Building for success today and tomorrow

Family Business Survey 2014
Australian results

Private Clients
pwc.com.au/familybusinesssurvey

Australian family business owners have a lot on their plate.

Many are working hard to find and sustain growth in a challenging market as well as trying to adapt to the dynamic global trends changing the face of business.

And whilst the majority are still growing, our most recent *Family Business Survey* found the growth of Australian businesses is currently below that of their global peers.

We are also below the global average on a number of issues and trends critical to the success of family business in the 21st century. These include our approach to: digital and technological innovation; succession planning; managing family conflict within the family business and the innovative use of capital for growth and development.

Even though family businesses are generally aware of these challenges, they are less sure when it comes to strategies and procedures to tackle them.

In addition to this – or perhaps because of it – we are seeing a surge in the number of family businesses planning to exit in what's fast becoming a crowded market. Unfortunately, many are not doing the preparation that's necessary to maximise family wealth in what, for most, is a once in a lifetime opportunity.

Without the necessary planning and investment to keep pace with emerging trends and innovations, Australian family business owners risk eroding the value they have worked so hard to generate – this applies whether they are planning to sell or pass the business on to the next generation.

As a means of individual comparison and benchmarking, PwC's global *Family Business Survey* provides important insights for Australian family businesses. It points to key areas for attention and investment to ensure the health of our family businesses stay strong.

Many Australian family businesses are on the cusp of major change. How they deal with it will help shape their future. There is work to do, but family businesses are famously resilient and remain confident of meeting the challenge.

David Wills
National Managing Partner, Private Clients

Contents

02 Introduction

06 Growth

08 Key issues and challenges

10 Digital innovation

13 The next generation

16 Future plans

20 Managing family conflict

22 What are the next steps for Australian family businesses?

A snapshot of the findings

2,378
interviews conducted in over 40 countries

90
in Australia

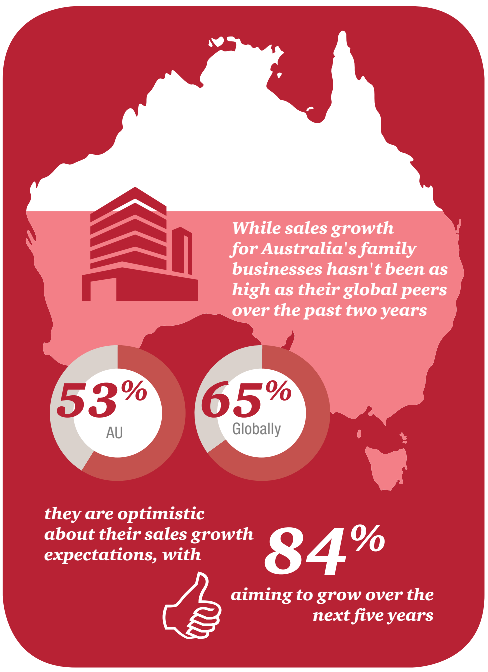
Australian family businesses seem to be ***falling behind on a number of closely linked trends including***

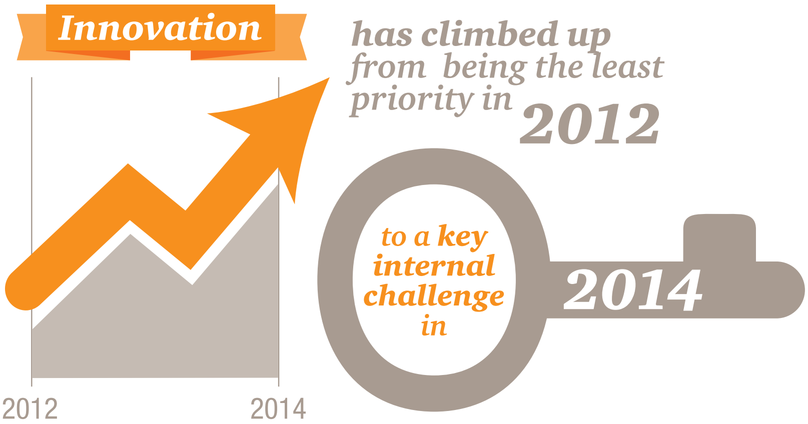
investment in digital innovation

succession planning

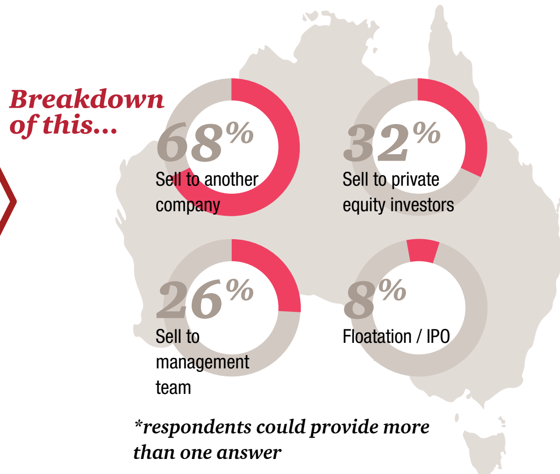
innovative use of capital

managing family conflict



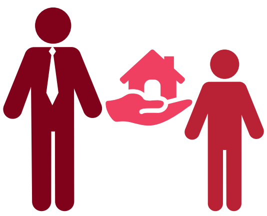


38% of family businesses are planning to sell or float their business



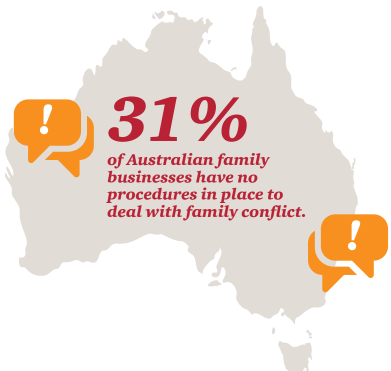
**respondents could provide more than one answer*

while only **24%** plan to pass it on to the next generation...



this is a shift from 2012

of Australian family businesses don't have a succession plan for key senior roles.



Growth

Australian family businesses appear to be struggling to find sustainable and reliable growth. Only about half (53 per cent) reported sales growth over the past 12 months; even less than the 56 per cent that reported growth in our 2012 survey.

More worrying is that family businesses appear not to be doing as well as their global counterparts, who on the whole reported higher sales growth over the last two surveys.

It's possible this disparity may be due to the fact Australian family businesses are coming off a higher base, having weathered the GFC better than many other countries.

But it may also be that many Australian family businesses are not taking full advantage of the global economic climate.

The subdued growth figures correspond to other indicators we are seeing in the market.

Despite this, Australian family businesses remain optimistic; 84 per cent are aiming to grow in the next five years and are largely confident of achieving it.

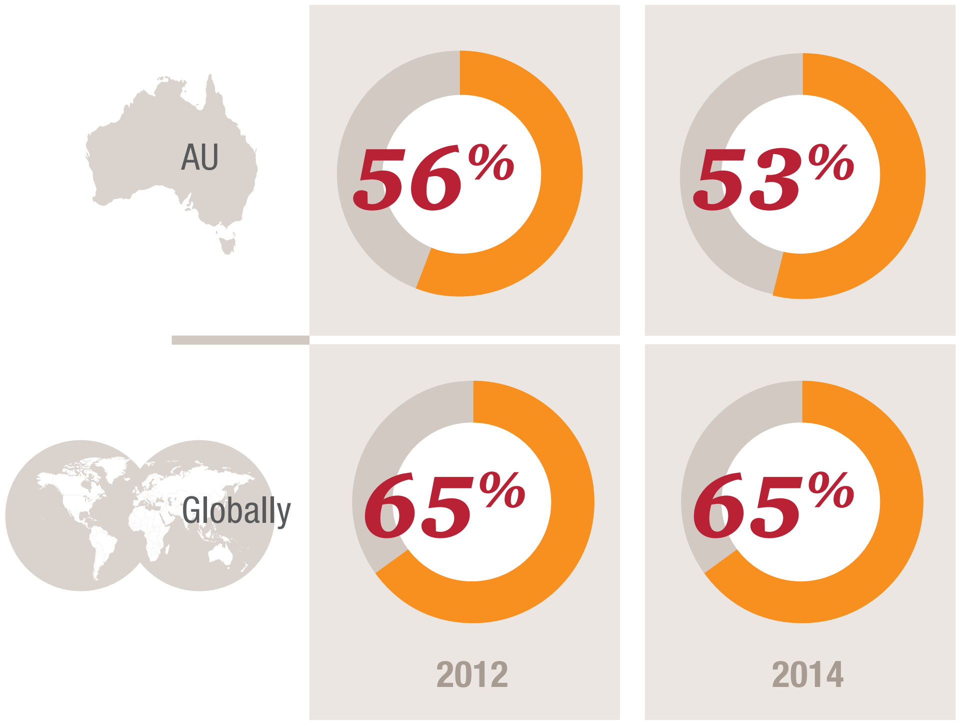
How they grow will, to a large extent depend both on how they deal with challenges inside their own businesses, and how they respond to the mega trends that are reshaping businesses all around the world.

"I think word of mouth from our customers would absolutely have had a huge impact on our growth."

John Winning
CEO, The Winning Group

> *"We need to continue our focus, in terms of our sales and marketing efforts, to continue to introduce the Coopers brand and particularly our ale products to new consumers around Australia to enable us to achieve ongoing growth."*
>
> **Dr Tim Cooper,** Managing Director, Coopers Brewery

Global sales growth comparison with Australian family businesses in the last financial year



Key issues & challenges

Staff recruitment appears to be a perennial issue for family businesses. It's been the number one short-term challenge over the last two surveys, for family businesses both in Australia and around the globe.

What did change in this year's survey was the number of Australian family businesses that identified business and product development as a key challenge for the next 12 months. Two years ago, only 10 per cent of family businesses saw it as important. This year that number jumped to 27 per cent, making it the number two short-term challenge, on par with cash flow and cost control.

And when asked about long-term challenges, innovation becomes even more critical. It was the top challenge family businesses in both Australia and the rest of the world said they would face over the next five years.

So while family businesses recognise the importance of innovation to achieve their growth prospects, they also see it as something they will deal with 'in the future' rather than a challenge that needs to be addressed today.

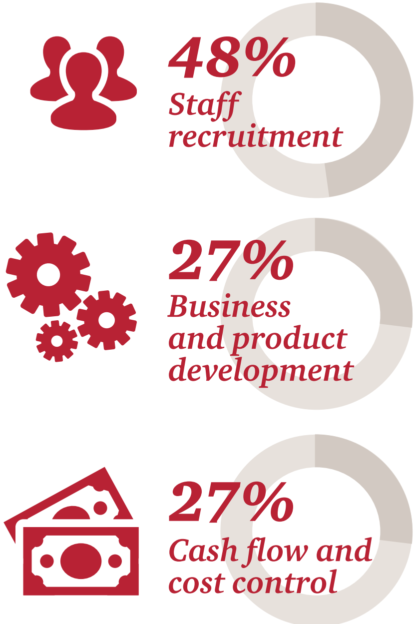
This disconnect is further reflected in the fact that less than half of Australian family businesses consider investment in technology and recruiting new talent – two critical solutions for addressing innovation – to be key challenges.

Equally concerning is that family businesses rate managing conflict between family members as their least important challenge. In our experience, being able to effectively and proactively manage conflict within the family is one of the key ingredients for a successful family business.

"By failing to explore the new opportunities, they pass you by and somebody else picks them up. If you don't continue to evolve, how does your business stay fresh."

John Riccio
National Digital Change Leader, PwC

Top 3 internal issues for Australian family businesses in the next 12 months



Data-driven innovation

The spin-off benefit of an increasingly digitised world is data. When used strategically, data helps businesses make informed decisions rather than rely on gut instinct or guesswork. It can help solve problems, create efficiencies and invent new products.

In 2013, data-driven innovation added an estimated $67 billion to the Australian economy, or 4.4 per cent of GDP.

But it's not just the domain of governments and multinationals. Family businesses can benefit from data-driven innovation too. They can use data to increase knowledge of their business, such as their costs and cash flow, as well as a better understanding of market trends to gain insights about their customers.

Digital innovation

Like their global counterparts, the majority of family businesses in Australia (71 per cent) recognise the need to adapt to an increasingly digital world. But only 57 per cent understand the tangible benefits of digital strategies and systems, or have a realistic plan for measuring them.

This misalignment may go some way to explain why less than one third (30 per cent) of Australian family businesses think attracting talent to help make the digital conversion is important. In this regard, Australian family businesses are well behind their global peers (43 per cent).

Unfortunately, the gap between idea and action is playing out in other types of businesses in Australia too. PwC's most recent *Annual Global CEO Survey*, for example, showed that Australian CEOs were strong believers that technology would be the biggest transforming trend for their business with 91% identifying technological advance as the single most important challenge for businesses to address. Yet only 45 per cent had a technology change program recently completed or underway.

"I think of social media as a hygiene factor nowadays, that we need to have it"

Dr Tim Cooper, Managing Director, Coopers Brewery

Case study:
John Winning
CEO
The Winning Group

How to win on the web: Appliances Online

The Winning Group was set up in 1906, selling parts and accessories for horse-drawn carriages. In the century since then the company has kept pace with technological change and it's now a major retailer of home appliances. There are 12 stores across Australia and a booming e-commerce business, Appliances Online, which was founded by John Winning, the founder's grandson, nine years ago.

Appliances Online is now Australia's largest online appliance retailer, has won multiple awards for its customer service and use of technology, and can boast over 340,000 likes on Facebook. It's a classic 'digital disruptor', and has made a spectacular success of the tricky transition from bricks to clicks. So how does Winning keep winning?

"It's about culture, and it's about the customer," says John Winning. "In fact the two go hand in hand. The customer always comes first in everything that we do, and our people know they are absolutely being empowered to make decisions to the benefit of the customer. We spend a huge amount of time listening to our customers and adapting our business to their needs - that's how we got the idea of the 'Handy Crew' teams we have today, who can connect appliances in customers' homes, if they want that. We call our strategy 'where, what, wow'. That means being where our customers want to shop with us, whether that's in-store, online or mobile; it's about offering what our customers want to buy from us, and it's about wowing them with the quality of our service."

As for technology, Appliances Online may sell leading-edge products, but it has no interest in being at the leading edge of the digital revolution.

"We tend to let the early adopter businesses get into a technology first – a lot of the time they do it for its own sake, just to have a mobile site or just have a particular app. What we'll then do is analyse what those businesses are doing and how it's working, and see how we can adapt that and make it into something that really works for our customers. I call it a leap frog approach: we let them make the first move, and then we try to overtake them with something much better."

Making the move to digital

Like all businesses, family businesses are working hard to come to terms with the global trend towards digital. But they also have some unique challenges to address.

"For many family businesses, technology has often been an area of under investment," say PwC's National Digital Change Leader John Riccio.

"But that view just doesn't hold any more. Technology is totally embedded in the way we all do business these days. It's also an opportunity to differentiate yourself from competitors who may not be prepared to invest."

The culture of tradition in family business can be a key barrier to embracing new business models.

"We sometimes see the next generation wanting to embrace digital technology, but then come up against the current business owner who may be reluctant to change what's worked in the past.

"There's a view that technical smarts don't equate to commercial smarts. But increasingly, it's the opposite that is in fact true."

John says it's important for family businesses to find a balance between making appropriate investment in digital innovation while protecting the revenues that have helped the business grow to date.

"The key is to take the curiosity, risk and experimentation that led to the business being a success in the first place – and now apply that thinking to digital innovation."

Here are some things that family business should be thinking about in relation to their digital strategy:

- Understand how your customers are using digital technologies and what they expect in terms of a digital experience – ask if your business is meeting those needs.
- Think about the sources of data that you could – or should – be accessing to get a better sense of customer sentiment or business efficiencies.
- Think holistically about your digital strategy – you may have a website, but are you investing in the right channels to drive traffic there?
- Be prepared to explore and experiment with new digital models – start with a small project and test how the business responds.

The next generation

Family businesses have a proven track record of achieving better results than other businesses. But only 12 per cent go beyond the third generation, according to PwC's recent *Next Generation Survey*.

For those looking to keep the business in the family, bringing the next generation into the business is critical to its longevity and success; yet most Australian family businesses are not doing it, or could be doing it better.

Less than half of the family businesses surveyed said they have members of the next generation working for them in any position.

And only one quarter have next generation members working as senior executives. In this regard, Australian family businesses are behind their global peers, of which almost half have family members in senior roles.

They are also falling behind when it comes to succession planning, something that can be a make or break moment for even the most successful family business.

Only 8 per cent of Australian family businesses have a succession plan in place that could be considered robust and comprehensive; the global average is 16 per cent.

Engaging the next generation

Generational issues have always been a challenge for family businesses. The technological revolutions of the last few decades have made the divide as wide as ever.

But PwC's Private Clients Partner Sue Prestney, says even though baby boomer parents might find it tough to get their gen Y children interested in the business, the benefits can be substantial.

"The next generation is not only critical to the continuation of the business as a family enterprise, but is often the source of necessary transformation, through new ideas, new experience and new energy.

Sue says that as 'digital natives', the next generation can be key players in helping family businesses adapt to emerging global trends such as digitisation, demographic shifts and climate change.

"The older generation needs to be careful not to undermine the enthusiasm of the next generation by underestimating their capabilities or discounting their ideas," says Sue.

Another important element of engaging the next generation in the family business is actually encouraging them to seek experiences in other organisations or fields.

"Children of the current business owners often need to feel that they have an identity that is their own, that is separate from the family business. And they also need to feel they have something unique to offer.

"Spending some time outside the family business can be a logical step in their own development. And it can also be a great source of innovation as the next generation bring what they've learned back to the family business.

"Effective succession ultimately comes down to good succession planning. Clearly define roles, responsibilities and entitlements as early as possible, and encourage open communication to help bridge the gap and make sure the next generation is prepared to succeed," says Sue.

Case study:
Dr Tim Cooper
Managing Director
Coopers Brewery

Keeping a family business strong through successful generation change

Dr Tim Cooper almost didn't follow in the footsteps of his forbears and become a brewer. Although he planned on joining the family business from a young age, his father actually encouraged a different path.

"When I was still at school in the 70's Dad asked what I wanted to do, and I said I would study mechanical engineering and go into the brewery. But he said no, the brewery is in the doldrums. You'll have to think of something else."

So Tim studied medicine and worked as a doctor in the UK through the 80s.

Eventually, however, Tim realised that helping the family business survive and pass to the next generation was too unique an opportunity to let go, and he returned to Australia to join the company in 1990.

And since then Coopers, which recently celebrated 150 years of operation, have achieved outstanding success: 21 years of continuous sales growth, much of it against a backdrop of declining beer sales nationally.

But rather than seeing time spent outside the family business as problematic, Tim believes this has actually been critical to the success of Coopers over six generations.

"The third generation of the company were sons of two directors who had incorporated the business back in 1923. There was an acceptance, I think, both in the third and particularly in the fourth generation that, on the one hand, they would go into the business, but that they should also have some knowledge which might contribute towards the business.

"So when we came to the fifth generation it was still seen as being advantageous that family members both had experience outside of the business and an educational background that was going to be beneficial," Tim said.

Coopers have discussed this at a board level and incorporated it into their business ethos, without being too prescriptive. Young family members interested in coming into the business should have experience that they can bring to bear when they join the company.

"We would like to think that the young people seriously think about what work they do to gain experience if they want to come into the business. You don't want, obviously, young people to come into the business and not be happy once they are involved," said Tim.

And successful generational succession remains a key priority for the current managers.

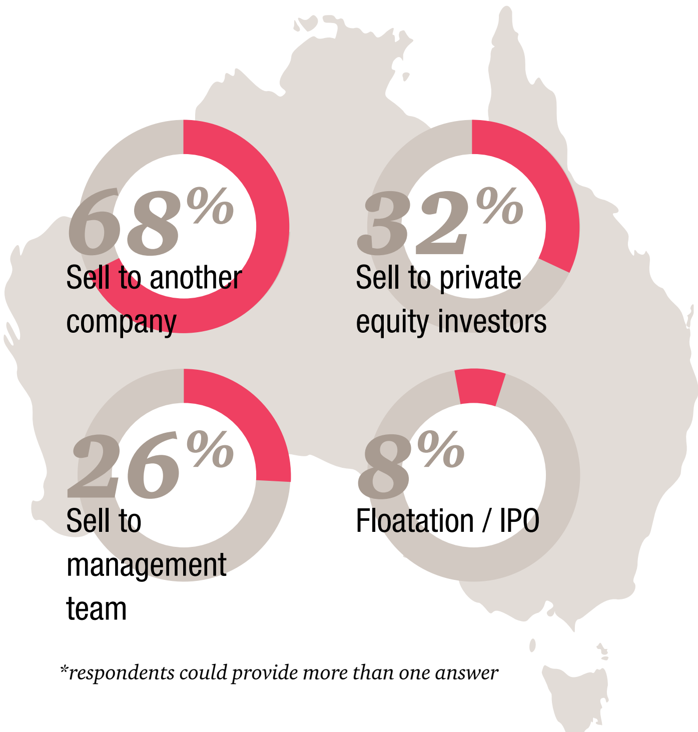
"Looking ahead, I would hope that we have successfully managed the transition to the sixth generation members of the Cooper family who are involved in the management of the business.

"If we can achieve that, I think we have successfully handed on the baton. As we like to say, we are custodians of the business for future generations."

Future plans

38%

of family businesses are planning to sell or float their business



**respondents could provide more than one answer*

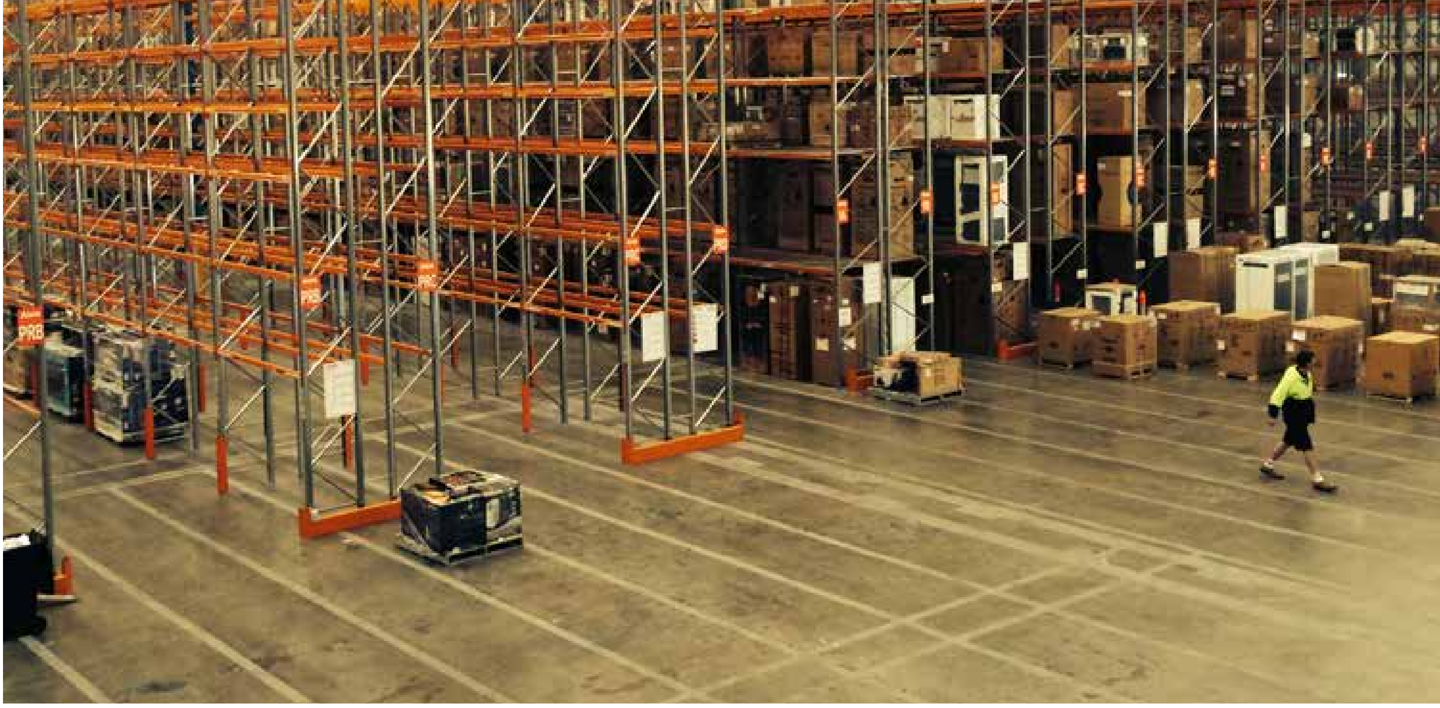
In the two years since the last *Family Business Survey* there has been a dramatic shift in the future plans of Australian family businesses.

More than one third (38 per cent) are planning to exit their business – by sale or float. But less than a quarter (24 per cent) are planning to pass the business to the next generation. In our 2012 survey the results were the reverse: more wanted to pass on than to sell.

The latest Australian results are also very different from the global average, where 40 per cent of family businesses plan to pass management to the next generation and only 20 per cent expect to exit.

What's behind this turnaround? One factor may be the swelling number of private business owners planning to retire. Recent research by PwC's Private Clients team has suggested more than 1.4 million owners will be retiring in the next ten years; a result of both our aging population and more favourable post-GFC market conditions.

Another factor may be that some family businesses have failed to innovate and keep pace with mega trends like digital transformation and shifting demographics. Others may have been unsuccessful bringing the next generation into the business.



What about private equity?

One exit option family businesses should consider is private equity, particularly if the business has not reached its full potential yet.

Private equity partners are professional business sellers, who typically take 3–5 years to prepare a business for sale. Prior to investing in a business they assess what the eventual exit will look like (who will be the buyers, how will the business be valued) and then set a strategic plan for the business that will maximise valuation at that time.

Partnering with private equity gives family businesses the opportunity to de-risk now by selling down some shares. And they can also draw on the expertise of the private equity partner to help grow the business and maximise its value.

Capital options for growth

The challenge for businesses not planning to exit is how to grow. The key to growth is appropriate investment in innovation.

There are an increasing number of alternative financing solutions available to family businesses looking for additional debt capital or more flexible lending arrangements to innovate, including:

- Asset backed lending solutions, where funding is advanced directly against specific assets of the business, such as receivables and inventory.
- Fixed interest rate instruments, such as corporate bonds, with longer term to maturity than typical bank debt facilities (i.e. greater than 5 yrs); typically these are applicable to businesses with larger property portfolios.
- Hybrids of senior debt and mezzanine financing, which may assist capital constrained businesses gain access to additional growth capital.

Selling the business

If you're thinking of exiting, now is a good time to sell according to Alan Elliott in PwC's Private Clients team.

"Valuation multiples have recovered from GFC levels, the window for IPOs is open, and private equity partners are cashed-up and looking for good businesses to buy.

"Overseas corporates are also looking for bolt-on acquisitions to enter or expand in the Australian market."

But Alan warns that buyers remain cautious and particular about what they invest in.

"While conditions are good, buyers are definitely looking for quality and can pick and choose from an increasing number of businesses coming to market. Generally speaking they would prefer to pay more for a well-prepared business rather than pay less and take a risk.

"Families typically only get one chance to sell their business and crystallise their wealth. So it's important to get it right."

Alan says that many family business owners don't prepare for the exit event very well; by rushing into a sale process, or by not spending the time to get their house in order, or by not understanding precisely what will enhance or diminish a buyer's valuation of their business. Value is in the eye of the beholder, after all.

Preparing for exit

Whatever the reason behind the decision, family businesses wanting to exit will need to undertake careful planning to ensure they are able to optimise value in a market that will allow buyers to pick and choose.

Here are the top 10 things to think about:

1

Take your time

You will generally achieve a better result if you allow at least 6-12 months to properly plan the sale of your business.

2

Put family first

Take family objectives into account prior to embarking on a path to sale; small differences now can become magnified nearer the point of sale and put the process at risk or lead to family conflict post sale.

3

Know your buyer

The natural buyers of your business will typically pay the highest price; identify who they are and how they assess value so you can prepare your business to maximise valuation and competitive tension on sale.

4

Make yourself redundant

If you are the key person running the business you need to step away and hire a strong CEO/GM and support team who can prove themselves for at least a year prior to sale; this will give a future buyer comfort the business won't fail without you.

5

Pay for some housekeeping

One of the biggest problems we see is a lack of investment in professionalising the business; sort out financial reporting and accounting, separate the owner's affairs from the business and tidy up legal and operational risks.

6

Work your EBIT (Earnings Before Interest and Taxes)

Every sustainable dollar added to the EBIT figure is worth 'x' times EBIT when you come to sell; ideally give yourself two years to realise profit improvement initiatives and demonstrate their sustainability to buyers.

7

Leave something for the next guy

Buyers will pay more if there are opportunities for future growth, such as new products, geographic expansion, or new channels; plan and partially implement these opportunities so that buyers can believe them, and therefore be willing to pay for them.

8

Protect your sales proceeds

Any proceeds you make from selling your business will be after tax; make sure you have the right tax structure for sale. Also, draw up a wealth strategy for protecting your post-sale proceeds to meet retirement and succession goals.

9

Be prepared as timing can be everything

The M&A market in any given industry can grow hot and cold very quickly, and have a large bearing on valuation; get your business in a sale-ready condition as early as possible so you can respond quickly to changes in the market.

10

Above all do your homework

You only get one shot at selling your business; engage the help of professionals when required; remember selling your business is very different to running your business.

Managing family conflict

When it comes to procedures and mechanisms for managing conflicts in family business, Australian firms are consistently well behind their global peers.

Only one third of Australian family businesses have a shareholder agreement in place, compared to more than half of family business from around the world.

And only 14 per cent have a family constitution, which is widely recognised as one of the best mechanisms for effectively managing conflict. But more worrying is that one third of Australian family businesses (31 per cent) have nothing in place at all.

Importance of a family constitution

A family constitution is an agreement that family members sign up to that sets out the key terms by which control, responsibilities and benefits are shared amongst family members involved in the business.

It is an important tool for not only managing succession, but also for managing conflicts as they arise.

For example it can address employment issues, such as whether future executives must be from the family or whether the business will look to talent outside the family. It can even set out how family members are paid based on their skills and contribution to the business.

A family constitution also can act as a business plan of sorts, describing the short and long term objectives of the business and clarify intentions as to whether owners plan to keep the business in the family or to sell it.

The process of developing a family constitution can also clarify important issues around ownership and structure that might not have been properly addressed before.

"When there is uncertainty, this can create distrust and tension."

Sue Prestney
Partner, Private Clients, PwC

Don't let small conflicts turn into big ones

Many difficulties in family business can be traced back to conflict within the family.

According to David Smorgon OAM, Senior Advisor to PwC – Family, Business and Wealth, the key to managing family conflict effectively is to identify it early and address it before it gets out of hand.

"I generally see two kinds of conflict in my experience working with family businesses – simple and complex. And the complex type nearly always started out as simple problems that were not handled properly.

"Differences of opinion in family businesses is normal and healthy. In most cases it can be worked through by open communication and common sense.

"But when conflicts are left unaddressed, mishandled or misunderstood, they can get serious and can lead to emotional and behavioural problems. At that point you might have to bring in specialists because rational thinking goes out the door."

David says that having a family constitution in place is an important first step, but you must also have regular meetings and establish a culture of openness and a willingness to deal with conflict.

"Family members must be able to feel safe to express their views, and know that whatever conflicts arise within the family can be dealt with. This means working through the day-to-day conflicts as well as the big decisions – on a regular basis.

"Early and regular resolution of conflict will help keep the bigger, more damaging problems associated with conflict at bay."

What are the next steps for Australian family businesses?

Whilst Australian family businesses are confident about their long-term prospects, there is important work to be done to ensure they are capable of adapting and thriving in a rapidly changing world.

Digital innovation

A key challenge for family businesses is innovation and digital technology. Family businesses should:

- Create a culture of innovation within the business, which includes a willingness to invest in new skills and technologies
- Explore and experiment with new digital and data-driven business models
- Invest in talent with the right digital skills – this may well be found in the next generation.

The next generation

Bringing the next generation into the business is a critical step for the longevity of family business. Family businesses should:

- Start the succession conversation with your family members as soon as possible
- Encourage family members to develop their own skills and experience that can one day be incorporated back into the family business, should they wish to do so
- Make sure you have a comprehensive, robust and well-documented succession plan.

"The smoking gun evidence suggests Australia's family businesses are at risk of eroding the value or even derailing the business they've worked so hard to achieve."

David Smorgon OAM
Senior Advisor to PwC – Family, Business and Wealth

Future plans

Whether you are planning to sell or pass the business to the next generation, you need a plan to add value for the future. Family businesses should:

- If planning to sell, make sure you have done your homework and properly prepared the business for sale
- If planning to grow, develop a plan for innovation including capital investment options
- Consider whether private equity is a suitable option for the growth and eventual sale of the business

Managing conflict

Successful family businesses are able to effectively manage conflict. Family businesses should:

- Develop a family constitution as soon as possible
- Make sure that day-to-day conflicts are dealt with as they arise
- If conflicts are deep and long-standing, bring in professional help.

For further information about PwC's Private Clients team and our services, please contact:

David Wills
National Managing Partner
Private Clients, PwC
+ 61 (3) 8603 3183
david.a.wills@au.pwc.com

David Smorgon OAM
Senior Advisor to PwC
Family, Business and Wealth
+ 61 (3) 8603 1368
david.smorgon@au.pwc.com

John Riccio
National Digital Change Leader
PwC
+ 61 (3) 8603 4968
john.riccio@au.pwc.com

Townsville

Carl Valentine
+61 (7) 4721 8543
carl.a.valentine@au.pwc.com

Brisbane

Chris Lowe
+61 (7) 3257 8561
chris.h.lowe@au.pwc.com

Gold Coast

Trevor Mahony
+61 (7) 3257 8807
trevor.mahony@au.pwc.com

Perth

Cesare Scalise
+61 (8) 9238 3417
cesare.scalise@au.pwc.com

Adelaide

James Blackburn
+61 (8) 8218 7100
james.blackburn@au.pwc.com

Sydney

Paul Brassil
+61 (2) 8266 2964
paul.brassil@au.pwc.com

Kel Fitzalan
+61 (2) 8266 1600
kel.fitzalan@au.pwc.com

Jason Habak
+61 (2) 8266 2964
jason.habak@au.pwc.com

Newcastle

John Campion
+61 (2) 4925 1154
john.campion@au.pwc.com

Greater Western Sydney

David Hegarty
+61 (2) 8266 5465
david.l.hegarty@au.pwc.com

Melbourne

Sue Prestney
+61 (3) 8603 1201
sue.prestney@au.pwc.com

Alan Elliott
+61 (3) 8603 2378
alan.elliott@au.pwc.com

Sanjiv Jeraj
+61 (3) 8603 3187
sanjiv.jeraj@au.pwc.com

Canberra

Eugene Kalenjuk
+61 (2) 6271 3604
eugene.kalenjuk@au.pwc.com

Acknowledgements

John Winning, CEO, The Winning Group
Dr Tim Cooper, Managing Director, Coopers Brewery.

PwC's Private Clients team would like to thank John and Tim for giving their time and providing valuable insights for PwC's *Family Business Survey*. It has been a pleasure to be able to share the experiences of these iconic family businesses.

Participants

PwC's Private Clients team would like to thank the participants who gave up their valuable time to take part in this important piece of research.

Follow the conversation #familybusiness

@PwC_Au

PwC Australia

PwC Australia

About PwC's Family Business Survey 2014

PwC's *Family Business Survey 2014* is based on interviews with 2,378 key decision-makers in family businesses across more than 40 countries. Ninety of these interviews were conducted in Australia between 9th May and 31st July, 2014.

pwc.com.au/familybusinesssurvey

The Design Group 21797 (09/14)