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Staying in the game

PwC Family Business Survey 2010/11

South African edition

We've talked to more than 1,600 family-business owners and managers around the world, including 81 in South Africa, to discover how you're dealing with the economic downturn, what challenges you're facing and how you're preparing for the future.

January 2011

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Foreword

Since the release of our last Family Business Survey in 2007, businesses across the globe have encountered some of the most difficult economic conditions in living memory. We witnessed many governments around the world rushing in with financial support to save their banking systems at the start of the crisis and then implementing stimulus packages to jump-start declining economies. While South African banks were somewhat sheltered from the global storm, the lack of liquidity in international markets eventually reached our shores and resulted in the first recession since the early 1990s.

For this year's survey we talked to more than 1,600 family-business owners and managers in 35 countries, including representatives of 81 family-owned businesses in South Africa, making this survey the largest of its kind ever to be conducted. We wanted to find out how you're coping with the economic downturn, what challenges you're facing and how you're preparing for the future. This report incorporates both global and South African results to enable readers to easily benchmark their businesses against local and international peers.

Despite the macroeconomic challenges, more than 75% of South African respondents believed that being part of a family business helped them through the economic downturn. This was almost 10 percentage points more than the global average, showing a slightly different picture of the core strength of local family-owned companies compared with their international counterparts.

The responses we received during this year's survey show that a more serious mood prevails than in 2007, with most family businesses determined to keep up the effort and stay in the game despite the prevailing economic conditions. In presenting the results we aim to highlight factors that differentiate South African family businesses from their peers around the world and which locally-shared characteristics may contribute to the resilience of these businesses. In a dynamic world where change is constant only those businesses that identify their value drivers will survive and grow.

We hope that you'll find the results illuminating and that they will help you in running your business.

Andries

Andries Brink
National Leader
Private Company Services (PCS)
PwC Southern Africa

"A large proportion of PwC's business is generated by privately-owned or family-controlled entities. As such this survey also assists us to identify the issues that are of most concern to family businesses in particular and private companies in general. To us, it is not the size of your business or industry that matters most, but rather how we can create value and help you achieve your goals."

About the survey

We interviewed 1,606 owners and managers of family-owned businesses in 35 countries around the world in the course of completing our second global Family Business Survey. We contacted representatives of 81 family-owned businesses in South Africa to gain specific insights about operating a family business in this country.

We define a family business as one in which the founding family has a significant stake in the business and one or more relatives hold senior management positions.

South Africa forms part of the Emerging Markets category which also includes Brazil, Russia, Middle East, the Caribbean and Turkey.

The majority of profiled companies employ between 21 and 500 staff.

Figure 1: Survey participants: position in the company

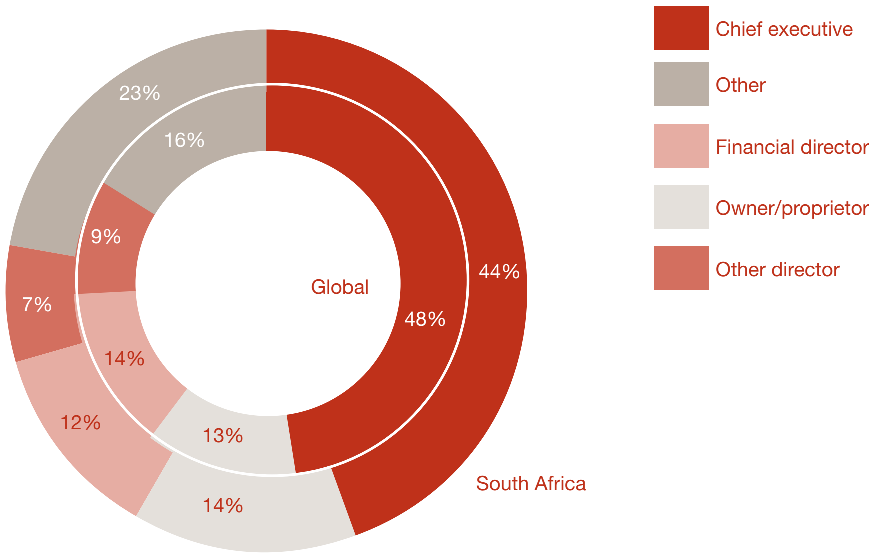
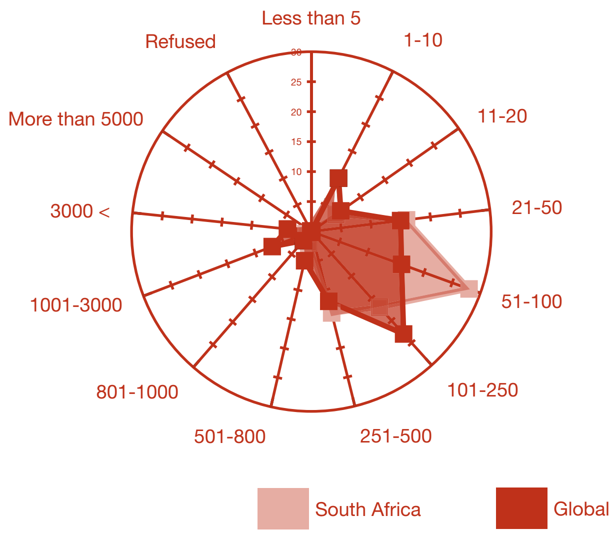


Figure 2: Respondents employee numbers



PwC's Private Company Services

A significant portion of PwC's clients are privately-owned businesses including family-owned companies. To meet their unique needs, our Private Company Services practice is dedicated to the long-term success of private companies and their owners. Our expertise in this market segment is underpinned by the surveys that we conduct to shape our understanding of the issues and needs of private companies and their owners. This enables us to deliver relevant services that unlock tangible benefits and deliver sustainable value for our clients.

Through our Trusted Business Advisors (TBAs), who work alongside family business owners, we provide advice and seek solutions on a variety of issues relating to running a successful business.

Look out for the maroon text blocks throughout this report, which contain advice and commentary from several of our South African TBAs.

What is a family business?

A family business is an enterprise in which the majority of the votes are held by the person who established or acquired the business (or by his or her spouse, parents, children or children's direct heirs); at least one representative of the family is involved in the management or administration of the business; and, where the company is listed, the person who established or acquired the business (or his or her family) possesses 25% of the voting rights through his or her share capital and at least one family member sits on the board.

Contents

Introduction to findings 8

Survey findings

– Fending off challenges and investing in the future 10

– Handing over the reins 26

– Managing family relationships 36

– Rules of the game 42

– What we've learned 48

Methodology and survey population 52

Contacts 55

References 56

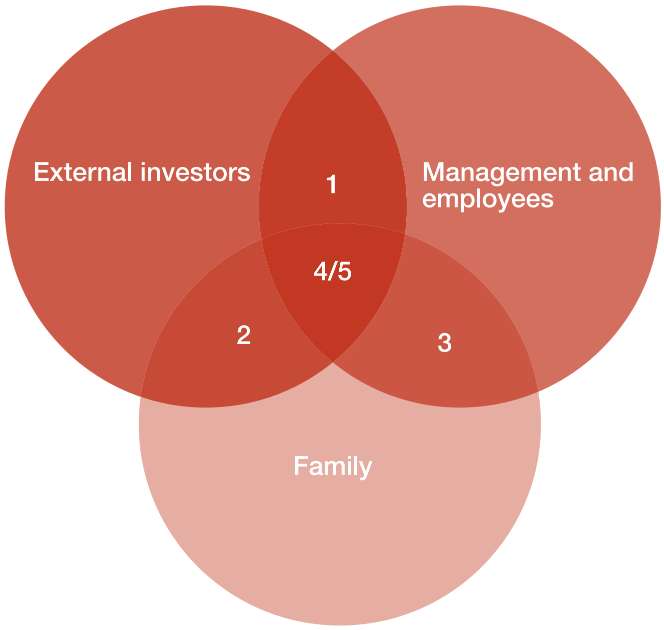
Introduction to findings

Thriving in an ever-changing world, whether these changes are due to macroeconomic issues, legislative processes or even technological advances, requires the continuous assessment of the environment in which a business operates. The comparison between business and sport is fitting when the changes that occur during a game are compared with the changes that occur in the business world. The title of our South African Family Business survey reflects this analogy. The most successful teams rely on the optimum interactions of the team as a whole, the skills of individual players and the effectiveness of their tactics to deliver winning results.

A similar concept underlies the well-known model of the family business as three overlapping circles: the company, the owners and the family (see Figure 3). The model shows the range of interests that exist, and where they intersect or diverge. It demonstrates how the perspectives of the different parties depend on where they stand within the three circles as much as they do on the personalities of the people involved.

It also illustrates how the family dynamics colour the business itself. If there's unhealthy conflict between the family members, it will spill over into the way the business is managed and owned – whether that's through disputes over money, charges of nepotism or infighting over who should head the business when it passes from one generation to the next. Conversely, if relations within the family are healthy, the business is more likely to be healthy, too. Solid, mutually supportive bonds help to encourage loyalty to the company, make people more motivated and facilitate decision making – qualities that mean the business itself is better equipped to deliver strong results.

Figure 3: Family businesses are often depicted as a set of three intersecting circles



1. Owner managers
2. Inactive or passive owners
3. Family employees
4. Working family owners
5. Family, owner and business leader(s)/'controlling owner'

The most successful family businesses are those in which there's a good balance between the three circles, with professional management, responsible business ownership and a harmonious family dynamic. Such companies tend to have clear written agreements about the composition and election of senior executives, the decisions that require a majority vote and the conditions under which family members can (or can't) work in the business. They also have robust governance procedures; bring in outside directors and managers, where necessary; and monitor the performance of relatives who are working for the business, just as they do the performance of outside directors and managers.

Ownership issues are likewise separated from family issues. The most long-lasting family businesses typically have rules about how shares can (or can't) be traded inside and outside the family, and when shares can be sold – be it to raise fresh capital for the business or to release cash for the family members. In other words, they provide solid mechanisms for ensuring the business has enough funds to grow while maintaining family control.

Lastly, in such businesses, the needs of the family itself are given due weight. When most of the family's financial resources are tied up in the company, it may be reluctant to take risks that might actually be good for the business. It may also have insufficient assets to treat all the family members fairly, regardless of whether or not they work for the company. Professional wealth management enables a family to spread its risk and manage its other investments as effectively as possible, thereby helping to preserve a healthy family dynamic.

In short, the most enduring family businesses have clear boundaries between the business, the owners and the family, with separate forums for discussion of ownership and family matters outside the boardroom. And there is separate financial provision, wherever feasible, for heirs who don't work in the business. This is particularly important when economic conditions are difficult, as they are for many companies right now.

Because of the dynamics involved in a family business, we have surveyed the following areas and have arranged the findings accordingly:

- Current activity and investment;
- Succession;
- Working with family; and
- Regulation and governance issues.

The structure of our findings:

- *Current activity and investment;*
- *Succession;*
- *Working with family; and*
- *Regulation and governance issues.*

Fending off challenges and investing in the future

We asked you to tell us about the challenges you're dealing with, and where you're investing. Nearly half the executives we spoke to said demand for their companies' products and services has grown during the past 12 months. But the recession has exacted a high price. More than a third of all respondents reported that operating profits had fallen, and more than two-thirds are worried about market conditions – up from less than half three years ago. Even so, relatively few companies have retrenched. Indeed, many plan to expand over the next 12 months.

More than two-thirds of South African respondents have business plans in place and for additional cash are dependent on bank and overdraft facilities rather than being able to use retained capital.

In terms of investing in the future, good governance and corporate and individual performance management mechanisms are becoming the norm in order to ensure consistent evaluation and reward for family members in the business. Such initiatives provide structure and transparency as well as ensuring that non-employee family members gain insight into these processes.

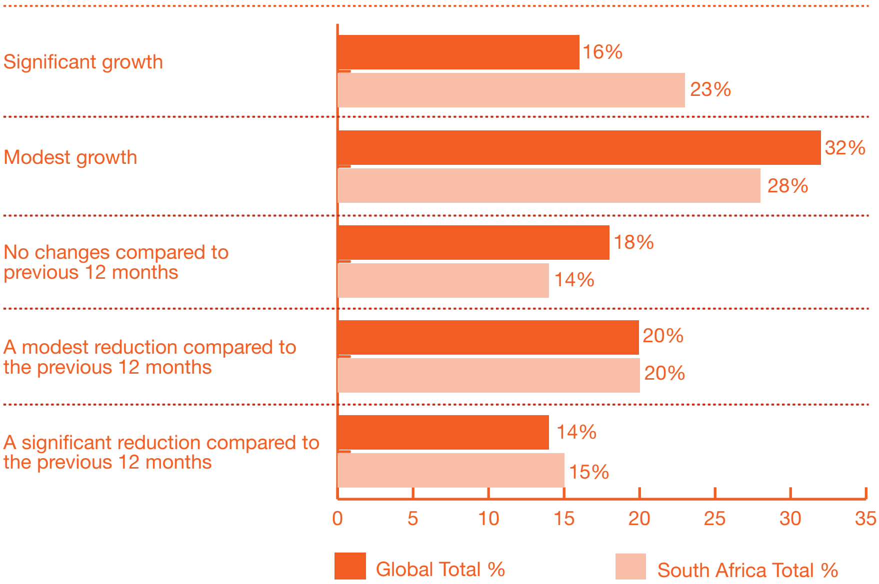
Fending off challenges and investing in the future

In 2007, when we completed our first global Family Business Survey, there were few signs of the financial crisis that was about to occur. The recession wrought carnage on numerous companies and, though the worst now seems to be over, fears of a 'double dip' remain. So how have family businesses fared during this period of economic turbulence?

Our second global Family Business Survey shows that many family businesses have prospered. Please refer to Figure 4 to see how respondents described the demand for their products and services over the past 12 months, compared to the previous 12 months.

However, the recession has certainly taken its toll. In 2007, only 10% of the companies we covered had experienced a reduction in demand for their products or services, compared to 34% surveyed in 2010.

Figure 4: A surprising number of companies have seen demand for their offerings increase during the past 12 months



"It is essential that businesses continue to focus on growth as part of their strategy."

– Abdul Essack

Fending off challenges and investing in the future

Globally, only 32% of all companies have increased their capital expenditure over the last year, compared with 50% in 2007.

In South Africa, 47% of companies increased capital expenditure. This may be attributable to the impact of the 2010 FIFA World Cup and the fact that South Africa has been less negatively affected by the global recession than many other countries.

Similarly, companies in emerging markets have done best, reflecting the speed at which these economies are expanding. Twenty-nine percent enjoyed significant growth and 50% have seen their operating profits rise, a performance that enabled 48% of them to lift their capital spending.

Figure 5: Capital expenditure has increased

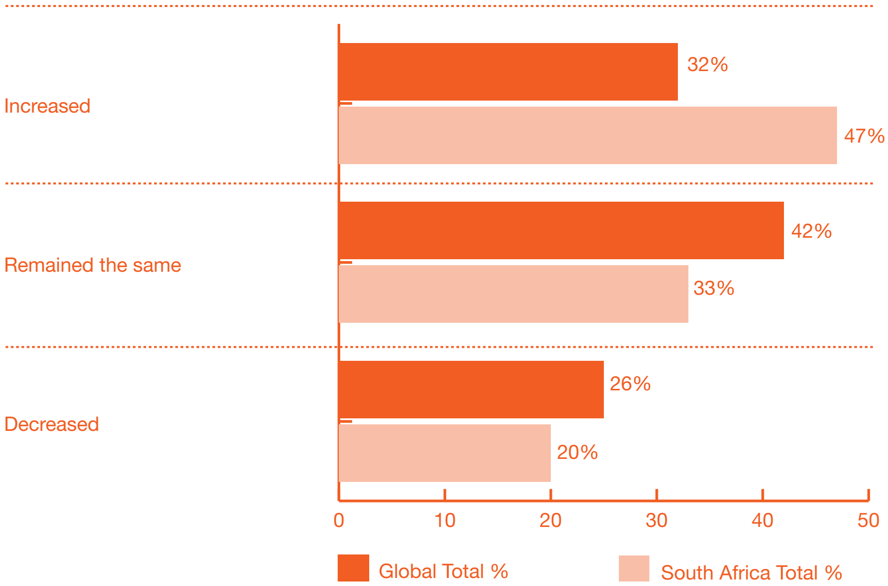
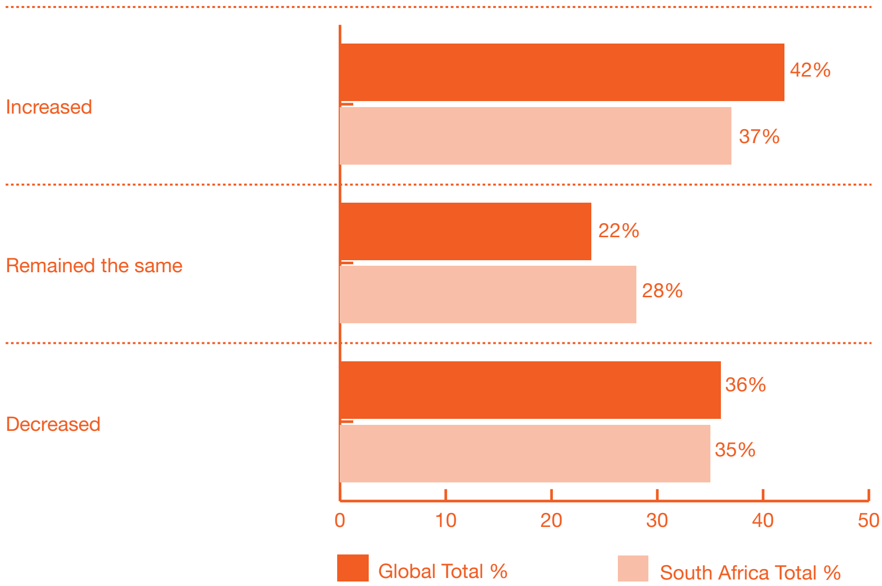


Figure 6: Operating profits up from earlier levels



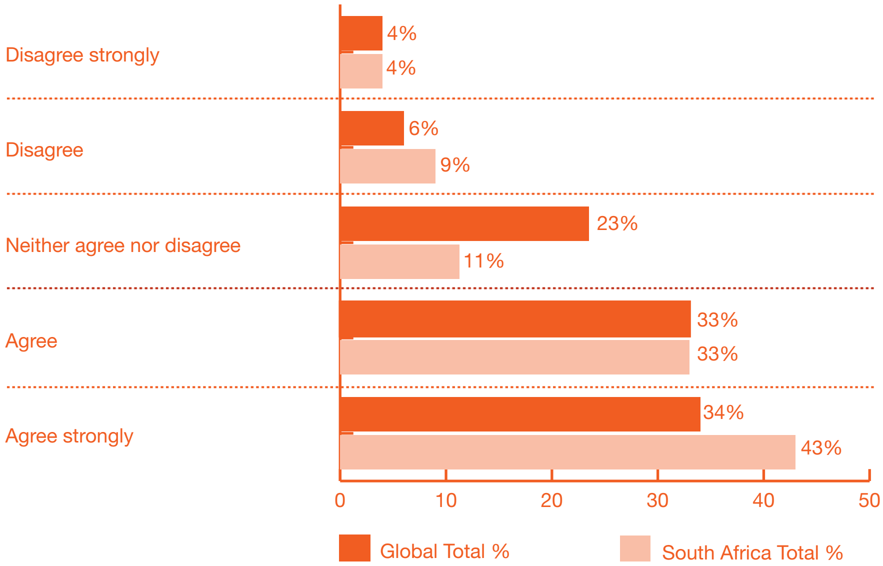
> *"The Reserve Bank rate cuts during the past 12 months should continue to ease the burden on the consumer and stimulate demand locally. Globally, rate cuts would have less of an impact on demand as interest rates are already at all-time lows."*
>
> *– Ewan Oberholzer*

Fending off challenges and investing in the future

Family businesses are better placed to take the long view than their listed counterparts because they're under less pressure to deliver quarterly results and pay dividends to shareholders. They tend to be more careful about overstretching themselves, and they're often underpinned by the values of the founding family, as opposed to being managed as purely commercial concerns. So they can weather storms that overturn larger and more aggressively managed operations.

This may be the reason why two-thirds of the people we spoke to believe that being part of a family business has helped them cope with the recession (see Figure 7). It may also explain why many of them are relatively confident about the future.

Figure 7: Most executives believe that being part of a family business has helped them cope with the economic slump



> *"Family businesses are able to adjust their equity requirements more quickly and use family resources to fund short-term capital. Values driven families are more focused on long-term and sustainable success than on meeting short-term financial targets."*
>
> *– Tom Blok*

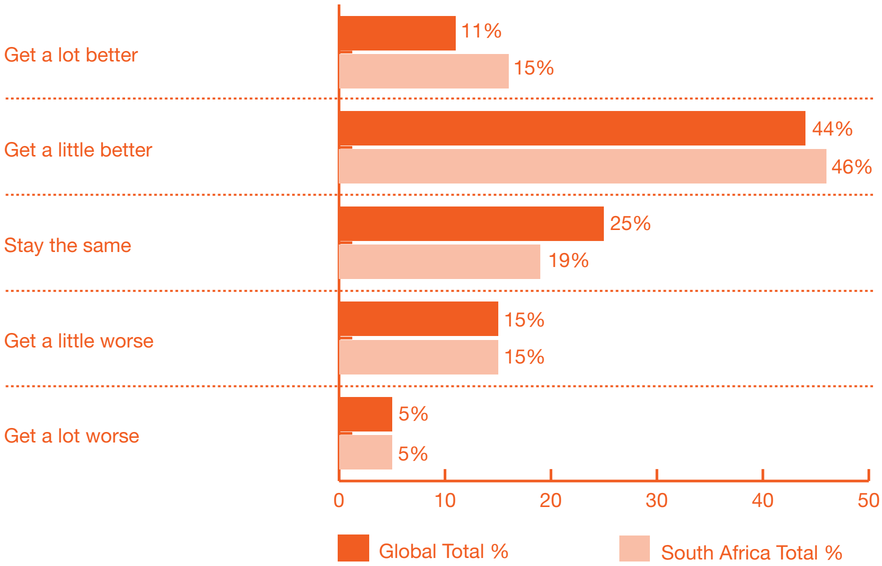
Fending off challenges and investing in the future

Most family businesses are positive about how the markets in which they do business will perform over the next year, which is broadly in line with the situation in 2007 (see Figure 8).

It is not surprising that most respondents expect a more positive outlook coming out of rather difficult conditions. The majority are probably cautiously optimistic and this is understandable in the context of the extended period (since the early nineties) of growth enjoyed internationally and locally. Where the global economy was driven largely by demand coming from the US consumer, the recent economic crisis has hurt the US consumer more than others and hence has left a void.

The question we should consider, and only the future will provide the answer, is to what extent alternative investment will replace the gap left by the US consumer?

Figure 8: Many people are positive about the immediate outlook

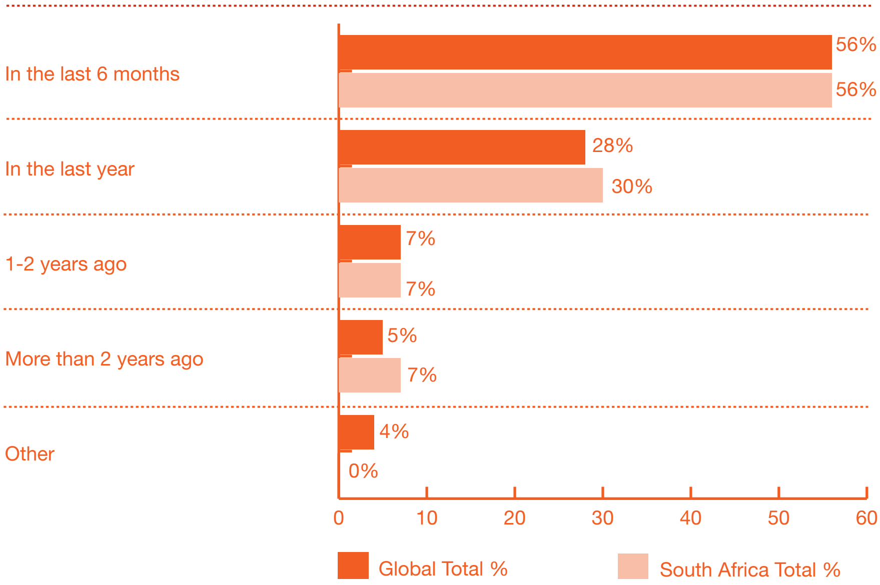


> *"Now is the time to be on top of the performance matrix to take charge of opportunities."*
>
> *– James du Preez*

Fending off challenges and investing in the future

Many of the family businesses in our survey claim they have both a business strategy and enough financial resources to capitalise on any opportunities that emerge. Most have business plans, and the vast majority of these companies have reviewed or updated their plans within the past 12 months (see Figure 9). Local companies are particularly well-prepared with 86% having proper business strategies in place.

Figure 9: Most companies with business plans have recently reviewed them



> *"Agility is the name of the game in this changing world and I know that issues regarding strategic direction cause the most tension internally when decisions about the future direction of the business are made."*
>
> *– Danie Fölscher*

Fending off challenges and investing in the future

In South Africa, many executives clearly envisage returning to 'business as before'. Only 16% have made significant changes to their business models over the past 12 months, while 22% percent have made minor modifications and 62% have left their business models untouched (see Figure 10). Ironically, family-business owners based in emerging markets are the most likely to have made major changes, whereas those based in North America – where the financial crisis originated – are more likely to have made tweaks. A substantial 58% of respondents also expect to keep using the same business models in future, regardless of the upheaval the crisis has caused (see Figure 11).

Figure 10: Most companies haven't changed their business models

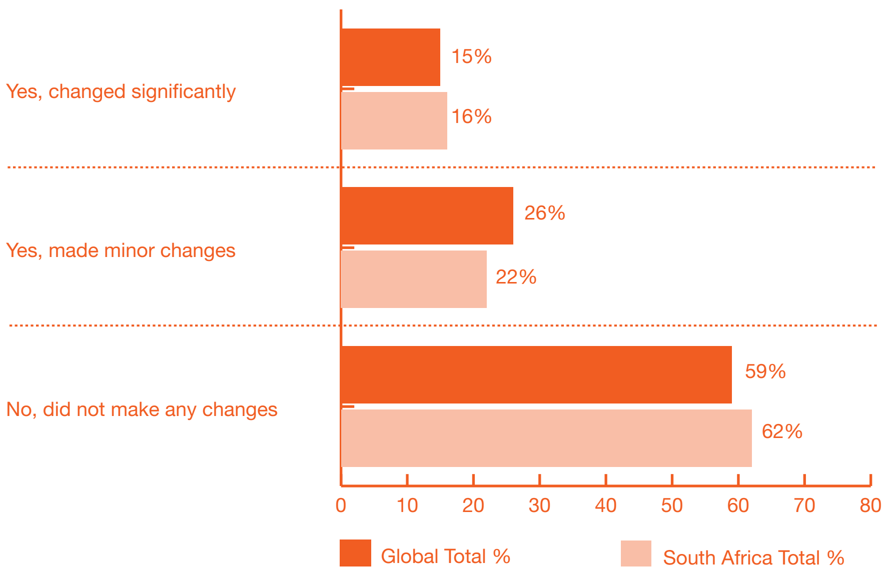
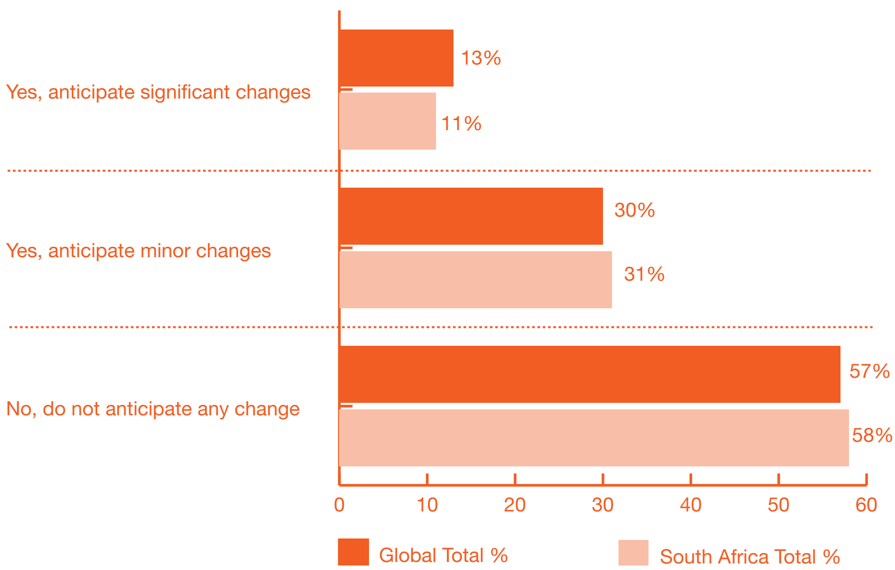


Figure 11: Most executives do not plan to change their business models in the near future



> *"Very few business models have changed as a result of the cautious approach taken by families. Focus has, however, been given to ensuring optimal efficiencies within existing structures."*
>
> *– Emsia Kruger*

Fending off challenges and investing in the future

What's more, even though two-thirds of respondents told us their companies have access to additional cash, closer examination shows that the vast majority of them would have to borrow the funds. Only 15% could manage their short-term financing needs via invoice discounting (i.e. getting faster access to income they've already earned but haven't yet been paid). The rest would have to resort to overdrafts, bank loans and other forms of debt or simply don't know how they would raise the capital (see Figure 12).

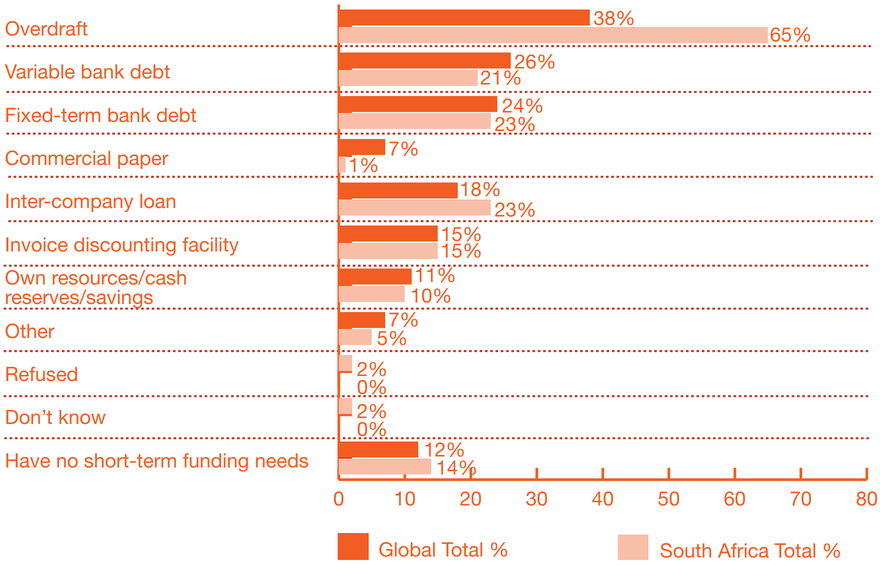
The extent to which South African respondents' use of an overdraft exceeds that of their global counterparts may in part be explained by a difference in terminology and financial products. Commercial working capital funding would typically be accessed via different forms of variable rate debt. In the South African context, overdraft facilities are generally utilised.

However, some businesses may find it harder than they expect to get credit. Under the new Basel III Accord designed to strengthen the financial services sector, the amount of capital banks are required to hold will rise from 2% of their loans and investments to 7%. The agreement, which is due to take effect in 2013 and be phased in over several years, is widely expected to drive up the price of credit and reduce the amount that's available[1]. The many family businesses that have never previously been burdened with debt facilities and covenant restrictions will also have another set of stakeholders to manage, as well as facing new pressures which could compound any existing business environmental strains.

"The banks are making it more difficult to get loans these days"

– Cypriot executive

Figure 12: Most companies would have to borrow money if they needed additional short-term cash



"Financing of growth and ongoing operations will remain a key strategic driver for family businesses as we foresee that access to funding could become increasingly difficult to obtain."

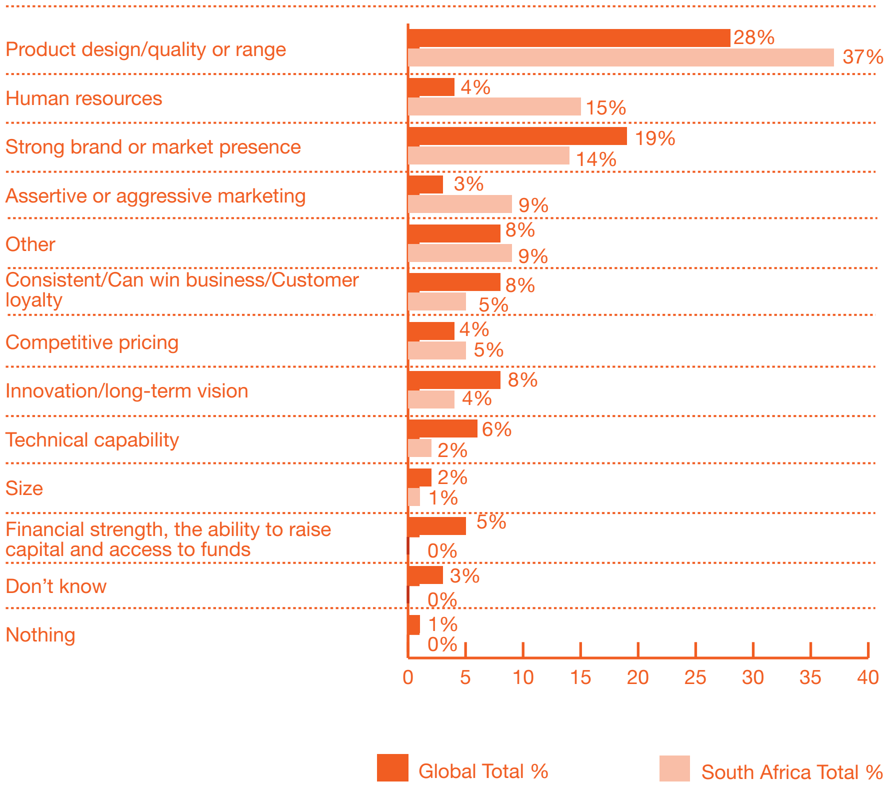
– Lynne Loots

Fending off challenges and investing in the future

Yet, despite these difficulties, 95% of family-business managers are somewhat or very confident that their companies can compete effectively with the market leaders in their sector. They're particularly confident about the design and quality of their products and the strength of their brands – the same traits they saw as key competitive advantages three years ago. But they now place more weight on product quality and branding than on customer loyalty, recognising that differentiation is critical in an era of lower consumer spending (see Figure 13).

> *"We have a very strong image in the market, we are very trustworthy and our brand is strong"*
>
> *– Finnish executive*

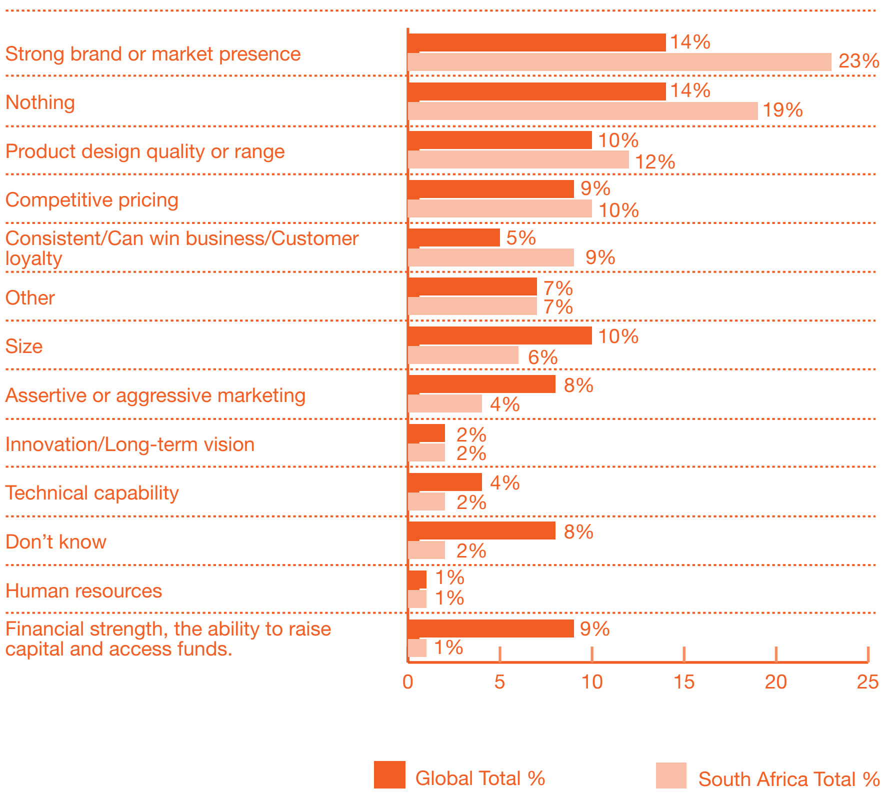
Figure 13: Product design and branding are key strengths



Most family-business managers are more grudging about praising their rivals. Although some of them admire the strong brands, product quality and size of their competitors, they're much more reserved about doing so than they are about expressing confidence in their own skills (see Figure 14).

Perspectives also vary slightly by region. Executives in the mature markets are more likely to think their companies are very innovative and to admire large competitors. Executives in South Africa, by contrast, are more likely to pride themselves on the quality of their staff and to praise their rivals' market presence and product range.

Figure 14: Strengths admired in competitors



But the power of the competition preys much less on the minds of respondents than it did in 2007, when 39% cited it as one of the top three external challenges they faced. Today, only 26% are concerned about losing out to competitors, whereas 69% in South Africa are worried about market conditions (other than competition) – up from 32% three years ago (see Table 1). For all their professed optimism about the prospects for growth, many family business owners and managers are obviously very nervous about the economy. Government policy (including regulation, legislation and public spending) also keeps some people awake at night. Most proprietors want a stable regime with a clearly defined five-year fiscal and monetary policy that will enable them to plan ahead.

Comparing the top issues from the previous survey results with the top issues from the current results reveals some change (Table 1). Looking at the current levels of the top issues compared with their levels from the last survey provides interesting comparison and food for thought.

The most prominent external challenge are market conditions, which in South Africa's case more than doubled in terms of response compared to the previous survey results. It is therefore clear that market conditions i.e. the economic environment, labour market, the ability to raise finance and the cost of finance, consumer behaviours and human capital issues remains key to the success of a family business.

Table 1: Key external challenges

	South Africa 2010	South Africa 2007	Mature markets 2010	Mature markets 2007	Emerging markets 2010	Emerging markets 2007
Market conditions	69%	32%	67%	44%	69%	37%
Competition	22%	28%	26%	39%	27%	38%
Government policy	25%	33%	24%	33%	31%	42%
Currency/exchange rates	24%	29%	15%	14%	20%	32%

"Taking into account the comments made in PwC's 13th Annual Global CEO Survey, which highlighted opposing views about changes in consumer behaviour, it remains difficult to see where the market is heading. What is interesting about the results shown here is that since growth in global demand is generally not expected to come from the US consumer, larger corporates' focus will inevitably shift to emerging markets and I expect competition to increase in the emerging markets when we see a global economic upturn."

– Brendan Deegan

Fending off challenges and investing in the future

Many of the executives we spoke to are likewise concerned about various internal challenges, although the order they rank them in has changed over the past three years.

Labour was the biggest source of unease in 2007 as well – and evidence, perhaps, that family businesses should promote differentiating factors like their business values and long-term perspective more actively in the battle for brains.

Managing cash flows and controlling costs has also increased in importance.

Table 2: Key internal challenges

	South Africa 2010	Mature markets 2010	Emerging markets 2010
Skilled labour shortage	54%	34%	54%
Cash flow and cost control	19%	32%	21%
Raw materials, price, quality and supply	19%	12%	12%
Capacity and ability to meet orders	15%	24%	18%
Finance and availability of funds	11%	12%	13%
Corporate reorganisation	10%	29%	29%

"Access to the right skills and cash flow remain the two key challenges that family businesses continue to face. In fact, these are the same for all South African businesses regardless of size, industry or market segment."

– Frans Weilbach

Fending off challenges and investing in the future

There are also some notable regional variations in the anxiety executives express. Executives in the mature markets are much less worried about labour issues and government policy than those in the emerging markets, for example. Conversely, they're much more concerned about managing costs and cash flows (see Table 2). This helps to explain why barely two-thirds of respondents from the mature markets intend to invest in human resources and training over the next 12 months, compared with more than four-fifths of their peers in the growth economies (see Table 3).

Table 3: Top five investment areas per region

	South Africa	Mature markets	Emerging markets
Human resources and training	75%	64%	81%
Marketing	68%	58%	67%
Sales activity	62%	61%	66%
Management & governance structure	49%	27%	57%
IT infrastructure	47%	51%	58%

> *"We're worried about the persistent influence of the financial crisis on consumer behaviour"*
>
> *– Austrian executive*

Fending off challenges and investing in the future

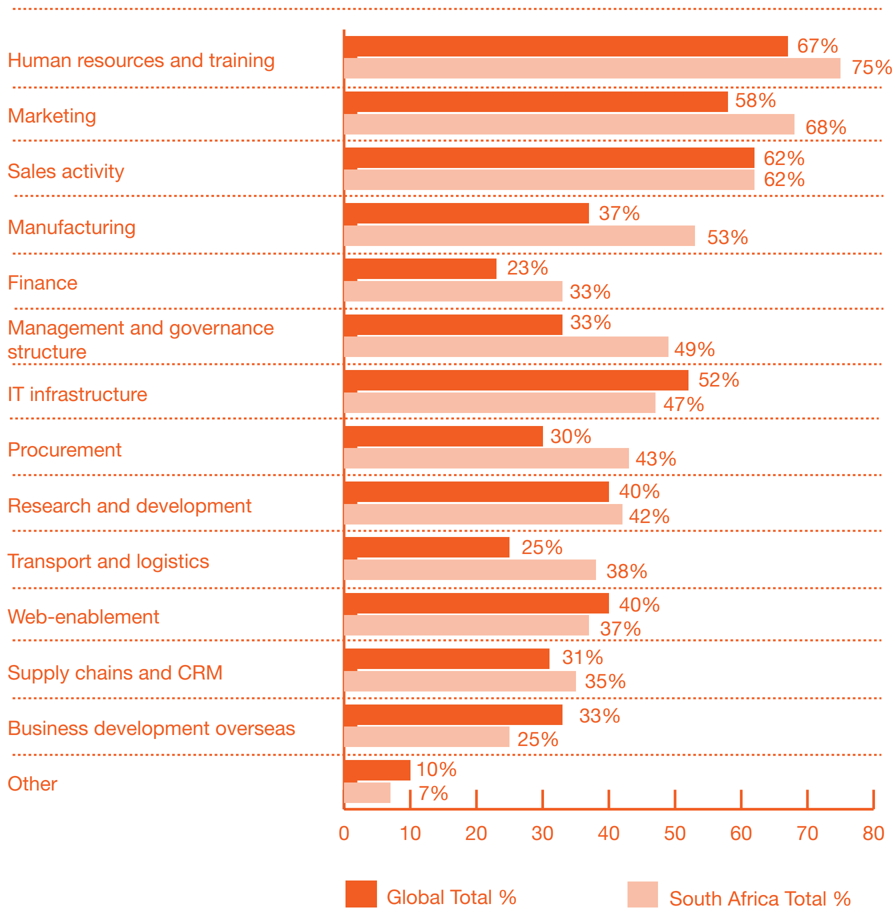
"Clients don't pay on time and it causes cash flow problems"

– Maltese respondent

Their investment plans reflect these anxieties. Sixty-seven percent of the family businesses in our sample intend to invest in human resources or training over the next 12 months (see Figure 15). This is only marginally less than the 73% that planned to do so in 2007 and a sign of the importance they attribute to the human factor.

However, comparing the results with those from three years ago reveals several significant changes. First, the number of companies (particularly smaller companies) planning to invest in each area is lower than it was before, suggesting that many businesses have had to rein in their spending. And, second, they're mainly economising on IT, management and governance, the supply chain, transport and logistics, and finance. While some companies may now have robust IT infrastructures, management, governance and finance are ongoing concerns.

Figure 15: Human resources, sales and marketing head the investment agenda



"It is clear that family business owners are very aware of the importance of a successful business being underpinned by a sound corporate governance environment. It is therefore not surprising that many family business are considering practical ways of implementing the principles of King III in their business."

– Andries Brink

Fending off challenges and investing in the future

It is not surprising, due to South Africa's geographical location, to note that 64% (see figure 16) of South African respondents export to Africa. What is perhaps a bit more difficult to explain is why 56% (see figure 17) said they have no plans to expand operations into Africa.

There may be a number of factors that explain why there is a reluctance to expand into Africa. Each of these whether bureaucratic red tape, unstable currencies, political uncertainties, lack of infrastructure, language barriers or indeed any other issue businesses have to deal with, increases uncertainty. High levels of uncertainty increase risk and we know that at the core of investment decision making the question is always the same: Does the return compensate the investor for the risk being taken? If the answer is no, then very little expansion will take place. However, it does not necessarily mean that expansion of operations in Africa should not be on the agenda as there may be other avenues that can be explored to reduce risk and make profitable investment in Africa a reality.

Figure 16: The countries with which companies that export goods or services trade

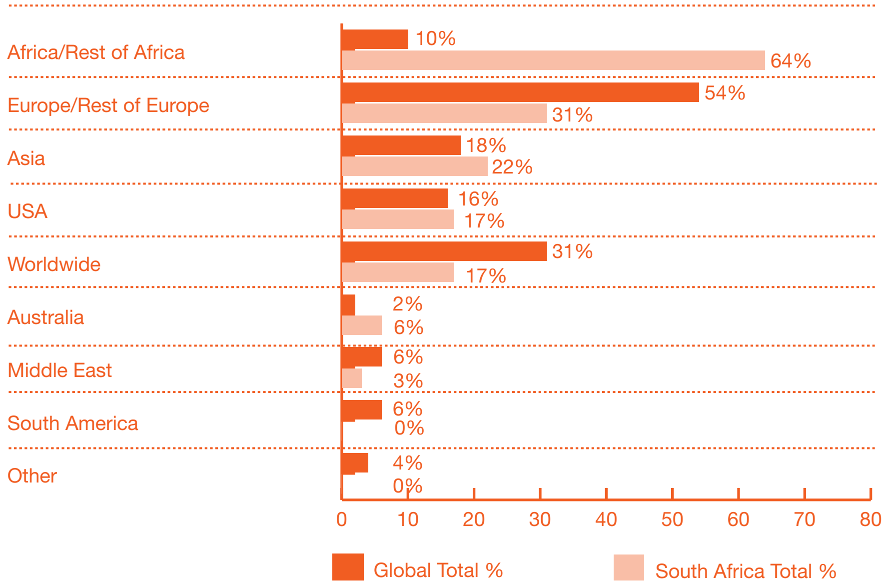
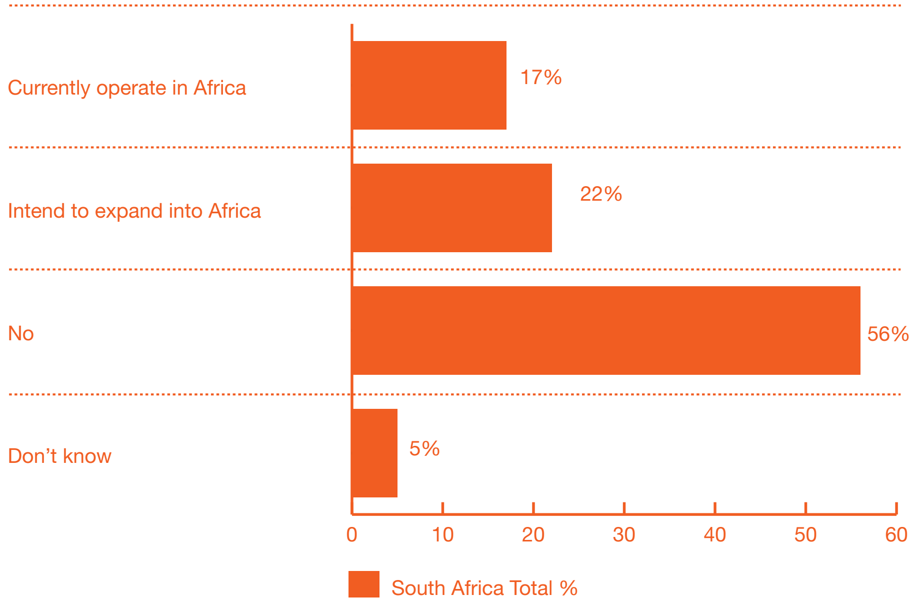


Figure 17: Expanding operations into Africa is not a priority for more than half of local companies surveyed



Fending off challenges and investing in the future

A number of avenues to be explored include linking up in partnerships with local operators, initially using South African expatriates who understand the local conditions as operators, and investigating governments' (both local and foreign) export and investment incentives.

Handing over the reins

We invited you to tell us how you're handling succession planning and ownership issues, and how you believe senior management should be rewarded. More than a quarter of the family businesses in our survey – rising to more than a third in the emerging markets – are likely to change hands during the next five years, and more than half of these companies are expected to stay in the family. However, almost half of the companies in our sample don't have a succession plan, and only half of those that do have designated a specific individual to take over the top job.

Managing ownership of the business and other family assets equitably is almost equally challenging. Only 60% of proprietors think they have enough resources to divide their assets fairly between all their heirs, including relatives who don't work for the company. A significant number have also failed to make any provision for dealing with family and business issues, if key personnel or shareholders should get ill or die, or to assess their potential tax liabilities. But most proprietors recognise the value of good management and believe the best way of retaining senior executives is to pay them well. They put much less emphasis on new challenges, career progression and work-life balance, an attitude they may need to change as Generations X and Y rise up the ladder.

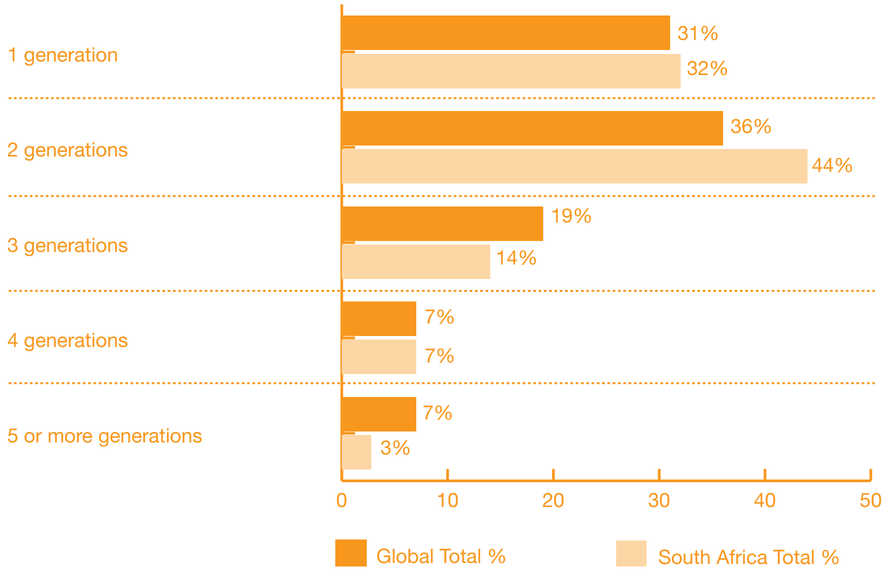
Handing over the reins

It's widely recognised that one of the biggest risks facing any family-owned business is the transition from one generation to the next. The Family Firm Institute estimates that only 30% of US family businesses survive the shift to the second generation, only 12% are still viable in the third generation and only 3% make it to the fourth generation or beyond[2]. Our research bears this out.

Of course, some family businesses are effectively 'lifestyle' businesses. If they've provided a comfortable income for the founder and his or her dependents, they've arguably served their purpose. But others generate a considerable amount of the world's wealth; indeed, some reports suggest that family businesses collectively create between 70% and 90% of global GDP per year[3]. The death of such companies is therefore a loss to the community at large.

So, what accounts for the high attrition rate? In some cases, the founder's simply too caught up in the day-to-day activities of running the business to plan for the future. But many entrepreneurs are also reluctant to cede control. The passion that drove them to set up their companies in the first place prevents them from stepping back from the helm. Selecting a successor can also be an extremely emotive issue. If more than one relative is interested in taking over the business, for example, it may be difficult to choose the best candidate without offending other family members.

Figure 18: Most of the family businesses in our survey have only existed for one or two generations



> *"The importance of having a well-defined executive organisational structure with clearly articulated roles and responsibilities is essential to ensuring proper succession planning and the development of the requisite skills of family members."*
>
> *– Gert Nel*

Handing over the reins

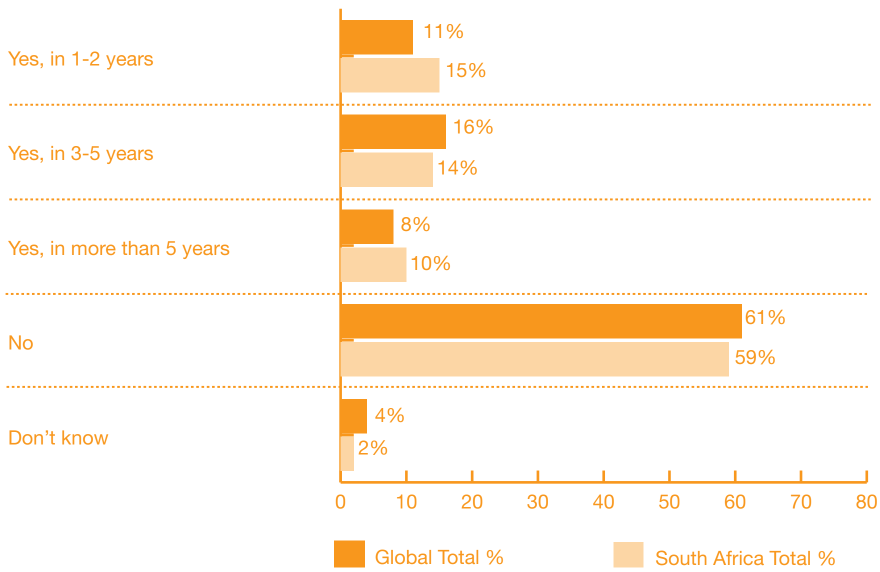
Yet careful planning is essential to ensure a smooth transition. As we noted in our previous survey, a good succession plan outlines how the succession will occur and what criteria will be used to judge when the successor is ready to take on the task. It eases the founder's concerns about handing over to someone else and encourages the heirs to work in the business, rather than embarking on alternative careers. And it endeavours to provide what's best for the business, recognising that competence is more important than family connections.

Twenty-seven percent of the companies in our sample – rising to 29% in South Africa – are expected to change hands within the next five years (see Figure 19). This is a similar percentage to that recorded in 2007, suggesting that the recession may well have delayed or derailed many succession and sale plans over the past few years. And over half of the people who anticipate a change of ownership think the business will remain in the family (see Figure 20). The older the company, the more likely this is; 66% of proprietors running businesses that have been trading for more than 50 years plan to pass the wheel to their offspring, compared with just 35% of those running businesses that have been trading for less than 20 years. This is consistent with the picture in 2007.

"To protect the value you have created, you should have a definitive exit strategy."

– Tom Blok

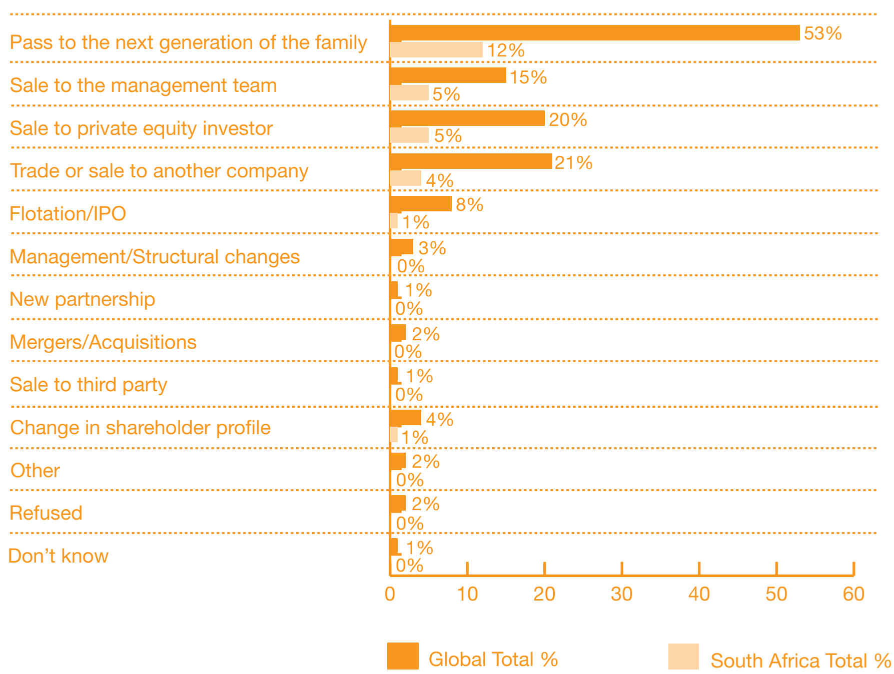
Figure 19: More than a quarter of companies are expected to change hands within the next five years



"It's a great responsibility to take over a family business, and it's important to keep the peace between the family members"

– Norwegian executive

Figure 20: Most of those that expect the company to change hands over the next five years expect the business to remain in the family



Handing over the reins

Also similar to the results in 2007 is the fact that nearly half the companies we surveyed don't have a succession plan, although larger companies are generally more prepared for the transition than smaller ones; 61% have some sort of plan in place (see Figure 21).

There's certainly a pressing need for better planning, even in many of the companies that have drawn up a succession plan. Sixty-eight percent of the executives who say they've prepared for the changeover expect family members to assume one or more of the senior management positions in the business, although 11% – rising to 34% in North America – intend to bypass their families altogether (see Figure 22). But only 50% have actually designated a specific individual to take over the top job, and the percentage is even lower in the emerging markets (43%).

Figure 21: More than a third of South African companies have no succession plan

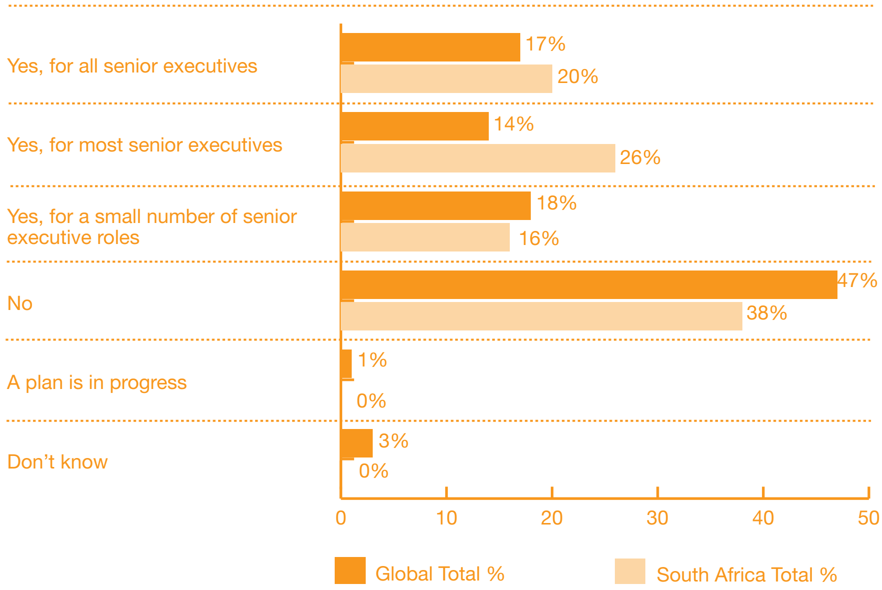
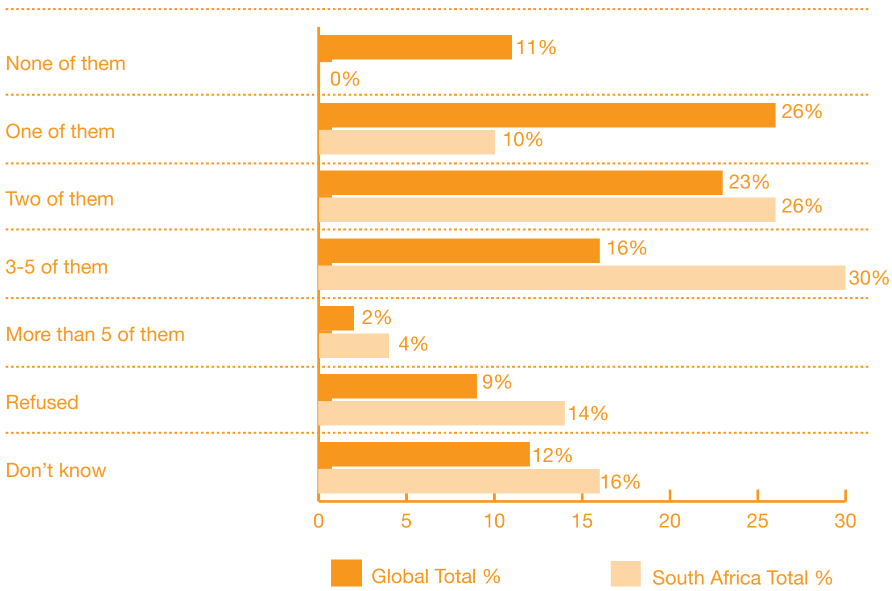


Figure 22: In most companies with succession plans family members are expected to assume at least one of the key roles



"My greatest desire is to guide the company through the current economic crisis and then hand it onto the next generation"

– Swedish executive

Handing over the reins

Moreover, some families have seen their wealth significantly eroded during the economic downturn. Globally, only 62% of respondents think they have sufficient resources to divide their assets fairly between all their heirs, including those who don't work for the business (see Figure 23). In South Africa, this figure stands at 80%. Conflicts over money could therefore compound any disagreements about which relative should succeed to the throne.

Further evidence that some family businesses may be less ready for the future than they realise comes from the fact that 35% haven't made any provision for dealing with family and business issues, should a key manager or shareholder get seriously sick or die (see Figure 24). In South Africa, 15% of respondents are in this position.

Many family businesses would face considerable difficulties if any sudden change of ownership occurred, regardless of the cause.

Figure 23: Equitable division of assets is a problem for many proprietors

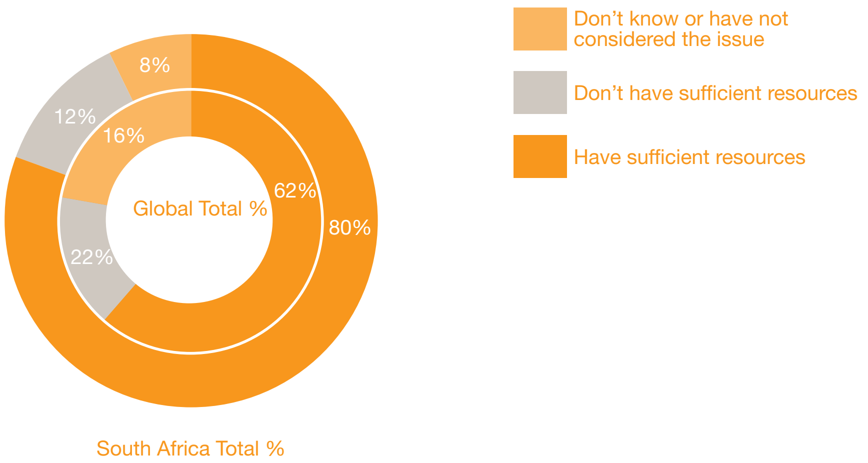


Figure 24: Many companies haven't prepared for the sickness or death of a key manager or shareholder

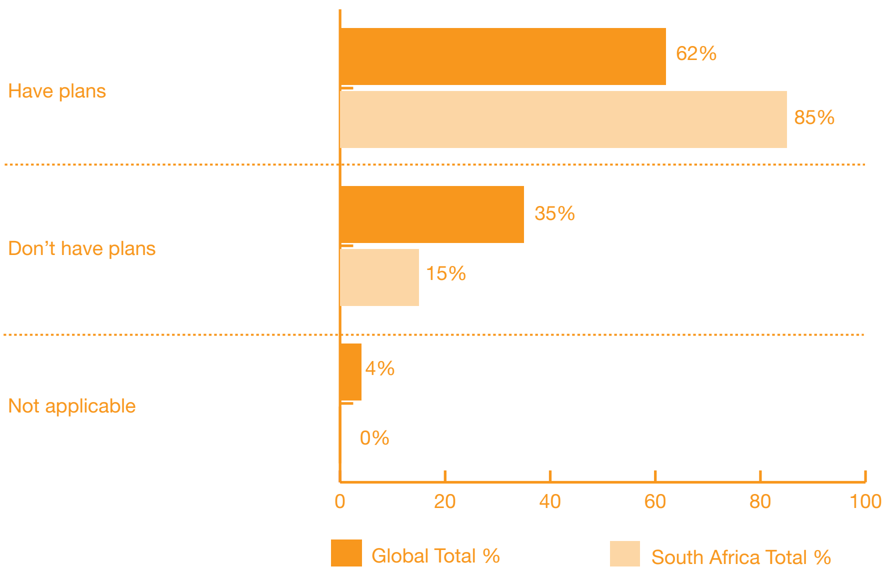
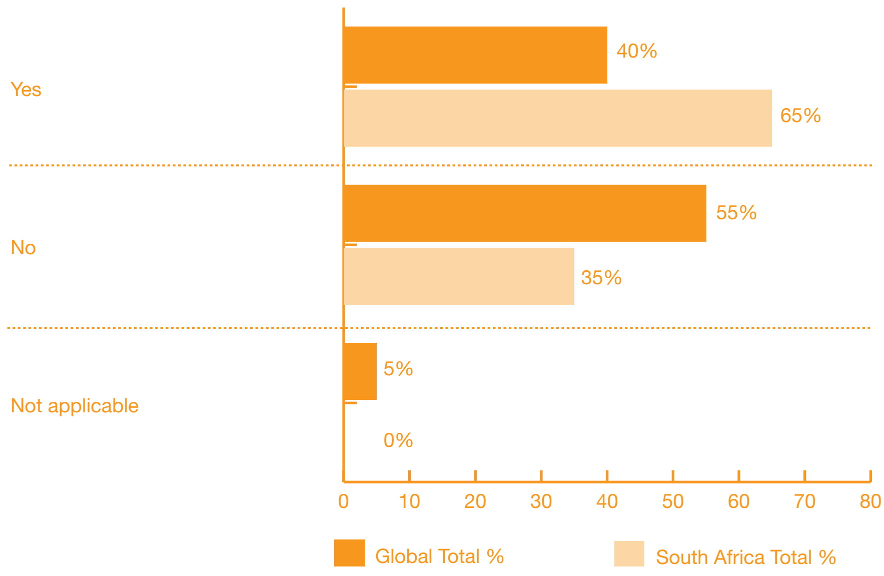


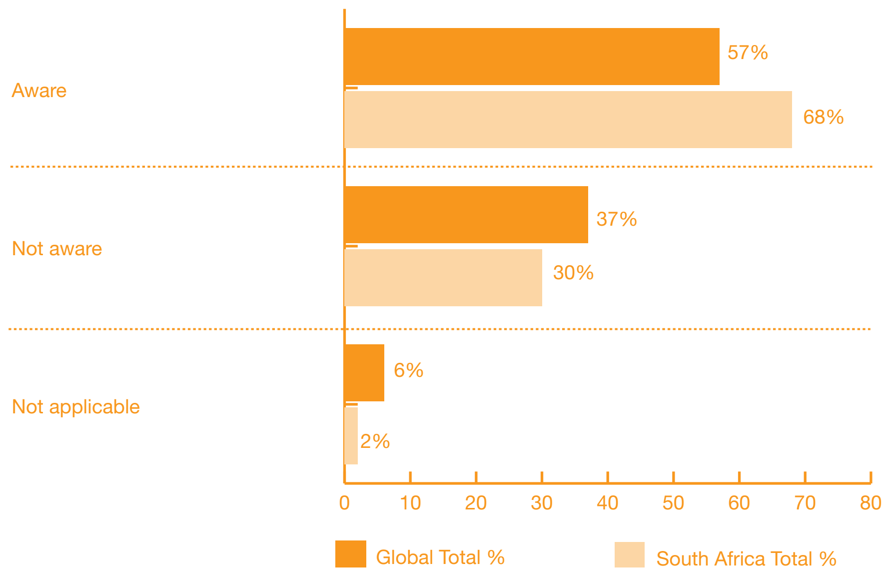
Figure 25: More than half of all proprietors haven't had their companies valued for at least a year



> *"Value is only value if you know about it. There is no value having a Picasso in the basement and not knowing about it."*
>
> *– James du Preez*

Many family-business owners have also failed to assess their potential tax exposure, even though taxes are rising in mature economies and planning is essential to realise any opportunities for mitigating the financial burden. The first step is to get the business professionally valued, in order to assess the likely tax liability if the business were to be sold to an external party or transferred to the next generation.

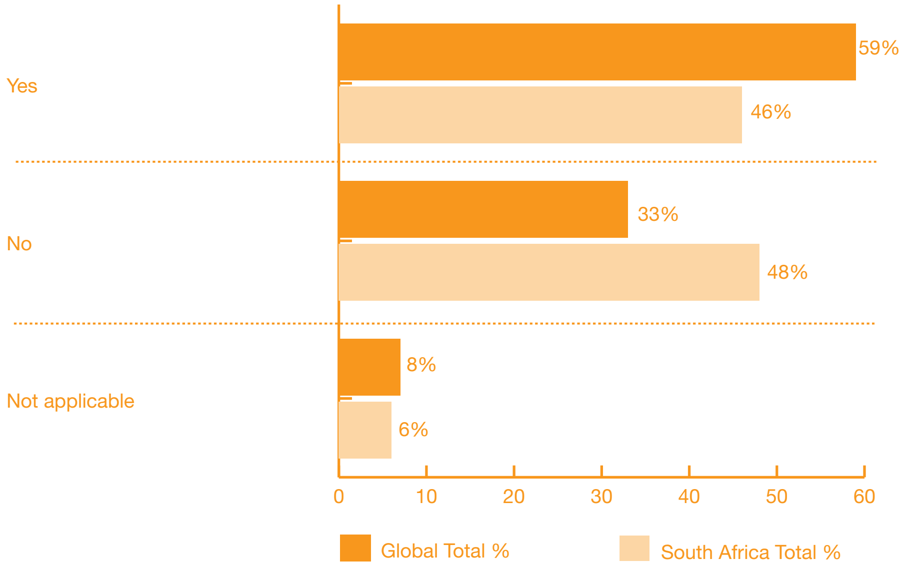
Figure 26: Many proprietors don't have a complete picture of their exposure to capital gains tax



Handing over the reins

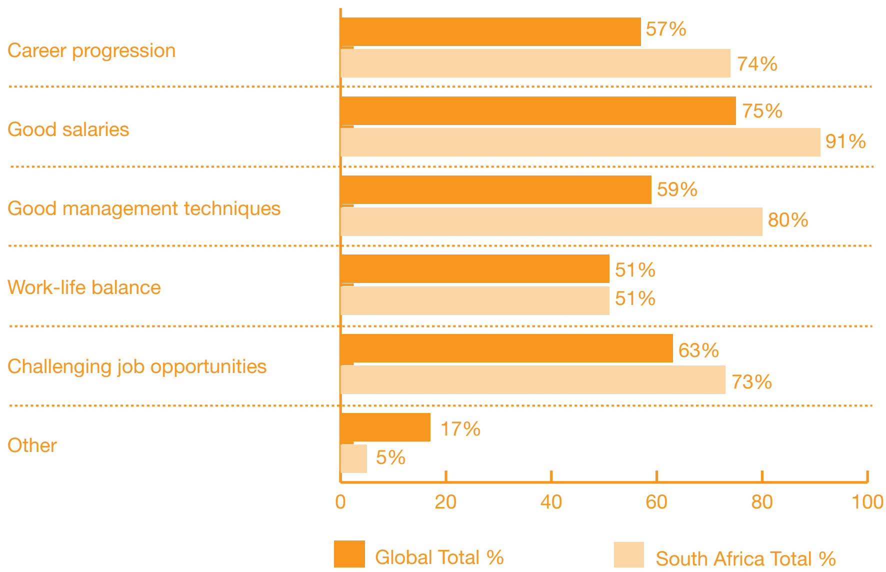
While many family-business owners don't know how much tax they or their heirs might incur, they are acutely aware of the need to remunerate senior management properly. They place much less emphasis on new challenges, career progression and work-life balance – a view they may need to modify in order to recruit the next generation of executives. Both anecdotal and empirical evidence shows, for example, that Generation X and Y workers rate leisure time much more highly than their Boomer counterparts[4].

Figure 27: Many proprietors are also unaware of the full extent of the inheritance tax their heirs might have to pay domestically



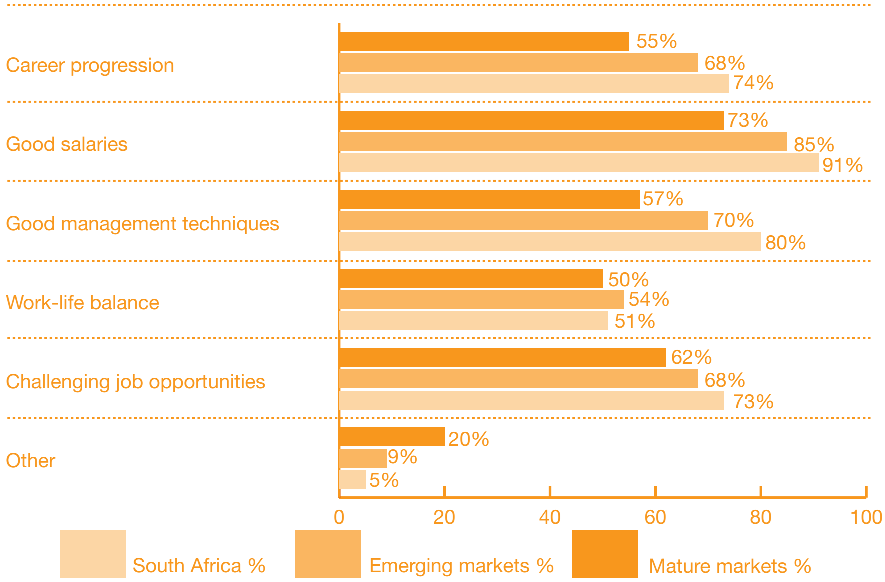
> ***"Like in the movie 'Avatar', things are connected. Consider the link between talent, remuneration and demographics to have more options regarding rewarding employees."***
>
> ***– Pienaar Zietsman***

Figure 28: Salaries top the list of measures family businesses use for retaining talent



The emphasis also varies from one region to another (see Figure 29). Executives in the emerging markets are particularly likely to see salaries, good management techniques and career progression as the most effective means of holding onto key staff.

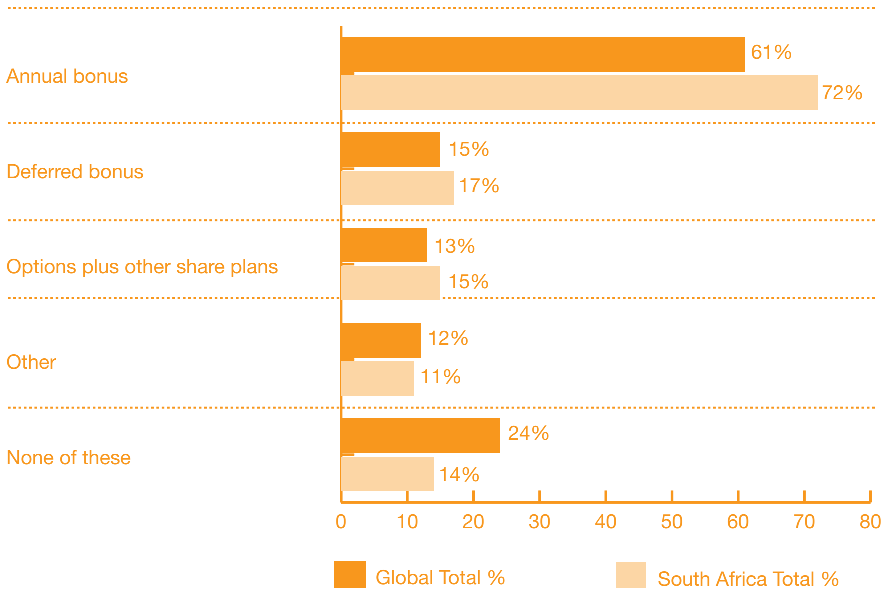
Figure 29: Companies in the emerging markets are more likely to stress the importance of multiple measures for retaining key staff



In addition to paying generous salaries, the majority of family businesses surveyed use other incentives to reward senior executives. Annual bonuses are still the most popular choice, as they were in 2007.

Payment of an annual bonus is particularly common in local companies (72%). However, most people, regardless of the size of their companies, believe such schemes have a positive effect.

Figure 30: The most popular means of rewarding senior management is the annual bonus



"I helped change employees' lives, improving their quality of living".

– South African executive

Managing family relationships

It's clear from your responses that the ability to manage differences of opinion smoothly is now more important than ever. The percentage of family businesses experiencing tension has increased significantly during the past three years. Nearly half the people participating in our survey told us they've argued about the future direction of the business, and nearly two-fifths said they've argued about the performance of family members employed in the business. Almost two-thirds of the family businesses in our survey also hire relatives without requiring them to compete for their jobs on the open market, which probably makes matters worse.

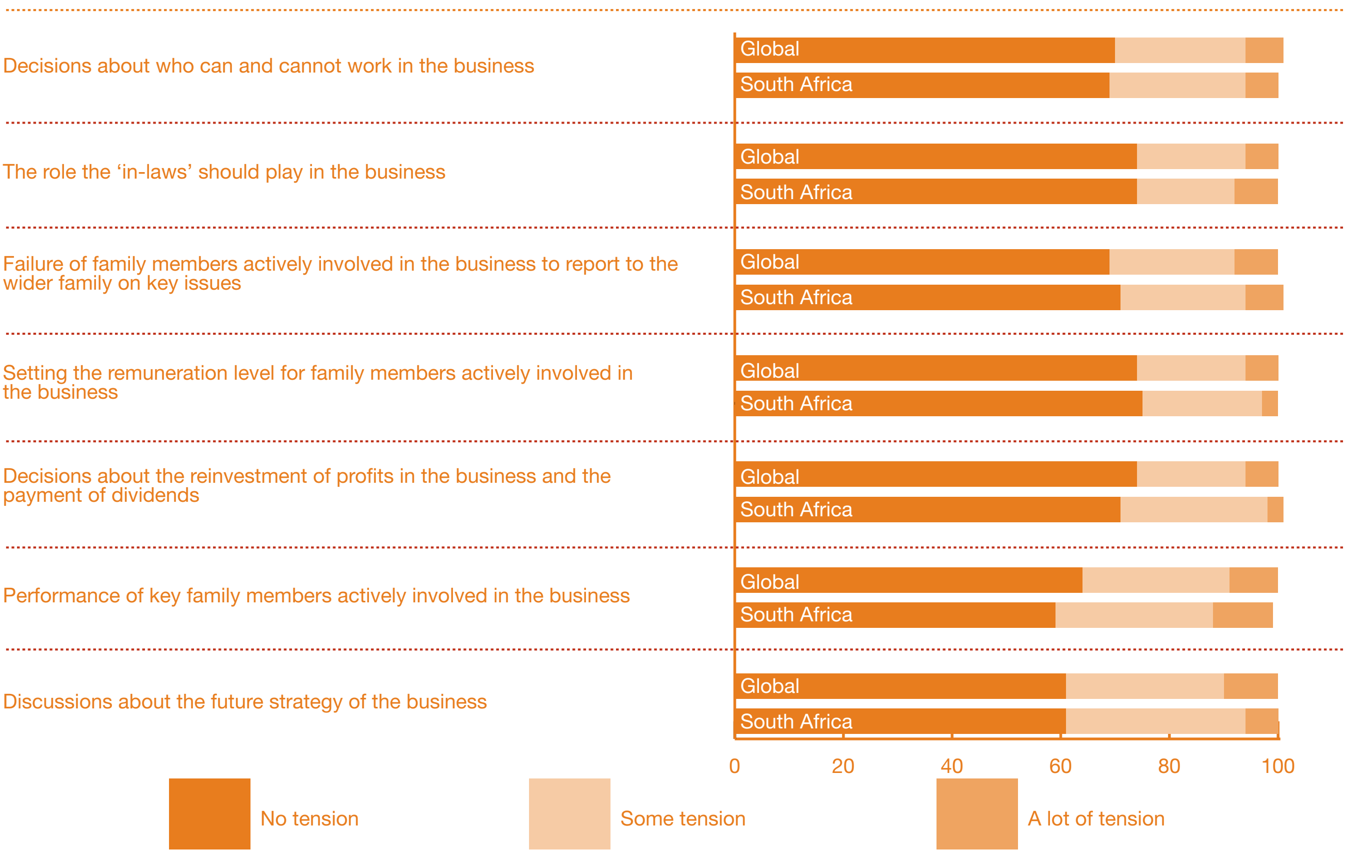
Yet, less than a third of all companies have introduced any procedures for dealing with disputes between family members. The smaller and younger the company, the less likely it is to have done so. The relatively few businesses that have put conflict resolution measures in place tend to favour shareholder agreements, whereas family councils were the most popular means of resolving arguments about the business in 2007.

Managing family relationships

As we noted in the introduction, a family business is essentially a combination of three different entities – the company itself, the family attached to it and the owners. The interests of the people in each circle overlap, but they aren't identical. These differences sometimes cause conflicts, especially in older companies, where it's more likely that some of the shareholders won't be involved in the day-to-day running of the business.

Certain subjects are particularly prone to making tempers fly.

Figure 31: Disagreements within the family business



Managing family relationships

> *"I hope that we're all still talking and not killing each other"*
>
> *– Irish respondent*

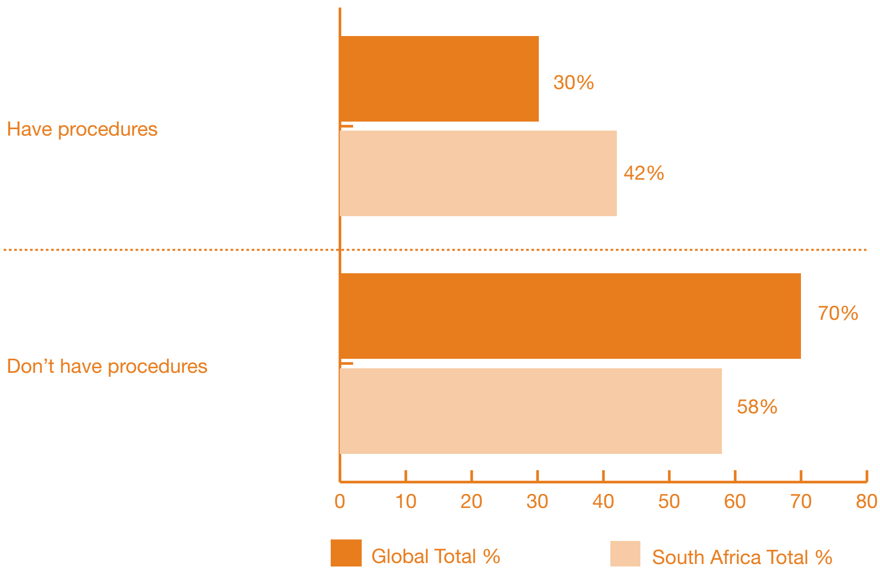
These are actually the same issues that caused most dissent in our previous survey. However, the percentage of family businesses experiencing tension has increased significantly, especially when it comes to discussing the future strategy of the business and the competence of the family members managing it.

The economic climate may be partly to blame. Shareholders may be more likely to question the direction and management of a company when it's going through difficulties. But some proprietors also seem to have relaxed the criteria they use when deciding to bring family members into the business. Preferential treatment of family members is particularly common in small companies and those based in North America.

It's probably understandable that so many owners should favour relatives when the recession has made it much harder for people to find work. Unemployment rates are currently hovering at about 10% in the USA and the Eurozone, for example, and may climb even higher in some countries[5]. Nevertheless, in hard times all companies need the best executives they can attract.

Less than a third of companies have introduced procedures for dealing with disputes between family members (see Figure 32). The smaller and younger the company, the less likely it is to have done so.

Figure 32: Most companies haven't adopted any procedures for resolving conflicts between family members.

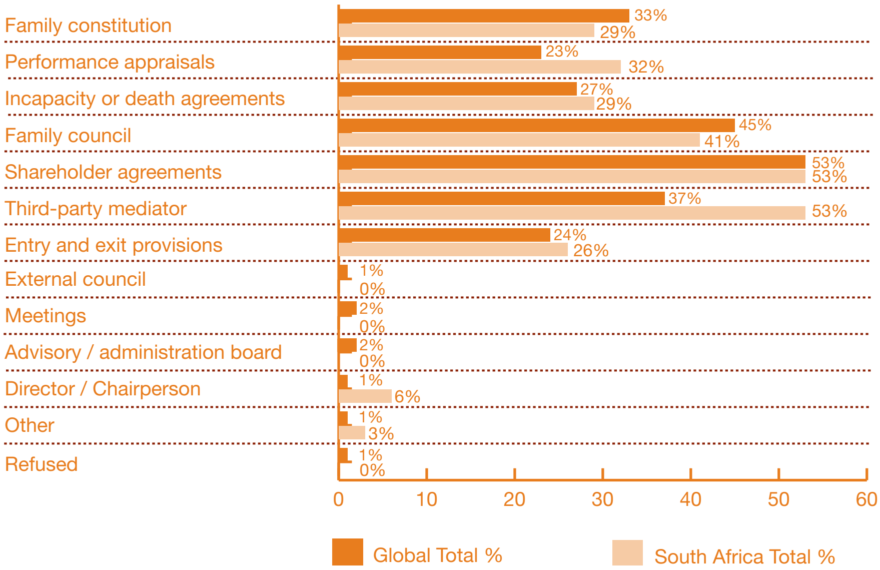


Managing family relationships

The number of family businesses with conflict resolution measures in place hasn't changed very much since 2007, but there has been some change in the procedures such businesses prefer. In 2007, family councils were the most popular means of resolving arguments about the business, whereas shareholder agreements are now the first choice (see Figure 33).

In South Africa the use of third-party mediation has also become more widespread, possibly because employing a non-executive director or independent business consultant to act as an impartial go-between has several advantages. It provides a neutral forum in which the disputants can air their differences without being intimidated; the process is more structured than 'ordinary' negotiation; and the results are often more long-lasting.

Figure 33: Shareholder agreements, family councils and mediation are the most common measures for resolving conflicts



"A family row can ruin a company"

– Brazilian executive

Rules of the game

Regulation, government incentives and corporate social responsibility are perennial concerns. So, what did you have to say on this score? The vast majority of family-business managers told us they would like to have a simpler tax regime and/or pay lower taxes. More than half also want to see a tougher corporate compliance environment, and many have serious reservations about whether their governments have done enough to support the business community during the recession. Criticism is particularly marked in the emerging markets.

But most people are much more upbeat about the growing emphasis on corporate social responsibility. Nearly three-quarters of the executives we spoke to said it's had a constructive impact on their companies. Almost half have already made minor or significant changes to their businesses in order to become more socially responsible, and half plan on doing so over the next two years.

We've discussed the key commercial and managerial issues family businesses face, and how they resolve internal disputes. But what's their attitude to regulation and corporate social responsibility? We asked respondents which regulatory changes they would welcome most. Top of their wish list is a better tax regime, as it was in our previous survey. More than four-fifths of the executives we spoke to say simplification of the corporate tax rules and/or a reduction in the tax burden is quite or very important to them (see Figure 34).

PwC's ***Paying Taxes 2011*** global survey issued in December 2010 found that it takes a medium-sized South African company an average of 200 hours per year to comply with all relevant corporate tax requirements. For a similar-sized British company, the same task would take 110 hours. While tax rules in many jurisdictions remain a significant burden, some governments are beginning to take action to ease the effort of paying taxes. In Britain, for example, Chancellor of the Exchequer George Osborne recently compared the 11,000-page UK tax code to a 'spaghetti bowl' and has established an office specifically to simplify the country's tax regime[6].

More remarkably, 56% of respondents also favour a tougher corporate compliance environment, a feature that ranked only fourth on their agenda three years ago (See Figure 34). This sentiment is echoed in South Africa where no less than 71% are in favour of strengthened compliance. This contrasts with the new Companies Act, which will remove statutory audit requirements for certain private companies and seem to provide a more relaxed or informal business environment.

Figure 34: Tax changes top of the list of changes family firms want

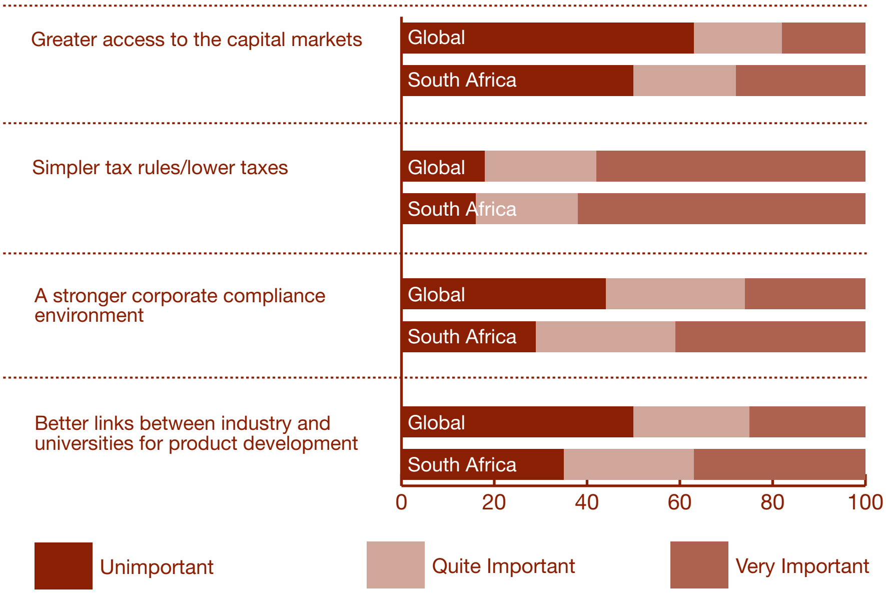
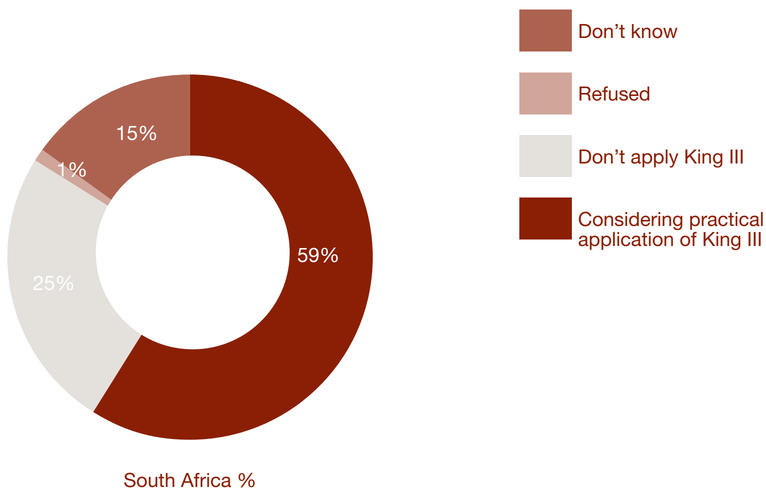


Figure 35: The majority of South African respondents say they are considering the practical application of King III in their businesses



It is interesting to note that more than half of South African companies surveyed say they will still conduct a full audit after the implementation of the Companies Act 2008. Furthermore, almost 60% of South African companies surveyed also say they are considering the practical application of the King III code of corporate governance.

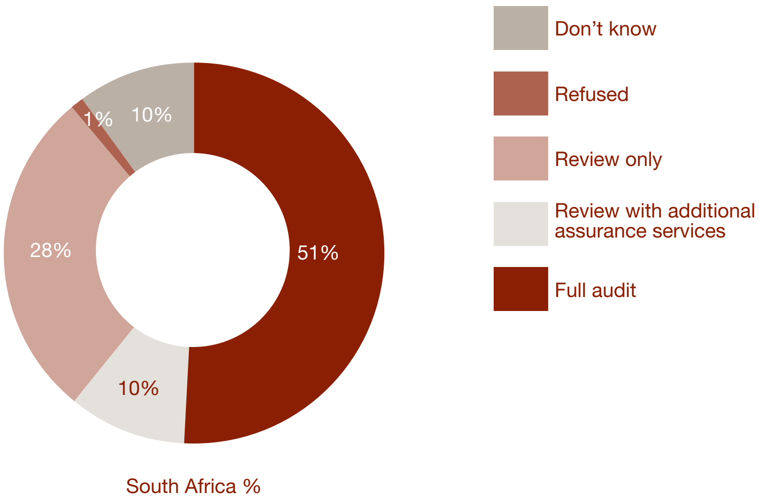
The virtual collapse of the global banking system in 2008 may account for much of the concern around compliance and corporate governance; many commentators have argued that one of the main causes of the financial crisis was inadequate or outdated regulation.

Half the executives we interviewed globally would also appreciate assistance in creating closer links with academia for the purposes of product development. In South Africa, 65% expressed this desire. In contrast, only 37% globally and 51% in South Africa are concerned about getting greater access to the capital markets (see Figure 34).

There are obvious reasons why relatively few entrepreneurs should be interested in floating their companies at present. Although the number of initial public offerings increased in the first half of 2010, the sovereign debt crisis in the Eurozone, the uncertain pace of the recovery and limited access to credit have all curbed interest in new offerings. Moreover, the main stock market indices are still languishing at levels well below those they reached in late 2006 and early 2007[7].

South African family-owned businesses consistently expect more from government when compared to the expectations of their global counterparts and those in other emerging markets. (See the Table 4).

Figure 36: Half of South African businesses say they will continue with a full audit once the new Companies Act is implemented



> *"The increased fiduciary responsibilities placed on directors by the new Companies Act and the value of independent external audit in providing comfort on the key controls and financial results of the company, are leading the directors of many smaller companies to continue conducting external audits regardless of whether the Act requires them to do so."*
>
> *– Andries Brink*

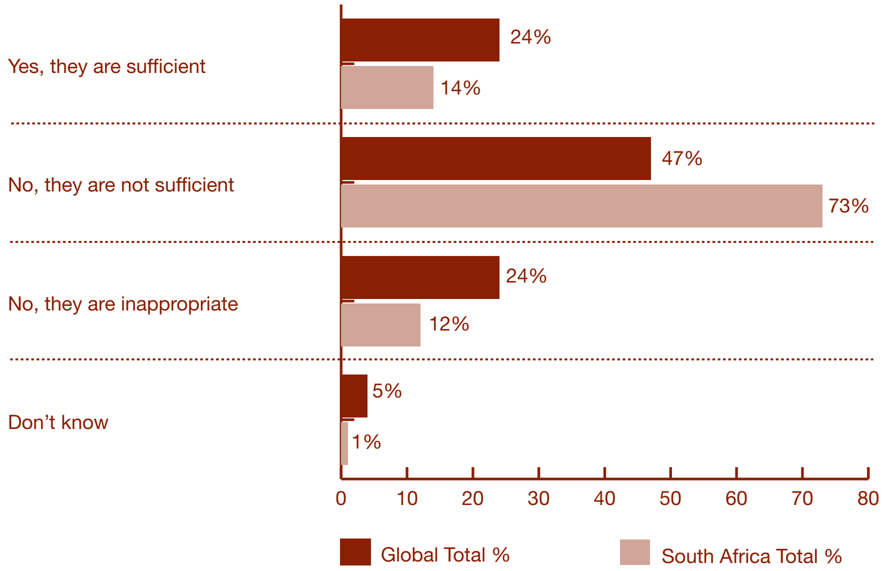
Table 4: Respondents who think government should give top priority to:

	South Africa	Mature markets	Emerging markets
• Simplification of business tax rules and/or a reduction in tax burden	68%	59%	60%
• Better links between industry and universities for product development	44%	28%	28%
• Greater access to capital markets	35%	25%	27%
• Strengthening the corporate compliance environment	41%	24%	40%

The difference in expectation between emerging markets, including South Africa, and mature markets may be explained by the example that was used on the previous page with regards to the effort it takes to comply with the tax regime in different jurisdictions. Since the British government has to some extent already taken strides to make it easier to run a business, the expectations of business owners are lower. Similarly, in countries with foreign currency controls, expectations will remain higher than in those that have none.

The precarious state of the global economy probably also explains why people think their governments have not done enough to support the business community during the recession (see Figure 37). Criticism is marked in South Africa where 73% of respondents think government can do more to help them.

Figure 37: Family business managers in the South African market are especially dissatisfied with government's initiatives to help them through the recession



> ***"Consider playing an active role in the lobbying of interest groups and civil society to enhance the legislative regime to support and grow your business."***
>
> ***– Brendan Deegan***

Rules of the game

However, most executives are much more upbeat about the growing emphasis on corporate social responsibility (CSR). Globally nearly three-quarters report that CSR has had a quite or very positive impact on their companies, and those based in the emerging markets are particularly positive (see Figure 38).

Forty-eight percent of all respondents have already made changes to accommodate CSR, while 49% plan on doing so over the next two years (see Figure 39). These people recognise that building a reputation as a responsible business helps a company distinguish itself from the crowd; customers often favour suppliers who demonstrate regard for the environment.

CSR can also help a business improve its performance by reducing energy and waste disposal costs, coping with new laws and restrictions more effectively and even developing new products or services.

"I want to build a thriving company that's careful about the environment, both social and ecological"

– French executive

Figure 38: Most executives believe CSR has had a positive impact on their business

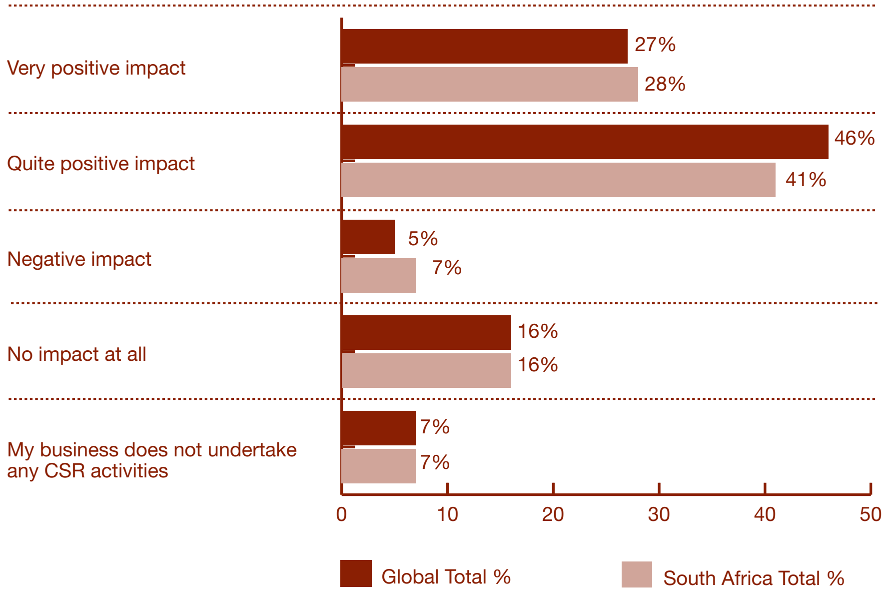
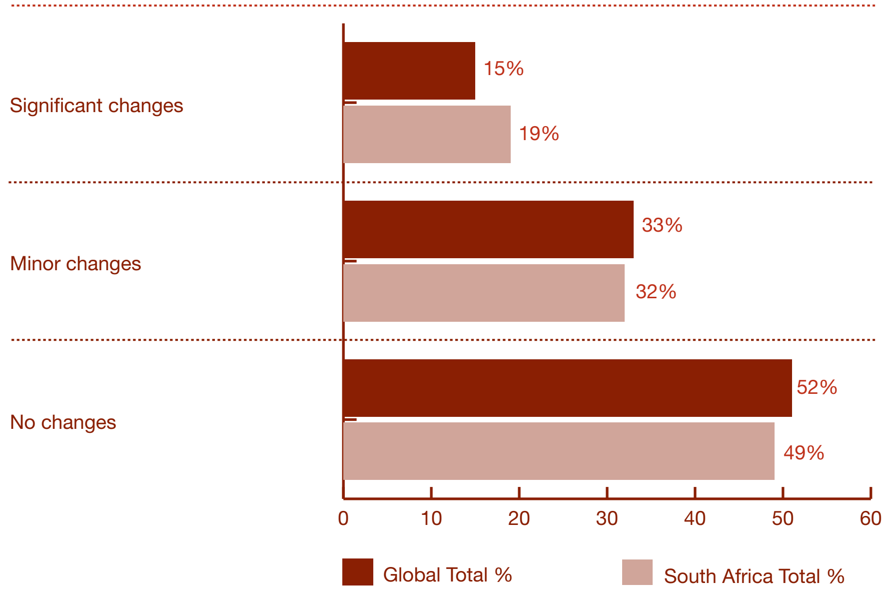


Figure 39: Many companies have already made CSR-inspired changes, and many more plan to do so over the next two years



"While CSR spending is prevalent in South Africa, it is essential that a well-defined strategy is followed to ensure that this spending can be well linked to marketing and BBBEE initiatives. There is great value that can be achieved by businesses if this is done properly."

– Abdul Essack

What we've learned

The responses we received during this year's survey show that a more sombre mood prevails than in 2007. A number of family-business owners talked in terms of 'trying to keep our heads above water' and 'making it through the crisis'. Several battle-weary executives also expressed a yearning to withdraw from the fray. 'I'd welcome anything that would enable me to retire earlier', one Maltese proprietor remarked.

But most people are determined to keep up the struggle and some have fared extremely well, regardless of the recession. 'I've grown the company tenfold in 10 years, which I think is quite an achievement,' a Finnish owner said. Others also have 'thriving and profitable' operations, enjoy 'international success' and aim to 'keep on growing'. Many of these entrepreneurs are eager to bequeath healthy businesses to their children. 'The business has been standing for over 50 years and that is the legacy of the family household. I'd like this to continue,' a South African proprietor observed.

They're not all confident that their heirs will rise to the challenge. 'The younger generation don't take the positions as seriously as the older ones,' a Canadian executive complained. A Cypriot family-business owner also has grave doubts on this score. 'I believe that, if I don't manage to take the company public, it will be destroyed,' he commented. Nevertheless, some successors clearly regard their responsibilities very seriously. 'I want to continue providing the quality product and exceptional service that my dad has been providing for the last 20 years,' said one person who's recently assumed the top job.

The desire to leave a stable and successful business for their offspring is by no means the only theme that emerged in our conversations with family-business owners. Many also stressed the importance of personal integrity. A South African business owner wants to be remembered for 'operating and leaving behind an honest and ethical company that conducted its activities according to the rule of the law and turned away business that did not adhere to the rule of the law'. Other local proprietors are concerned about their employees and improving their lives by operating it in a sustainable way. 'To provide a sustainable business for future generations' was the focus for one South African respondent.

To be sustainable is only possible when a company is successful – and commercial ambitions featured regularly in the feedback we received. 'I want to grow the business much bigger, let's say tenfold,' a Cypriot proprietor remarked. Other respondents spoke of driving up turnover and profits, and creating 'durable value'. 'Getting the company on the maximum profit level, without thinking about my own pocket', a South African proprietor remarked.

However, it's obvious that many respondents attribute much of their companies' resilience to the fact that they are family businesses. There are a few notable exceptions who want to 'escape from the family model', as one person put it. But for the majority of the participants in our survey, being part of a family business is a big plus. It 'means that we're looking at the business long term rather than short term, which gives us a lot of motivation and a good position', a Finnish respondent explained. 'The unity of our family has helped us. We respect each other and each person has a different expertise,' a Brazilian respondent added.

Indeed, the aspirations of many of the 1,606 respondents who generously contributed to our research can be summed up in the words of one Dutch family-business owner, who said: 'We've been trading for 78 years. Let's go for the 100 not out'.

Methodology and survey population

Our survey covers small and mid-sized family companies in 35 countries: Austria, Bahamas, Bahrain, Barbados, Belgium, Brazil, Canada, Cyprus, Denmark, Egypt, Finland, France, Germany, Ireland, Italy, Kuwait, Jamaica, Japan, Jordan, Malta, Netherlands, Norway, Oman, Russia, Saudi Arabia, South Africa, Spain, Sweden, Switzerland, Syria, Trinidad and Tobago, Turkey, United Arab Emirates, United Kingdom and United States. We interviewed top executives in 1,606 companies operating in 15 industry sectors between 26 May and 17 August 2010, including representatives of 81 companies in South Africa. All respondents were interviewed via a 20-minute telephone call, with the exception of respondents in Japan and Turkey, who were interviewed face-to-face. The research was coordinated by the PwC International Survey Unit, Belfast, our global centre of excellence in market research, which designed the questionnaire in conjunction with family business experts from PwC.

Methodology and survey population

Eighty-two percent of the companies in our global sample and 69% of South African respondents have been trading for at least 20 years. Globally, 42% have been in business for at least 50 years, compared to 30% in South Africa. Thirty-one percent employ more than 250 people (SA 24%) and 28% (SA 10%) generated revenues of over 50 million euros.

Globally, 54% export goods or services to foreign markets, compared to 44% in South Africa and 31% trade worldwide, compared to just 17% of their South African counterparts. The largest companies have generally been in business longest and are more likely to export to other countries.

Companies in the consumer goods and manufacturing sectors tend to be particularly active overseas; 61% and 81%, respectively, export products or services to other territories (see Figure 41).

Figure 40: Survey participants by industry sector

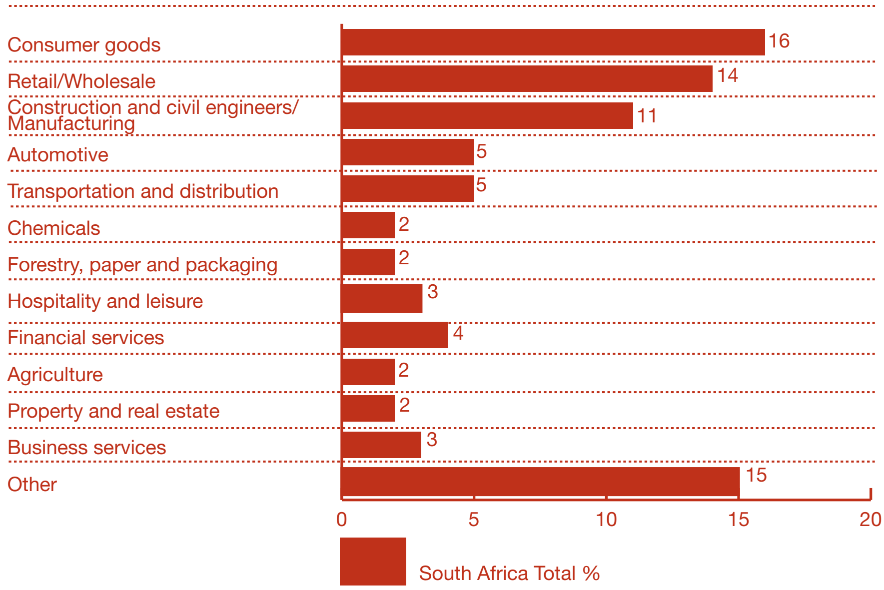
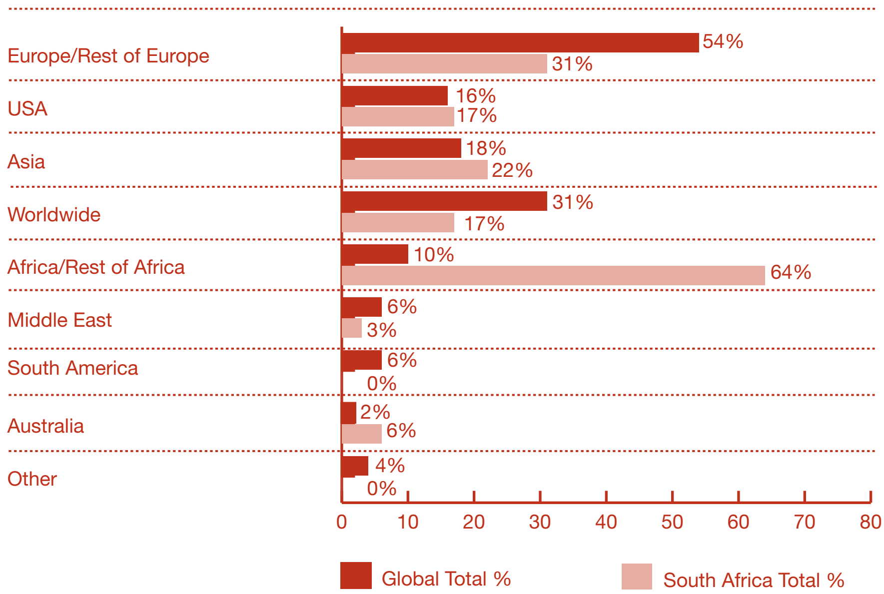


Figure 41: The countries with which companies that export goods or services trade



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Notes