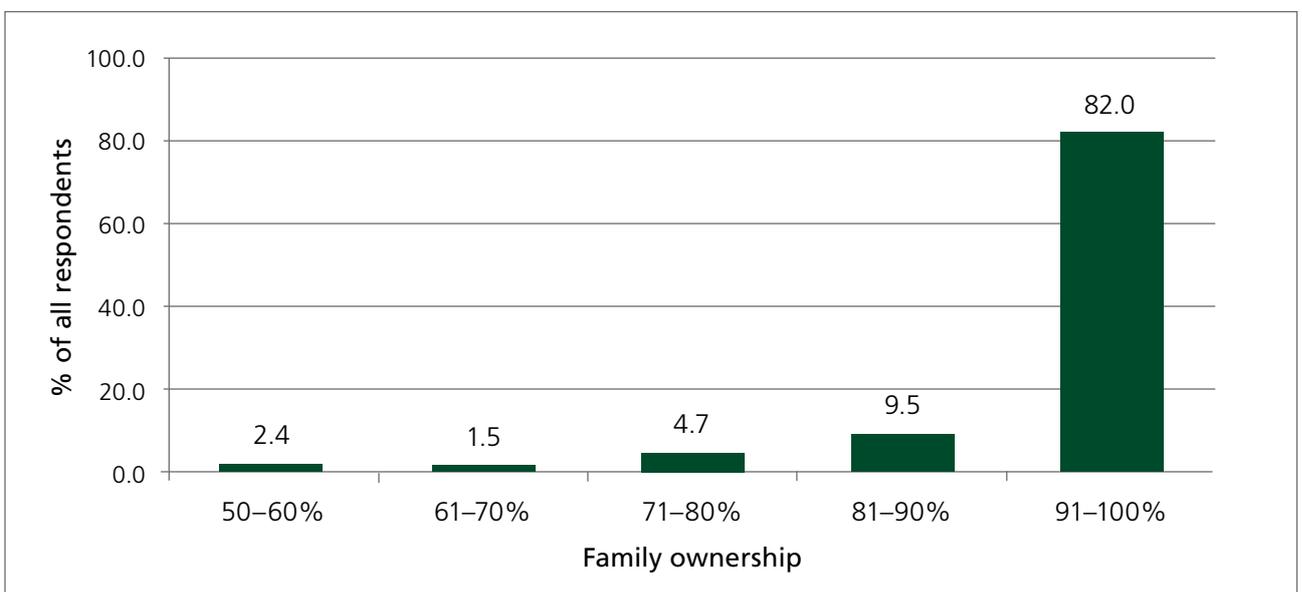


Scoring: 1 = fully disagree to 7 = fully agree.

followed by non-family-centred non-economic goals (such as preserving and improving relationships with stakeholders). Family-centred goals, like maintaining control of the firm within the family and preserving harmony, are less important but nevertheless still significant. Family influence in terms of decision-making authority and commitment does not necessarily result in a greater importance of family-related goals or of non-economic goals compared with economic goals, but it increases the number of goals and their diversity.

The research results also show that family firms which prioritise non-family goals are more entrepreneurial in terms of firm-level EO compared with firms that prioritise family goals (64 per cent for non-family goals versus 48 per cent for family goals). However, some caution is in order here as the difference is only weakly significant and may be due to the desire to maintain stability and continuity.

Figure 11: Family ownership distribution



Family involvement in the firm

The survey offers a detailed picture of family involvement in ownership and management. As illustrated in Figure 11, most family firms in the sample are owned by families with an ownership share that exceeds 90 per cent. Similarly, family involvement in management is widespread, with almost 80 per cent of family firms having a family CEO. Moreover, having a family CEO is beneficial for entrepreneurial orientation. Most CEOs are male (93 per cent). The top management teams (excluding board members) involve, on average, 5.5 individuals, of whom only one is a family member. This data suggests that family members commonly hold leadership positions in their firms' management but are involving non-family managers to a great extent as well. Most family firms (77 per cent) have not made a clear decision about who is going to be the next CEO of the firm. However, against the backdrop of the vast majority of CEOs currently being family members, it is interesting that while 60 per cent of respondents expressed a preference for a family member, 84 per cent are open to appointing a non-family member as the next CEO.

Also, the findings offer important insights about the generational involvement of family members. As illustrated in Figure 12, earlier stage first and second generation run family firms are equally represented in the research sample and altogether constitute almost three-quarters (73.5 per cent) of the respondent firms. The representation of longer-standing family firms run by later generation family members is nonetheless significant given the attrition rate of family company survival across generations. Over a quarter (26 per cent) of firms are run by the third generation or later, including 5 per cent representing family firms run by the fifth and older generations. Separately, in terms of the role of family, almost 60 per cent of responding firms have two generations of family members involved in the business, whereas approximately 35 per cent of family firms have only one generation involved (see Figure 13). Cases of family firms where three or more generations are involved are naturally rarer.

Figure 12: Generational distribution

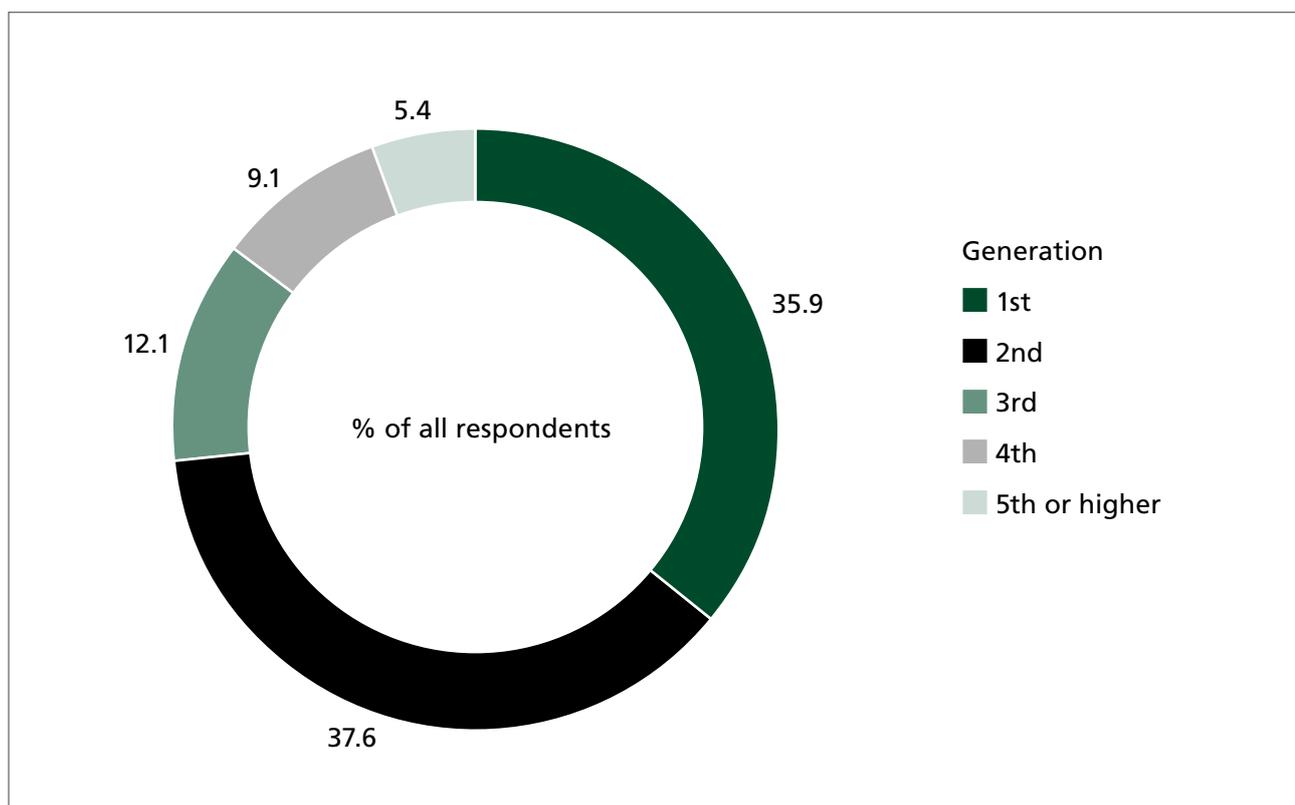
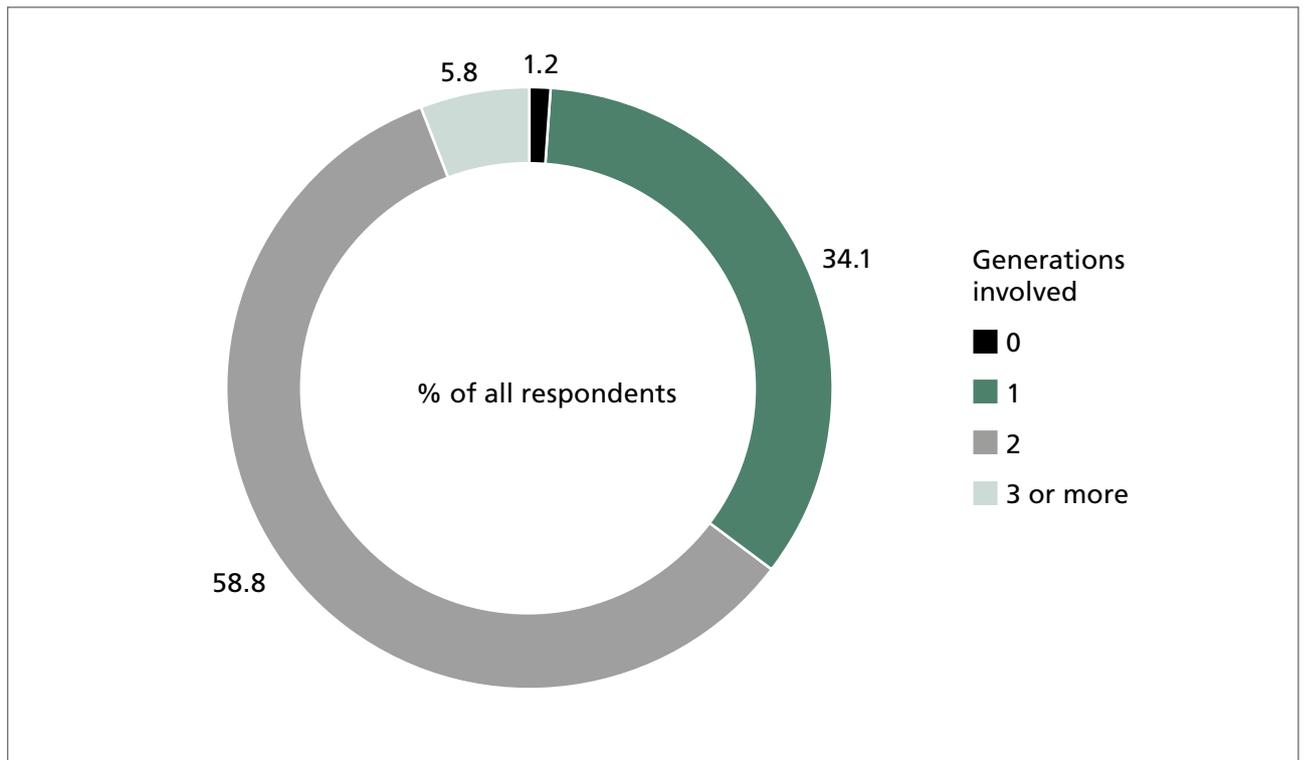


Figure 13: Number of generations involved in the management of the firms



The generation involved in the running of the firm is very important in terms of entrepreneurial orientation. Studies have suggested that later generation family members tend to be less dedicated to their family firm and that because of this lack of commitment, entrepreneurship and innovation can suffer. Both first and second generation as well as later generation firms think that incremental innovations (for example product improvements) are much more important than radical innovations (for example new technology development). However, first generation firms are more likely to be involved in radical innovations than firms owned by later generations. This finding may partly explain why firms run by later generations do not perform as well as their first generation forebears. The average return on capital employed between 2011–13 for later generation firms is significantly lower at 11.2 per cent than for first generation firms at 20.6 per cent. Our cases suggest that later generation firms may need to prune and concentrate ownership in order to minimise resistance by those family owners not involved in running the firm to actions by the current generation of family owner-managers to introduce innovation to sustain the firm. For example, Howarth Timber (Case study 2) and Bibby Line Group (Case study 5) have both engaged in ownership pruning and concentration to this effect.

4 Evaluating and managing entrepreneurship and innovation: The role of governance

Evaluating and managing concerns the governance mechanisms that family businesses develop to address the risks associated with entrepreneurship and innovation. These mechanisms can be crucial in supporting entrepreneurship and innovation in family firms, especially across generations. For example, at Linn Products (Case study 4), the board has extensive business experience and has been introduced to help develop the company's innovative approach in a challenging but supportive way.

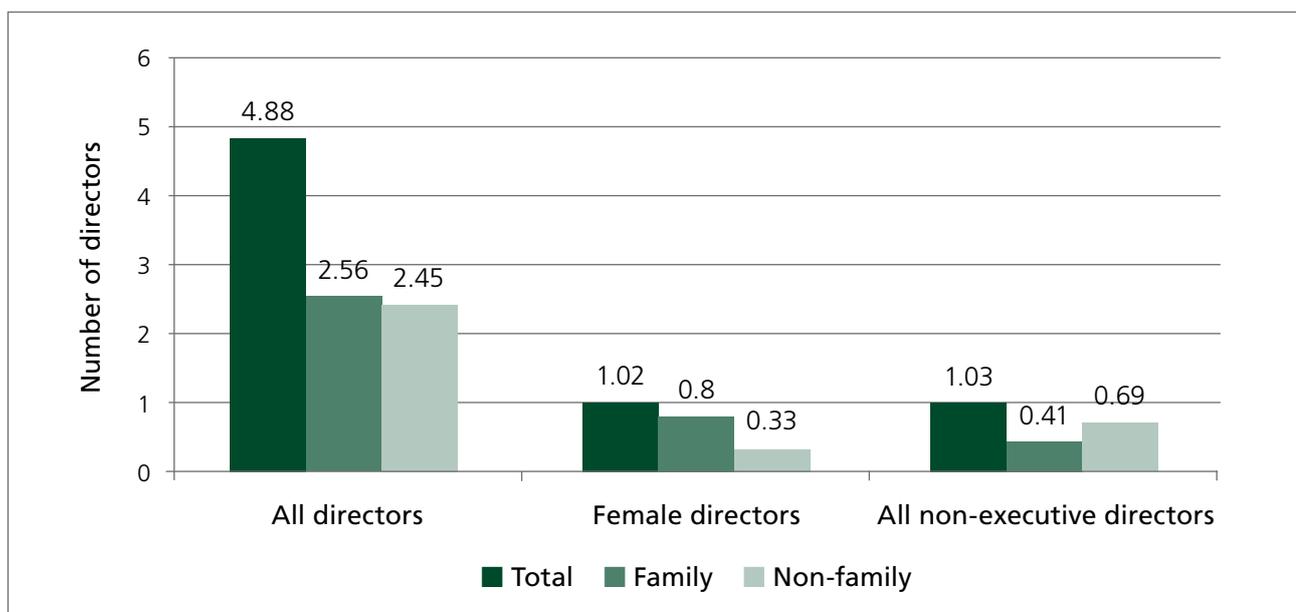
The survey provides insights into the governance of family firms, including boards of directors, operations boards and trustees, and the relationship with entrepreneurship and innovation. Overall, the results point to the complex, varied and multi-level nature of governance.

Board of directors: Composition and roles

The family firms surveyed have on average five directors sitting on their boards, half of whom are family members,¹⁷ and they commonly have one non-executive director, in most cases a male non-family member (see Figure 14). As might be expected, in nearly 9 out of 10 businesses, the board of directors of UK family firms is chaired by a family member.

The data shows that women tend to have low representation on family firms' boards of directors, with

Figure 14: Composition of the board of directors

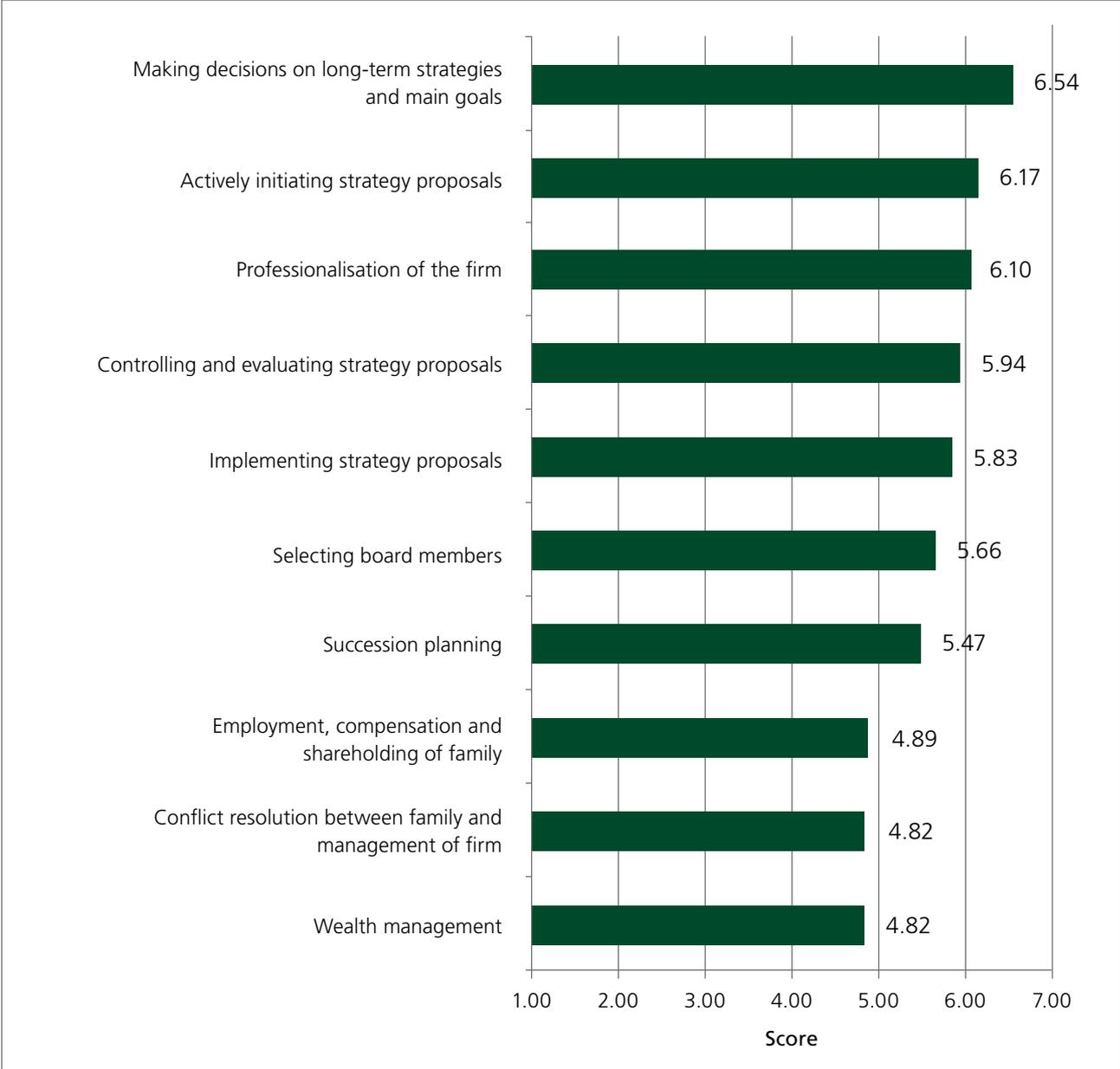


Note: Family and non-family numbers do not add up to the total since the respondents did not complete all of the questions. This data however gives an indication of the trends.

17. For further details, see Table 2 in Wright et al. (2016).

on average each board having only one female member. Gender represents an important dimension of diversity in family business governance, and prior research has emphasised how having women on the board can result in higher levels of entrepreneurship, innovation and financial performance.¹⁸ Our findings support this idea, indicating that increasing female participation on the board of directors is an area that family firms could address. Women can change the nature of the conversation in the boardroom, sometimes acting as a catalyst for more productive debate. Having a board with a balanced gender mix can lead to a more positive working environment, which in turn contributes to a better functioning board overall. Women directors may also encourage the firm to introduce more flexible working practices for employees, which can increase workforce morale, leading to superior results in entrepreneurship and innovation.

Figure 15: Role and tasks of board of directors



Scoring: 1 = no involvement to 7 = fully involved.

18. Jehn, Northcraft and Neale (1999); Huse, Nielsen and Hagen (2009); Wilson, Wright and Altanlar (2014).

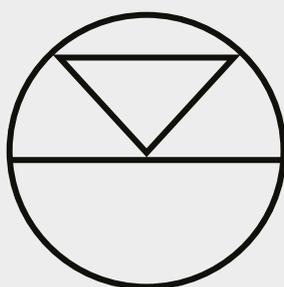
The data also reveal the main tasks and activities carried out by the board of directors in UK family firms. The strategic role of the board is the most important activity for the directors, as the board is mainly concerned with making decisions on long-term goals and strategies, along with initiating, implementing and controlling strategy proposals (see Figure 15). This suggests that the traditional control role of the board is less important than strategy initiation, possibly reflecting that for the family firm there is less need to monitor managers as compared with assisting them to formulate effective strategic plans from which entrepreneurship and innovation can flow. Professionalisation is the third main concern of the board, reflecting the importance attached to developing formal managerial structures in family businesses. Interestingly, while succession planning is important to the directors, the board is less involved in employment and compensation of family members, conflict resolution and wealth management, suggesting that these more family-oriented issues may also be addressed through other mechanisms.

In the context of boards of directors, there are important differences in levels of entrepreneurship and innovation depending upon the governance configuration of the family firm. When the board is made up of a majority of non-family individuals the *firm*-level entrepreneurial orientation seems greater; 67 per cent of firms are entrepreneurial compared with only 57 per cent of firms where family members make up the majority around the board table. There is no relationship to *family*-level entrepreneurial orientation, however.

When the CEO of the firm is a family member, family-level entrepreneurial orientation is also significantly greater; 50 per cent of firms have a higher entrepreneurial orientation compared with only 30 per cent when the CEO is not a family member. This could be the result of such families having a propensity towards risk, being more proactive in introducing innovations and being able to anticipate the competition.

Case study 4

Linn Products



LINN

Significant product innovation and the importance of a strong board

Linn Products, founded in 1973, is located in Scotland and is second generation managed. The company manufactures high-end music systems for the home, operating within a very competitive and innovative sector. The firm was very successful in developing novel products under its founder, but then lost its way when the founder became ill in 2001, such that by February 2007 the need to change had become imperative. After 2001 there had been two succession attempts involving non-family managers that were not successful. During this period, innovation did not progress at the rate required for the company to succeed.

By February 2007 the bank refused to extend the company's overdraft or support the then non-family CEO. The bank appointed a turnaround specialist in 2007 who worked with the founder to

restore the company to financial health. The turnaround was completed by 2009. The founder's son had been working in the business since 2003 as R&D director and was appointed CEO in 2009 once the turnaround had been completed.

The son was at the forefront of the turnaround as by August 2007 the technology platform that he had designed was launched. This platform was introduced to address the growing customer demand for streaming music from hard drives and the internet. Delivering higher performance than anything on the market at that time, this innovation allowed Linn to establish a market-leading position, which they have since retained. The new platform therefore played a significant part in the turnaround, offering something highly innovative to the market, and helping to repay the bank. The son was clear that his father wanted the company to be more innovative, and clear also about his role in turning around the business to achieve this goal.

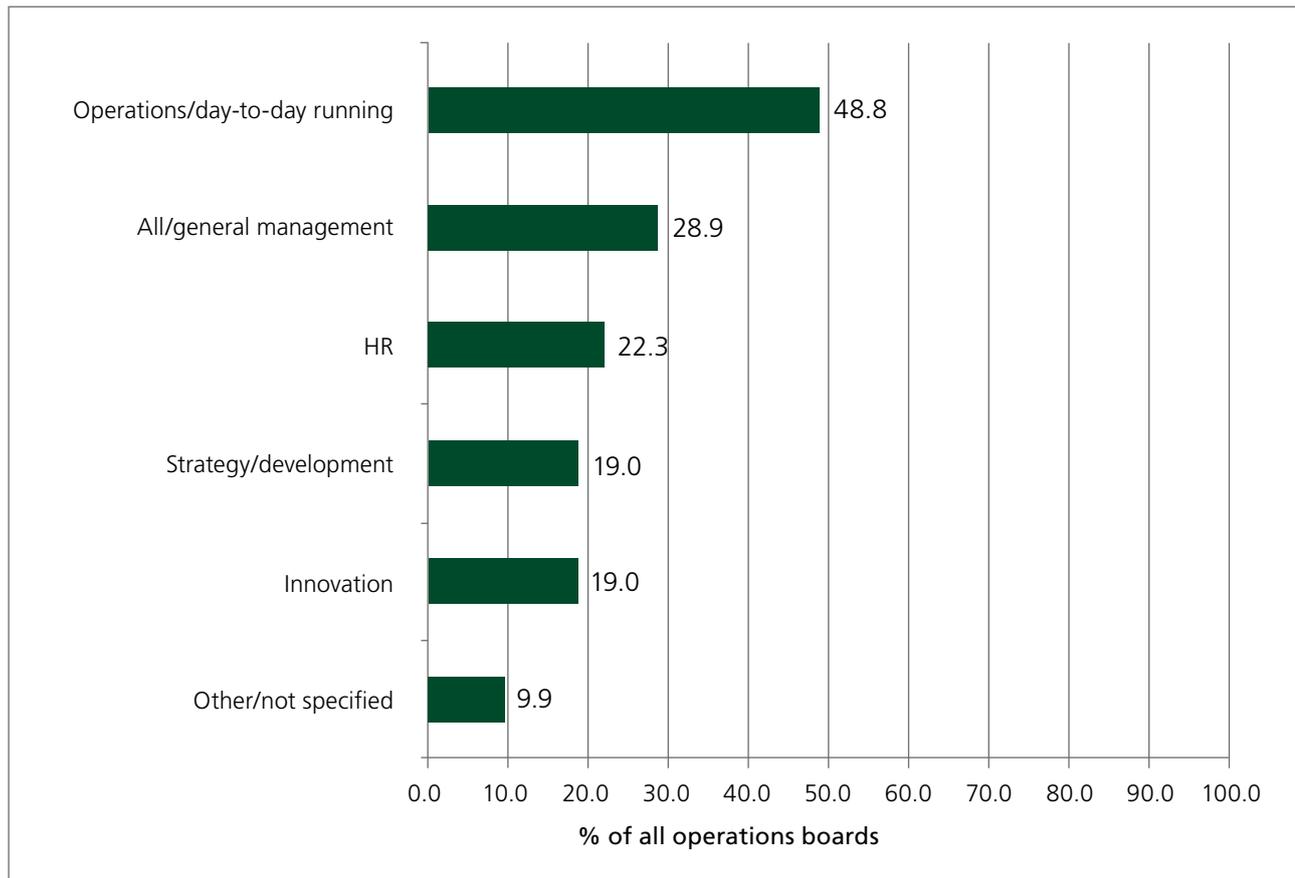
Governance at Linn has changed over time. The founder created the group structure in 2001 (phase 1) and the board at that time comprised the most senior managers in the company. When the non-family CEO was appointed in 2005 (phase 2), the board became a formal "family" board made up of family members and the non-family CEO. This board did not support the management adequately because the objectives for the business tended to be dominated by family objectives. In 2009 (phase 3), under the son as CEO and after the turnaround, Linn moved from a family board to a professional board with three non-family outside directors selected because of their business experience in areas including operations, marketing and technology. The current Linn board has independence, enabling a better balance between family and business objectives to be achieved. This supports the company's innovative culture. The board challenges, but is supportive of the CEO, and provides an effective way of formalising the relationship between the CEO and his father as founder.

Innovation is now seen as a continuous process, and capabilities have to be continually built. The company's engineers understand its values, which allows innovation at a grass-roots level. Financial resources are sometimes ring-fenced for new business ideas, some of which have their own three-to five-year plans. Linn Products remains today one of the most innovative companies in its industry.

Operations boards: Roles and tasks

Just over one out of three family firms in the research sample has an operations board (also termed a management board) in addition to the main board of directors. Management boards are primarily concerned with operational matters and the day-to-day running and wider general management of the firm (see Figure 16). However, these boards also have less common responsibilities, including HR and strategy development. Only one in five of the sample firms discuss innovation at their operations board meetings. It would seem likely that those who include discussion about innovation at their operations board will have a significant chance of this leading to the development of innovative new products or improvements to existing products. HMG Paints (Case study 1) sees its operations board as playing an important role in innovative activities. This board involves senior non-family employees imbued with the culture of the business who have the expertise to develop innovative products.

Figure 16: Roles and tasks of operations boards



Family councils and family offices: Roles and tasks

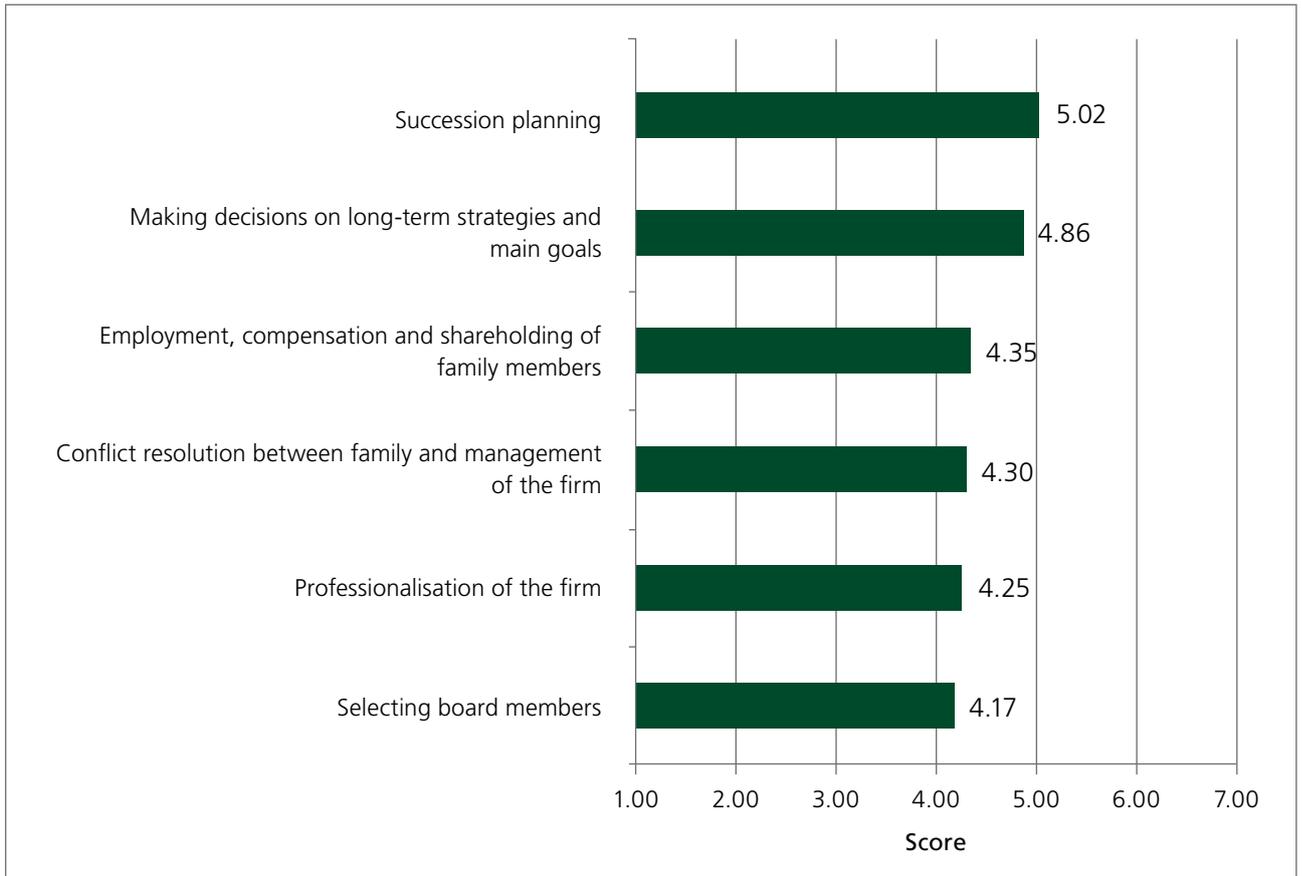
A significant minority of family firms in the sample (16.8 per cent) have a family council. Family councils have a pivotal role to play at the interface between family and business, with their most important contributions relating to succession planning, longer-term strategy and goal-setting. They also have important involvement regarding remuneration of family members and conflict resolution (see Figure 17). However, this analysis also indicates that family councils support the main board in service activities such as taking part in strategy formulation, professionalisation and selection of board members. The presence of a family council is not significantly associated with the entrepreneurial orientation of the firm, despite the fact that one of the main discussions is around long-term strategies and key goals. This suggests that either these discussions do not focus on entrepreneurship and innovation activities, such as introducing new products or improving existing products, or that such discussions are not translated into action by the board of directors.

It is less common for responding family firms to have a family office – an investment, liquidity management and administrative centre that supports the governance structure. Only 13.6 per cent of firms surveyed have a family office.

Trustees: Composition, roles and tasks

The survey also throws light on ownership structures, and only 8.5 per cent of family firms in the study have trustees. In the small minority of cases where trust ownership is present, there are on average 3.1

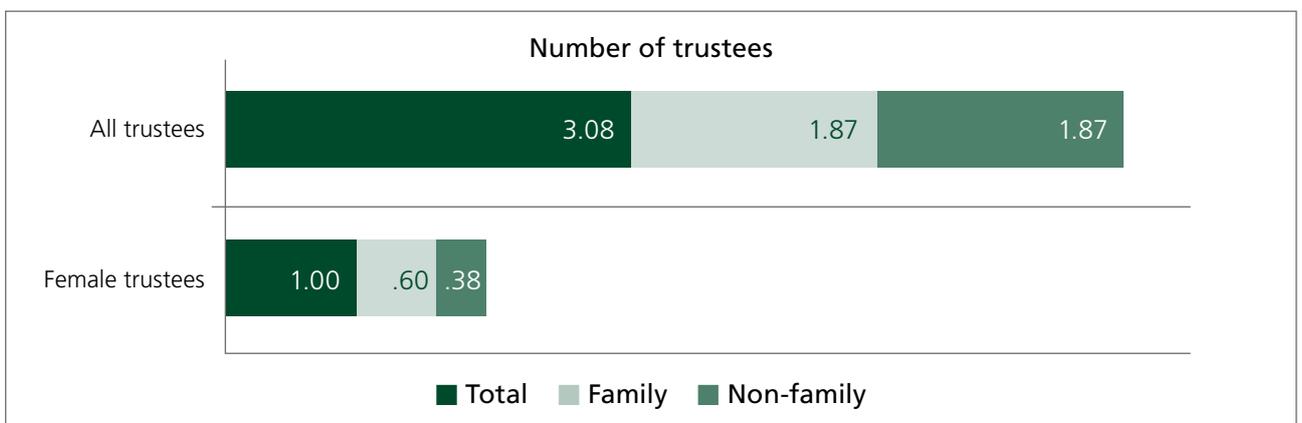
Figure 17: Roles and tasks of the family council



Scoring: 1 = no involvement to 7 = fully involved.

trustees involving a balance of family and non-family members (see Figure 18).¹⁹ Female involvement as trustees is limited but relatively higher compared with female involvement on the board of directors. Where a trust structure exists, trustees have on average 51 per cent of the shares in the company.

Figure 18: Composition of the trustees



Note: Approximately 20 respondents only. Family and non-family numbers do not add up to the total since the respondents did not complete all of the questions. This data however gives an indication of numbers.

19. For further details see Table 3 in Wright et al. (2016).

Figure 19 summarises the roles and tasks carried out by the trustees, which include most prominently wealth management, succession planning and conflict resolution, but also encompass strategic issues and professionalisation. The idea that trustees may have an impact on entrepreneurial orientation or innovation because of the influence they have on board members has not been demonstrated in this study. The presence of a trustee is not significantly associated with the entrepreneurial orientation of the firm. Some trustees do get more involved in their companies, but when they do they appear to have little influence on entrepreneurial orientation according to the survey. Despite this general evidence, formation of a trust can be a means to overcome resistance to innovation on the part of dispersed family shareholders because it can help concentrate decision-making authority. For example, Bibby Line Group (Case study 5) introduced an ownership trust structure with the aim of enabling family members involved in management to take strategic decisions regarding the development of the business without encountering conflicts with family shareholders not involved in the business.

The presence of trustees is generally associated with lower firm performance. This does not appear to be because it is poorer performing firms that are engaging trustees,²⁰ but it may be that trustees devote insufficient attention to ensuring that the firm has appropriate governance mechanisms including a good board.

Figure 19: Roles and tasks of boards of trustees

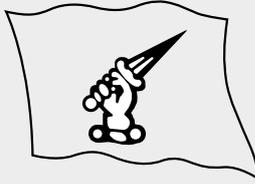


Scoring: 1 = no involvement to 7 = fully involved.

20. Work in progress by Louise Scholes and Mike Wright, which examines a sample of 250 UK family firms, half of which have trustees.

Bibby Line Group

BIBBY
LINE GROUP



Innovation and entrepreneurship through diversification accompanied by ownership restructuring

Bibby Line Group was founded in 1807 and is now led by the sixth generation group managing director, Sir Michael Bibby. The company had grown successfully for many years but by the early 1980s was experiencing serious challenges brought on by the recessionary conditions of the 1970s and family crises. The recession meant over-capacity in the company's main line of business, leading to redundancies and ships being sold at low values.

On the family front, some 45 per cent of shares were in the hands of cousins who were unable to influence the dividend or share price due to the corporate structure. The then fifth generation managing director, Derek Bibby, was also looking for a timely retirement but there was no obvious family successor as his children had not yet entered the business. To address these challenges and secure the survival of the business, Derek Bibby set about rebalancing the company's business model, reorganising its ownership and restructuring its management based on a four-point plan:

- **Innovation through diversifying the business in order to reduce its reliance on the cyclical shipping industry:** Bibby Line had developed a financial services business in the 1970s through its leasing activities, and in 1981 it moved into debt factoring by buying up small businesses and creating a financial network. The company then expanded its maritime business to include "coastels" (floating accommodation) and jack-up platforms (mobile self-elevating accommodation platforms used in shallow sea depths). Third, the company moved into distribution to take advantage of the increasing involvement of third-party contractors in the domestic movement of goods, acquiring a warehousing and distribution contractor.
- **Professionalisation of the business** involved formalising some of the group's important structures, processes and procedures, notably strengthening the skills of the board and appointing a non-family group managing director who was to spend some 30 years with the business, latterly as non-executive chairman.
- **"Pruning" the ownership tree** to ensure closer alignment between ownership and management through the branch of the family involved in managing the business acquiring shares from cousin shareholders not involved in management. After these transactions Derek Bibby owned 80 per cent of the shares, which means that today the business is the equivalent of a second generation "sibling partnership" as opposed to a sixth generation "cousin consortium", while opening the way for further business diversification, with the new, tighter ownership group more willing to take a longer-term view.

- **Setting up an ownership trust** so that owners of almost 80 per cent of the business became trust beneficiaries rather than direct shareholders. This change involved a significant transfer of power towards the board and the management of the business, with the aim of enabling management to take strategic decisions regarding the development of the business without encountering conflicts with family shareholders not employed in the business. Further, involvement of the family in governance was now on an informal, ad hoc basis. Of the two family members involved in management, Michael Bibby as managing director focuses on the business while his brother Geoffrey is non-executive family director.

During 2005–07, Bibby Line Group sold all of its chemical and LPG tankers and jack-up platforms, using the funds to pay off debts and invest in developing its offshore interests (which, in 2013, were the most profitable parts of the group) and coastel fleet. The divestments allowed the group to continue diversifying, including acquiring a majority stake in the fascia group Costcutter, and subsequent acquisitions in plant and equipment hire and burial parks.

Source: Summarised from “Bibby Line Group Case Study”, part of the IFB Research Foundation Family Business Case Studies Project (in preparation), authored by Professor Ajay Bhalla, Cass Business School and Professor Joseph Lampel, Alliance Manchester Business School.

5 Business performance consequences of entrepreneurship and innovation

To examine business performance, the research survey included four financial/quantitative measures over the period 2011 to 2013: growth in turnover; growth in the number of employees; average return on capital employed; and average profit margin.

Entrepreneurial orientation and business performance

Entrepreneurial orientation (EO) has a marked positive impact on achieving higher performance in the family firms surveyed.

High EO is associated in the sample with a greater increase in sales revenue, a greater increase in the number of employees, a larger average return on capital employed (ROCE) and a larger average profit margin. In the case of *firm* EO,²¹ there is strong evidence that EO affects performance. Profit margin is significantly different for the two groups: 6 per cent for firms with higher EO compared with 3.8 per cent for firms with lower EO.²² In the case of *family* EO,²³ there is also strong evidence that EO affects performance. ROCE is significantly different for the two groups: 17.4 per cent for firms with higher EO compared with 11.9 per cent for firms with lower EO.

Decision-making authority, commitment and performance

There is weak evidence of an association between family owners' decision-making authority and performance, with firms with lower decision-making authority (score 3.5 or less) having a lower profit margin compared with those with a higher level of decision-making authority.²⁴

For firms with very high family owners' commitment,²⁵ ROCE and increases in sales revenue are greater than in the group with lower commitment. These differences are, however, only weakly significant.²⁶

21. For further details see Table 4 in Wright et al. (2016).

22. The level of entrepreneurial orientation was calculated by averaging the responses to all of the questions on EO on a scale of 1 (low EO) to 7 (high EO). Companies deemed to have a high EO were those that scored 4.5 or greater. This cut-off was chosen, rather than the median value of 4, since it would ensure that most of the firms in this group would be exhibiting higher than average EO.

23. For further details see Table 5 in Wright et al. (2016).

24. The level of decision-making authority was calculated by averaging the responses to all of the questions on this theme on a scale of 1 (low) to 7 (high). Companies deemed to have a low decision-making authority were those that scored 3.5 or lower. For further details see Table 6 in Wright et al. (2016).

25. The level of commitment was calculated by averaging the responses to the first three questions on this theme on a scale of 1 (low) to 7 (high). Companies deemed to have very high commitment were those that scored 6 or higher.

26. For further details see Table 7 in Wright et al. (2016).

Firm goals and performance

When non-family goals become more important than having a balance between family and non-family goals there is weak evidence that performance is affected.²⁷ Family-centred goals could be for example “maintaining firm control within the family; generating family wealth” whereas non-family-centred goals could be “improving firm growth and profits”. The average profit margin is lower for firms that favour non-family-centred goals. This could be an indication that these family firms are focusing more on short-term wealth generation and possibly making poor strategic decisions, resulting in reduced profits. The evidence points towards firms that prioritise non-family-centred objectives as being more entrepreneurial (although there is only weak evidence for this) but the strategic decisions taken, if not the correct ones, may naturally lead to falling profits.

Boards and performance

Professional board structures are associated with enhanced company performance. There is weak evidence that sales revenue growth is greater when the board is not controlled by family – that is, when the family directors make up 50 per cent or less of the board.²⁸ This difference may be due to boards that are not controlled by the family pursuing primarily commercial goals, thereby diluting the importance of family goals.²⁹ This evidence is also consistent with our earlier finding above that boards that are not controlled by family are likely to have higher EO. The average increase in sales revenue is 24.9 per cent for firms with 50 per cent or less family on the board compared with 9.1 per cent when more than 50 per cent of the board is family. There is no evidence that the status of the CEO (family or non-family) affects performance.

There is, however, strong evidence that the presence of females on the board is associated with better performance. The profit margin is significantly different for the two groups; 5.8 per cent for firms with females on the board compared with 4.2 per cent for firms with no females on the board.³⁰ Having women board members is often associated with less risk-taking by the firm, which might imply less entrepreneurial and innovative activity and less variability in profits. On the other hand, the role that women play in stabilising boards combined with the fact that women have their own ideas about new products, could enhance the entrepreneurial orientation of the firm.

Trustees and performance

There is weak evidence that having family firm trustees is associated with poorer performance. Average ROCE is 15.3 per cent for firms without trustees compared with 7.2 per cent for firms with trustees.³¹ External and internal advisers, mentors and advisory boards are all important resources for family firms.

27. For further details see Table 8 in Wright et al. (2016).

28. For further details see Table 9 in Wright et al. (2016).

29. Kotlar and De Massis (2013); Bammens, Voordeckers and Van Gils (2011).

30. For further details see Table 10 in Wright et al. (2016).

31. For further details see Table 11 in Wright et al. (2016).

Trusts are a type of advisory service, established by the family business owner, that allow assets (shares) to be transferred to the trustees. The relationship of trustees with the family firm is a complex one that could be subject to divided loyalties. The trustees should have a very good relationship with the board of directors, having been appointed by the owner and CEO; at the same time they should have a strong relationship with the beneficiaries whose interests they must uphold; and finally, as shareholders with associated legal liability,³² they have their own reputation and that of their employers to protect and uphold. It is therefore possible that, for example, if reputation is the most important factor then the trustees may become risk-averse, discouraging what they see as risky projects that require capital expenditure, and this may have a negative impact on R&D and ultimately overall firm performance.

32. The liability of trustees in the UK can be protected through indemnity insurance (either personal or professional).

6 Conclusions and key recommendations

Some of the most interesting findings from this research on entrepreneurship and innovation in family businesses are:

- **Firms that prioritise non-family goals** tend to be more entrepreneurial.
- **Firms with boards with more non-family members** are more entrepreneurial.
- **Firms with women on the board** are more profitable.
- **Family firms with a family CEO** are more entrepreneurial.
- **The firm EO and the family EO are strongly related to each other** and both have a positive influence on family firm performance.
- **Firms with trustees** may be associated with lower performance (ROCE).
- **Firms with operations boards** do not in the majority discuss innovation at their meetings.

Key recommendations for family firms regarding entrepreneurship and innovation

Governance

- **Make greater use of operations boards to generate ideas and proposals for innovation**, capitalising on their deep “on the ground” knowledge. Family firms can devolve entrepreneurial activity to the operations board but at the same time oversee its compatibility with the overall goals of the business through main board monitoring.
- **Appoint non-family directors to the main board to increase entrepreneurial activity.** Non-family directors can be most important when the firm is growing. They bring new ideas, skills and a new network of contacts.

“ **What we have today is a board that ... challenges, but they support an effective way of formalising the relationship between myself as CEO and my father.** ”

Gilad Tiefenbrun, CEO, Linn Products

- **Develop ownership structures that are effective for entrepreneurship and innovation while protecting the stability of family ownership.** For example, giving key non-family employees shares or share options (or equity-related substitutes), or consolidating diverse shareholdings can facilitate entrepreneurial and innovative decision-making by those more actively involved in the business.

“ **The only two directors are myself and our Finance Director, who has a share option in the company.** ”

Peter Shipp, CEO, EYMS Group

Non-family employees

- **Promote communication about innovation throughout the company.** For example, this could involve (as at EYMS Group, Case study 3) communication and regular topic-focused meetings between the senior management team and the CEO.

“ **We don’t have an innovation board. We favour having specific meetings involving all the people concerned in the area we are looking at.** ”

Peter Shipp, CEO, EYMS Group

- **Recruit, develop and incentivise non-family employees to be more innovative and entrepreneurial,** consistent with the goals of the business. Non-family employees often have deep insights into the business and emerging market developments, which can be harnessed to foster entrepreneurial activities.

“ **We see our staff as the most important part of who we are – we wish to be known for their ability and passion. We actively support training and development, and have Investors in People. We have many long-serving members of staff – it is something we are very proud of.** ”

Nick Howarth, CEO, Howarth Timber

“ **Innovation is continuous ... everyone can understand the company values and that allows the engineers to innovate from a grass-roots level.** ”

Gilad Tiefenbrun, CEO, Linn Products

Next-generation family members

- **Involve the next generation in the business, giving them space and encouragement to foster entrepreneurial developments** to enhance the business. The next generation may have identified potentially profitable opportunities from their experiences working inside or outside the family firm. These opportunities may involve either developing the core family business or creating ventures in new areas under the umbrella of the family firm. Pursuing these activities can be an invaluable training ground for when their turn comes to take over the reins.

“ **He [the son] is now working here as our group performance/development manager ... he has a wide-ranging job description ... and can get involved in anything really ... he has the advantage of not having line management responsibility and is able to take time to look at business development and other areas.** ”

Peter Shipp, CEO, EYMS Group

- **Consider candidates for family CEO (or family management)** who have the skills needed to champion entrepreneurship and innovation activities within the family firm. Distinguish the management role from the championing role when considering how to best organise entrepreneurship and innovation projects. The two roles may require different skills and it may be important for a family member to take the championing role if there is a need to overcome resistance to innovation from the family.

Strategy

- **Stimulate the risk propensity of the family** in order to develop a fit between the family owners' commitment and the firm's strategic, structural and tactical decisions around entrepreneurship and innovation in order to build competitive advantage. This could be achieved through stimulation of key individuals or groups, either internally by freeing up management to allow time for creative thinking and experimentation, or externally by exposure to selective networks with competitors, policy-makers (government), professional membership groups and educational establishments.
- **Consider making greater use of ring-fenced subsidiaries** to reduce the risks associated with more radical innovations. This can be an opportunity to pursue risky new ventures, perhaps led by the next generation, which may or may not be successful. If they are ring-fenced from the core business it is easier to avoid escalating commitment to them, which may be detrimental to the core business, and to terminate them if they prove not to be successful.

“ Faced with a family business that's got stability, security, don't bet the farm ... so [in Byotrol] we have a small PLC which is divorced [from the main group]. We spun it out – [in this case] the right thing to do with innovation. ”

Stephen Falder, brother of CEO John Falder, HMG Paints

7 Actions to consider

Embedding entrepreneurship and innovation

Family businesses need to consider ways in which they can develop entrepreneurship and innovation:

- Do you give enough priority to entrepreneurship and innovation?
- How can you embed entrepreneurship and innovation in your firm?
- Are you clear about the kind of entrepreneurship and innovation that you need to undertake (radical, process, etc.) and what different expertise you need?
- Do you have a strategy and process for undertaking entrepreneurship and innovation in a structured and timely way?
- How does the history and tradition of your family and/or your firm influence entrepreneurship and innovation?
- How can the next generation can be prepared and encouraged to be entrepreneurial and innovative?
- Do you need to consolidate diverse ownership in order to focus your firm's ability to make entrepreneurial and innovative decisions?
- Would the creation of a trust maintain family ownership stability and facilitate entrepreneurial and innovative decision-making?

Add your own questions...

Enabling entrepreneurship and innovation

Family businesses need to consider ways in which they can access the expertise to enable them to implement their entrepreneurship and innovation strategies:

- Who needs to be involved in entrepreneurship and innovation?
- Do you have sufficient family commitment to support entrepreneurship and innovation?
- Do the existing structures and processes in the firm support entrepreneurship and innovation?
- Are you making full use of the expertise of non-family employees in entrepreneurship and innovation?

- Do you need to recruit additional expertise at board and management level?
- To what extent is the board involved in fostering entrepreneurship and innovation?
- Does the formulation of strategy involve the identification of opportunities and the taking of entrepreneurial decisions?
- Does the board comprise members able to monitor and support driving entrepreneurship and innovation?
- What EO practices/mechanisms from both successful and less successful businesses can you put in place?
- Should you have an operations (or management) board to support entrepreneurship and innovation?
- To what extent should the family council, the family office, and/or the trustees be involved in supporting entrepreneurship and innovation?

Add your own questions...

Evaluating and managing the risks in entrepreneurship and innovation

Family businesses need to consider ways in which they can evaluate and manage the risks associated with entrepreneurship and innovation:

- Does entrepreneurship and innovation align with the family goals and not just business goals?
- Do you have a process for monitoring entrepreneurship and innovation in a structured way?
- How do you measure the success (or failure) of entrepreneurship and innovation?
- How might entrepreneurial and innovative activities be ring-fenced from the main business?
- How should you address challenges when entrepreneurial and innovative activities by family members are not deemed successful?

Add your own questions...

Appendix: Glossary of terms

- Board (or main board)** The board of directors is an elected group of people including the CEO, the chairman and other directors (executive and non-executive). Its function is to oversee the direction and strategy of the business.
- Commitment** The disposition of family owners to engage in distinctive entrepreneurial and innovative behaviour based on the goals, intentions and motivations that drive these owners to influence the firm's behaviour in directions diverging from those of non-family firms or the institutional norms among family firms.
- Decision-making authority** Family owners' power to direct, allocate or dispose of a firm's resources. It includes latitude and discretion in selecting the goals of the organisation and in choosing among a range of feasible strategic, structural and tactical options.
- Entrepreneurship** Actions taken by the firm and its managers to identify and pursue opportunities to generate new wealth for the business.
- Family council** A forum for communication among family members that typically meets once or twice a year. The family council helps family members understand each other's expectations about the current and future management and ownership of the family business.
- Family EO** The entrepreneurial mindset, attitude and goals of the family. Family EO deals with behaviours geared towards expressing the wider attitudes and mindset of the family. These typically include its own view of risk-taking, innovativeness and proactiveness, but are also about security and control (of family assets), stability (versus growth and a willingness to change) and long-term view (preserving the firm for the long term, being conscious about the next generation).
- Family office** An investment, liquidity management and administrative centre for affluent individuals or families.
- Firm EO** The methods, practices and decision-making styles managers use to act entrepreneurially. Firm EO consists of risk-taking, innovativeness and proactiveness. It relates to the behaviours of the firm itself and how risk-taking, innovativeness and proactiveness are present in strategic decisions, the management of resource availability and how the firm is developed over time.
- Innovation** Innovation generally comes in two forms: radical innovation, which is the creation of a "new" product or service that is materially different from existing products or services in the market-place; and incremental innovation, which is the updating of an existing product or service with additional features, and not in itself "new" to the market-place.
- Operations board** A secondary board (also termed a management board) which reports to the main board but which is primarily involved in discussing the operations of the company. Members of the operations board can include senior managers in the company responsible for functions such as operations, R&D, sales and marketing.
- Socioemotional wealth (SEW)** Non-financial aspects of the firm that meet the family's affective needs, such as identity, the ability to exercise family influence and the perpetuation of the family dynasty.
- Trusts and trustees** Trusts are a type of advisory service established by family business owners that allow assets (shares) to be transferred to appointed trustees. The trust is created as a "benefits trust" where income flows or capital gains from the company's assets are designated for the benefit of specified family members and/or employees. In the UK the main type of trust is a discretionary trust, either set up during the lifetime of the business owner (a "lifetime trust") or established under a will (a "will trust").

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The IFB Research Foundation is a charity (no. 1134085) established to foster greater knowledge and understanding of family firms and their contribution to the economy and society, as well as the key challenges and opportunities that they face.

The Foundation's vision is to be the UK's centre of excellence for family business research, and to this end its publications are designed to create a better understanding of family business for the benefit of all stakeholders. Alongside ***Family Business Research and White Papers***, providing thought leadership on key family business characteristics and issues, its work covers a broad range of publications, including:

- ***Family Business Sector Report*** – benchmarking the size and importance of the sector.
- ***Family Business Challenges*** – offering practical guidance for family business owners on a broad range of topics, including family business dynamics, governance, performance, succession and wealth management.
- ***Family Business Case Studies*** – showcasing family business exemplars.

The Foundation disseminates knowledge and best practice guidance through printed publications, online media accessible via the IFB website and other activities.

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The Foundation works closely with its sister organisation, the Institute for Family Business, which is a membership association representing the UK's family business sector. The IFB is a member of FBN International, the global network for family businesses.

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