Celebrating cultural trends

FAMILY BUSINESSES IN HONG KONG AND CHINA
COUTTS INSTITUTE

Advisory Panel

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INTRODUCTORY NOTE

Summarising different research findings, The Chinese University of Hong Kong estimates that the majority of companies in Hong Kong and China are family businesses.

In global terms, family businesses in Hong Kong and particularly in China are relatively young. In Hong Kong, many of the high profile family businesses were set up immediately after World War 2, and are now in transition from the second to the third generation. While in China, many family businesses have only been in existence for a couple of decades and in many cases are still being controlled by first generation members.

It is with this in mind that we have set out to outline some of the cultural trends affecting family business owners in Hong Kong and China, highlight potential family risks and suggest a few practical ideas for families planning for the future.

We are extremely grateful to the independent panel of experts who volunteered their time to share their different perspectives. These individuals have many years of experience working with global family businesses, and are well placed to identify and explore trends and cultural influences.

We hope that family business owners in Hong Kong and China will be inspired to celebrate these cultural trends in their quest for family harmony and business success.

Iggy Chong | *Managing Director*
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Methodology

This briefing paper on family businesses in Hong Kong and China has been written by the Coutts Institute, in collaboration with Ledbury Research, the wealth research specialists.

The trends contained in this paper reflect the views of our Advisory Panel of 11 leading consultants, educators and advisors, but do not necessarily reflect their individual positions, except where statements are directly attributed to them. This paper also references data gathered by the Coutts Institute and external research.

For Coutts clients seeking more information, Coutts offers a range of family business advisory services, publications and access to the Knowledge Exchange, an online interactive platform that brings together insights from Coutts in-house specialists, industry experts and clients from around the world.

FAMILY CULTURES IN CONTEXT

Greater China

Contemporary society in Greater China tends to attach a great deal of importance to the family as a basic social unit – diverging from recent demographic and societal trends prevalent in large parts of Western Europe, North America and Australasia.

In Greater China, commonly accepted as comprising the mainland, Hong Kong, Macau and Taiwan, family relationships tend to be governed by respect for the elder members, with the individual seen as secondary. This creates a dynamic whereby the senior members of the family continue to have a strong influence on the younger generation, particularly related to family unity and mutual respect.

As a result, tradition and cultural heritage teaches children to be obedient to the father as the head of the family. They both honour him during his lifetime and then his accomplishments after his passing. This often helps avert family conflict, especially when this core family value is successfully inculcated from a very early age. An indirect testament to this traditional core value can be seen, for example, when the second and third generations put less emphasis on re-inforcing it with their children.

In return, fathers are relied upon to give their sons a good start in life. They are responsible for educating them and mentoring them. Often, they also help them find a spouse and help provide them with a successful occupation or business. Daughters, on the other hand, are expected to take on another family name and share the wealth of their husband.

When the father passes away, the belief is that the mantle of authority passes to the eldest son. He is expected to be generous to his siblings while remaining respectful of his mother -- who often plays a pivotal role in maintaining strong family relationships.

Some say cultural influences like these are key drivers of success. Others say they are impediments to progress. The reality is that they can be both.

As mentioned on the cover, this report will specifically discuss family businesses in Hong Kong and Mainland China and the issues they face, even though the general cultural context can be seen as being reasonably relevant for Greater China as a whole, including elements of the diaspora, and other large communities of Chinese living overseas.

“修身 齊家 治國 平天下”

(Mencius 372 – 289 BC)

(“To govern the country (and bring peace to all), one should first be able to govern one’s family; to govern one’s family successfully, one should first learn to govern oneself.”)

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| 01 | TREND 1: COLLECTIVE OWNERSHIP

There are increasing numbers of family business owners who are not involved in the management of the family business

"In China and Hong Kong, it is traditional for ownership succession to follow the coparcenary principle where the male heirs are given equal shares in the business, and it is customary for the eldest son to take on leadership supported by his brothers," says Professor Kevin Au.

However "the probability that you have the best person to run the family business within the family isn't always very high" observes Annelie Karlsson. So perhaps it is not surprising that there are increasing numbers of family business owners who are not involved in the running of the business, signifying a break with tradition.

The survival of a family business that is owned but not managed by the family will depend on factors such as the relationship and communication between individual family members and between family and the non-family managers, the family's understanding and passion for the business and how business, family and individual interests are balanced.

Issues can arise if communication, decision making and planning are not transparent. For example conflict can occur when there are differences in opinion on whether profits should be given out in dividends or reinvested in the business. In addition, family owner-managers can resent the fact that non-family owner-managers are benefiting from their hard work.

There are also significant risks of conflict when shares pass to family members who are not working in, or interested in, the business or when a family member who is not working in the business receives more shares than a family member who is.

On the other hand, some family business owners see collective ownership as an opportunity to create a family consortium (jia-zuji-tuan) that allows individual family members to take responsibility for separate divisions and provides scope for the next generation to start their own businesses, expanding horizontally rather than vertically.

Dr Roger King notes that in young Asian businesses, the notions of the family and the family business are very closely intertwined, and that changes to one can have profound effects on the other. "If you start excluding people from the ownership, you virtually exclude them from being a member of the family." What is important is to 'give face' to the family and respect the family's heritage.

Potential family risks:

- Individual interests taking priority over collective interests or not being discussed
- Too much focus on treating children equally, but not treating them fairly as owners and/or managers
- Share dilution among family members who are not passionate about the business

Things that may help:

- Be clear about the different roles of owners and owner-managers, and ensure that performance review processes are in place for owner-managers
- Establish rules on how shares will be passed on and owned, and put in place exit procedures for anyone who may want to sell their shares
- Encourage regular meetings and social occasions amongst family shareholders

Talk to Coutts

- About creating an ownership succession plan

Results of a recent pulse survey by Coutts among Asian family business owners suggest that the majority of family business owners believe that the business belongs to the whole family.

	Strongly disagree	Slightly disagree	Neither disagree nor agree	Slightly agree	Strongly agree
Family members who don't work in the business should have the same right to ownership as those who do	10%	25%	8%	31%	25%

Source: Coutts' survey of Asian family business owners attending Family Business Forums in April and June 2012.

| 02 | TREND 2: APPOINTMENT OF NON-FAMILY MANAGERS

There is a growing move towards appointing non-family business managers in family businesses

Bringing in outside management to family businesses means challenging the traditional levels of trust in Hong Kong. Dr Roger King emphasises this point by saying that family business owners in Hong Kong and China "will not bring anyone in that they don't have prior knowledge of and feel is totally trustworthy."

For many families, it's not just the fear the patriarch might have of losing family decision making powers over the company. It's also the fear that the next generation might have about what happens to the balance of power after the patriarch has passed away.

Family members may also feel threatened by the introduction of new rules and procedures and concerned about replacing family members who can be trusted. Equally it might be about losing the social and intellectual capital that comes with the family's reputation and provides a competitive advantage for the company.

However, sometimes the reasons for making non-family appointments clearly outweigh the reasons for holding back. The business might get too big or complex for the family to manage or there might not be sufficient family interest or talent in taking the business forward, but it can also introduce new technical skills, a spirit of entrepreneurialism or challenge ineffective governance structures.

In Hong Kong and to a lesser extent in China, Professor Kevin Au observes that the supply of quality professional managers has increased over the last 10 to 12 years, contributing to this trend. Mr John Mok, Co-Founder & Chairman of AML Holdings Ltd also observes an increasing appointment of non-family professional managers & directors heading up Asian family business.

These non-family or 'professional' managers do not always replace family members. In some cases, they act as mentors for the next generation until they are ready for senior roles. This is common in Hong Kong and China, according to Juliette Johnson, "Knowing when it's time to call in outside help isn't easy. Often it can take either some very difficult conversations or some sort of emerging crisis to act as catalysts for looking at management," Juliette explains.

Introducing professional managers into family businesses is not without additional challenges, both for the outsiders and the family members. Professional candidates need to have what Dr Dennis Jaffe describes as "an exquisite sensitivity to family politics, and at the same time you have to create an agreement that allows you to negotiate and to deal with the family issues".

What families need to guard against, as Professor Nigel Nicholson starkly puts it, is "treating external professionals as pathogens to be killed off by the family's immune system". Discussing how this is best done, David Bork repeatedly stresses the importance of boundaries, which prevent family interfering with the professional's decision making and help ensure a more consistent family voice.

Potential family risks:

- Family loyalties concealing issues that threaten the performance of the business
- The absence of appropriate reward and recognition for non-family members
- Potential conflict between family members and professional managers over how decisions are made and who makes them

Things that may help:

- Perform an assessment on family leadership and management abilities
- Define roles and responsibilities of both family and non-family, and be clear who has the final say
- Prepare the family to embrace an openness to change

Talk to Coutts

- About getting the right balance between family control and effective management

Results of a recent pulse survey by Coutts among Asian family business owners suggest that the majority would prefer to see a family member at the helm (even though they no longer expect the next generation to come into the business – see Trend 6).

	Strongly disagree	Slightly disagree	Neither disagree nor agree	Slightly agree	Strongly agree
I am confident that the CEO role would be best filled by a family member over the next 10 years	4%	8%	8%	38%	42%

Source: Coutts' survey of Asian family business owners attending Family Business Forums in April and June 2012.

"Attracting professional managers to work in family businesses can be hard. The highest prize in the 'career tournament' – the CEO title – is often attached to family membership. This can make the career less attractive for professional managers in the long run."

Jeremy Cheng Chi Yeung, The Chinese University of Hong Kong Business School

| 03 | TREND 3: FOCUS ON VALUES

There is an increasing focus by family business owners on matching the values and cultures of new recruits to their own

When appointing professional managers, families aren't just looking at skills and experience, they also want to explore candidates' values, and whether these align with their own. As Juliette Johnson puts it "A family business that brings in a non-family member that doesn't share the company's values and respect its culture is asking for trouble."

A basic requirement for joining the business is knowledge of the values of the family business. Values often act as glue to hold the family business together and can be a differentiator for the business. Identifying what they are isn't always as straightforward as it sounds, particularly as businesses move into the third generation and beyond. Family members may have conflicting, vague and frequently idealised concepts, which will be difficult to communicate to outsiders.

Dr Annelie Karlsson has observed that families in Asia struggling with high turnover of non-family employees, are now asking themselves whether they need to be clearer about articulating who they are and what values they stand for.

"I think family businesses [generally] have got a lot of homework to do in terms of [accurately identifying] values, because it's easier to identify the nice values, instead of really getting to know the values for better or worse," says Dr Annelie Karlsson.

Ian Marsh notes that Eastern families typically don't discuss values in a formal way. " This is in part due to the prevalence of Confucian norms of harmony and hierarchy, guanxi (personal connection) and face concerns."

Dr Dennis Jaffe argues that families also need to think how these values need to evolve to meet the challenges that the business is facing. Whether these are written down in the Western way or verbally agreed in the Asian tradition, the important thing is that present and future values are properly discussed and agreed.

Another important consideration is the communication of values, to family and non-family alike. Stories illustrate how values should be lived in a way that appeals to the heart and remains in the brain, and can be told by different generations. David Bork mentioned that he liked to include an item on the agenda at family meetings called 'story time' when individuals have the opportunity to share stories about the family and how they have demonstrated their values.

Potential family risks:

- Confusion and conflict among family members because of different individual values and lack of understanding of family values
- Non-family employees not understanding or embracing family values which leads to them feeling disgruntled, causing a potential source of harm to the family and the reputation of the family business
- No action being taken when someone acts outside the family values

Things that may help:

- Ensure that family values are clearly articulated and understood by the family
- Distinguish between aspirational values and the values that the family live by. Think about the usefulness of stories in demonstrating values and how values may need to evolve in order to succeed in the future
- Ensure effective recruitment processes are in place to check that the values of professional managers fit with the business. Ensure non-family managers understand the importance of espousing family values

Talk to Coutts

- About agreeing a family code of conduct

Results of a recent pulse survey by Coutts among Asian family business owners suggest that family business owners are now testing the values of professional managers for a fit with their own.

	Strongly disagree	Slightly disagree	Neither disagree nor agree	Slightly agree	Strongly agree
Before employing any senior managers, we test whether they share the same values as our family's	4%	8%	8%	38%	42%

Source: Coutts' survey of Asian family business owners attending Family Business Forums in April and June 2012.

A famous story about filial piety (wo bing qiu li) gives an account of how a son gets fish for his sick mother by using the heat from his body to melt the ice on a river. The moral of the story is that children should sacrifice themselves for their parents.

"Wang Xiang lay on the ice on a river seeking fresh fish for his stepmother, who said all the bad things about Wang in front of his father. The ice broke all of a sudden – and two carps jumped up."

Wo Bing Qiu Li(臥冰求鯉) – one of the 24 Chinese traditional stories on filial piety

| 04 | TREND 4: FAMILY GOVERNANCE AWARENESS

Family business owners are increasingly aware of the need for good family governance, but often do not know where to start or what to do

Many first and second generation family business owners in China and Hong Kong believe that there is less need for formal family governance because it is commonly assumed that the patriarch dictates the decisions when alive, and custom and tradition provide sufficient rules that are morally binding, albeit unwritten.

It's also the case that, although there is more awareness of family governance nowadays, it's not widely understood and is often characterised as a Western export.

Nonetheless, the absence of any family governance is generally thought by family business experts to be one of the main reasons why family businesses fail, and there are so many high profile conflicts, especially as more family members become involved and authority devolves from one generation to the next.

Perhaps the best way of describing the importance of family governance in China and Hong Kong is that it helps to sustain family harmony. Family harmony is not guaranteed to last unless it is continually worked on and family governance provides a framework for reaching agreements and creating a climate for open and transparent decision making. Dr Roger King puts it this way "The continuity of the business and the continuity of family harmony are intrinsically linked."

Nonetheless it remains the case that the majority of family businesses haven't addressed the family element of governance effectively. Research by Egon Zehnder in 2011 found that just 25% of owners of family businesses in Asia Pacific said they have professional family governance procedures.

Barriers to establishing family governance could be the risk that challenging topics will be raised that the family does not want to, or is not equipped to, discuss, hence making it a difficult task.

Juliette Johnson believes this is the main obstacle to progress, "When something is difficult and you don't make it your top priority, then it continually gets pushed aside and left for another day. Additionally there is a concern that developing a governance and succession plan could create confrontation or conflict."

Part of this perceived difficulty stems from a general lack of knowledge about options. Dr Panikkos Poutziouris believes education is key here, specifically case studies which show how others have successfully tackled family governance. Appointing a qualified family business consultant can also play a key role in facilitating challenging family conversations and creating a safe atmosphere within which everyone feels comfortable in expressing their views.

The sophistication of family governance mechanisms should be determined by the financial and family complexities that exist, according to Dr Dennis Jaffe. Where there is low complexity, simple solutions like regular family meetings may be sufficient; while high complexity may call for solutions like shareholder committees, family councils or family charters.

Dr Roger King stresses that families don't necessarily have to adopt formal constructs like family constitutions and councils, what is much more important is that these issues are properly discussed with all the family members. He notes that this can be hard for the next generation in Asia to broach the subject of what happens after the patriarch dies – it would be seen as 'un-Asian' or 'un-Chinese'.

Potential family risks:

- Lack of communication and joint planning
- Inappropriate levels of informal and formal family governance
- Conflict arising from issues that could have been anticipated and planned for

Things that may help:

- Get 'buy-in' from the family to introducing a governance system
- Establish the criteria for involving family members
- Agree the process for discussing and recording governance policies
- Review the governance policies

Talk to Coutts

- About developing a family governance system

Results of a recent pulse survey by Coutts among Asian business family owners suggest that three out of every four individuals felt they needed a formal family governance system.

	Strongly disagree	Slightly disagree	Neither disagree nor agree	Slightly agree	Strongly agree
We need a formal internal family governance system for the family members (e.g. Councils, Constitutions, Charters)	0%	13%	10%	27%	50%

Source: Coutts' survey of Asian family business owners attending Family Business Forums in April and June 2012.

| 05 | TREND 5: NEXT GENERATION INDEPENDENCE

The next generation are thinking more about the pros and cons of joining the family business

For a long time, the next generation in Hong Kong would have said that they did not have any choice but to enter the family business. The same would have been said in China more recently. Now more next generation family members in Hong Kong and China are questioning the relative merits of joining.

The reasons for considering options outside the family business seem to range from the impact of a Western education to concerns about working under parental control and from wanting to start their own business to doing something entirely different. Mr John Mok, Co-Founder & Chairman of AML Holdings Ltd, observes that Western educated youngsters are increasingly reluctant to join their Asian family business, especially if their elders are non-professional hardworkers. Many of the next generation are also attracted by the potential of sectors such as technology and finance.

Dr Roger King observes that Chinese next generation returning from overseas universities, “come back and they look Chinese but they don’t think like Chinese anymore. So we see some cultural, I wouldn’t want to use the word ‘clash’, but clearly differences of opinion of how things should be done.” It’s also true to say that the better their educational qualifications the more opportunities the next generation have.

Whether their aspirations translate into actions are likely to depend on the strengths of family ties and pressures, with Dr Panikkos Poutziouris noting that for smaller families running larger businesses there is more pressure for next generation talent to be ‘repatriated’ after their foreign education. At the same time, Professor Nigel Nicholson, contends that dutiful children do return to the business, irrespective of their education.

Recently, Shanghai Jiao Tong University surveyed 182 leading Chinese family businesses operating in a variety of fields, and found that 82% of the owners were finding it difficult to convince their sons or daughters to take over from them (Ming Pao newspaper March 2012). The next generation said they were put off by the amount of sacrifice involved and a concern about being scrutinised and criticised by their elders. Losing face in front of family and non-family employees alike may also be a worry.

Filial piety in the patriarch’s mind, and a desire by the next generation to pursue their own ambitions, can create conflicts. As a result, recognising the aspirations of the next generation and sympathetically engaging with them is high on the list of priorities of family business owners around the world according to a recent research report entitled ‘Best Practices of Successful, Global, Multi-Generational Family Enterprises’ by Dr Dennis Jaffe with Jane Flanagan, Family Office Exchange’.

To promote the link between family businesses and the next generation, a couple of panellists stressed the importance of instilling pride in children about their business origins and keeping them updated on business progress.

Dr Roger King mentions a move by some families in Hong Kong and China to set aside funding specifically to support the entrepreneurial aspirations of next generation individuals after they have been educated abroad. These new ventures can serve not only to attract the next generation back to the family but also help to diversify the business and open up exciting growth possibilities. Key is getting the balance right between giving the next generation enough financial support to be meaningful, but not so much as to become meaningless.

Potential family risks:

- Dissonance of cultures and values between generations
- Negative attitudes toward the family business from the next generation if they feel that they cannot make their own career decisions
- Concerns that the next generation may have about working with parents and siblings, and being respected by non-family members

Things that may help:

- Promote the advantages of being part of a family in business together
- Create a climate that allows the next generation to talk openly about their aspirations and expectations
- Consider a mentor to offer the next generation independent support and guidance

Talk to Coutts

- About career planning for the next generation

Results of a recent pulse survey by Coutts among Asian family business owners suggest that only 16% expect the next generation to be involved in the running of the family business.

	Strongly disagree	Slightly disagree	Neither disagree nor agree	Slightly agree	Strongly agree
I am confident that the first choice career for my children when they finish their studies will be joining the family business	31%	31%	21%	10%	6%

Source: Coutts' survey of Asian family business owners attending Family Business Forums in April and June 2012.

"When I initially took over the baton of general manager, my office was located in the position opposite to the stairs, while my father's, who is still the president, stands at the end of the corridor. The purpose of this arrangement is to assure that business affairs can be directly reported to me. However, in practice, most of the subordinates are still heavily dependent on my father. When they have something to report, they will reluctantly, at first, come to my office; if I am absent, they will 'happily' walk straight to my father's office."

(Source: The succession process in Chinese family firms: A guanxi perspective, Junsheng Dou, Shengxiao Li)

| 06 |

TREND 6: FEMALE EXECUTIVES IN SENIOR ROLES

More women are willing and able to take senior, visible roles within the family business

The fact that power and authority traditionally resides with men in family businesses in Hong Kong and China partly explains why there are not more women in the boardroom, although women do have a more established presence in the professions, academia and local politics.

Although there are still issues in attracting women, it is becoming more acceptable in Asia for women to hold senior positions in family businesses. In some cases, it might be the result of China's one child policy, the absence or indifference of male heirs or the death of the patriarch.

In other cases the role might be temporary. Professor Kevin Au comments that even if a woman has held a senior position for some time, she may be asked or expected to take another role or even leave the company, when a brother joins the business.

Dr Roger King makes the point that family businesses have been ahead of the pack generally when it comes to the advancement of females in the workplace. Women also play key roles in developing and safeguarding family values and relationships and Coutts has observed an emerging involvement of women in philanthropy.

Most importantly, women can be better at getting the family to work together. In the book 'Family Business Key Issues', chapter contributors Dr Annelie Karlsson and Joseph Astrachan note that women often play important parts in managing social capital. "Entertaining, for example, is not only a private affair, it is also a strategy for converting social networks into financial gain.

Somewhat controversially, Juliette Johnson argues that the choices of women themselves are holding back their progression. She says that while there are increasing opportunities for women, they are still choosing not to join the family business because they have got other priorities in their lives. However Juliette also thinks that many family business owners are recognising this challenge and using the family business to create a more flexible environment than traditional non-family businesses. This enables more women to be able to balance their priorities between home and work.

Whatever the obstacles for women and for the businesses, there is a compelling case for encouraging more women into and up the organisation if their skills meet the needs of the business, and families need to be addressing the remaining barriers and even thinking about ways to help women get ahead. In this regard, Professor Nigel Nicholson stresses the importance of open communications and decision-making to encourage female involvement.

Potential family risks:

- Not recognising the important role women play behind the scenes
- Preferential treatment of male candidates for senior roles, even if female candidates have a stronger skill set for the job
- Loss of female family members to competitors and other industries if family business owners cannot encourage and retain senior female talent

Things that may help:

- Create a climate of meritocracy, where talented women are invited to apply for leadership roles and treated fairly in the selection process
- Look at ways to attract women into the family business and be creative about adapting traditional business procedures to make them more women-friendly
- Ensure women have the right development plans in place and support networks at home and work

Talk to Coutts

- About conducting an independent family skills assessment

Results of a recent pulse survey by Coutts among Asian family business owners suggest that there is growing recognition of women in leadership positions.

	Strongly disagree	Slightly disagree	Neither disagree nor agree	Slightly agree	Strongly agree
Within family businesses in general, women are being invited to take up senior management roles	2%	8%	29%	42%	19%

Source: Coutts' survey of Asian family business owners attending Family Business Forums in April and June 2012.

"Ms Aw who has been running the Sing Tao Daily for forty years since her father died was recently quoted as saying 'I don't think I behave differently from men, but in meetings I always find myself as the only lady.'"

(The New York Times, January 1996)

| 07 | TREND 7: WEALTH CREATION

There is an increasing focus on wealth creation, and openness to think about trade sales and IPOs

The term family enterprise is becoming more prevalent as family business owners and experts alike comment on how families are transitioning from owning a single business to owning a portfolio of assets that might include property, liquid investments and equity stakes in other businesses.

This is particularly relevant in China and Hong Kong where over two thirds of family businesses in the recent Coutts pulse survey said that they were considering wealth creation strategies.

One of the key drivers for realising cash is undoubtedly the global economic crisis which has challenged assumptions about risk and financial security. "People want to make sure that not all of their eggs are in one basket," says Juliette Johnson. "I think if the current financial crisis has taught them anything, it is that."

Other drivers include diversification and sale of non-core assets. Professor Kevin Au mentions that increasing numbers of private equity companies are coming to China offering more opportunities for family businesses. Dr Roger King suggests that in China and Hong Kong a public listing might also be about "recognition and reputation building".

IPOs do, however, bring a range of other costs and complexities, which need to be carefully weighed up by family businesses. These may include changes to corporate governance, the introduction of independent directors, and measuring performance against short term goals.

In addition, liquid wealth obviously requires managing, and some families are electing to create family offices for this purpose. Indeed, Ian Marsh notes that increasingly the role of the next generation in more established Asian businesses is 'running money', or looking after the wealth created by past generations.

Family governance, succession and communication are just as important as more wealth becomes liquid and family members transition from being part of a 'family business' towards being a 'family in business'.

Families shouldn't feel eternally bound to their businesses, and should consider what is best for the family, contends Ian Marsh. "I don't think any given family should stay in business or any given business should stay in family just for the sake of it. Sometimes it's right for the family to exit, take that money and do something else with it. The worst outcome you can have is a family that shouldn't be in business together, staying together. You end up with the business going down the tubes because they're too busy fighting and the destruction of family relationships."

Potential family risks:

- Conflict between the liquidity needs of individual family members, the family as a whole and the business
- The absence of a strategic financial plan
- Loss of significant amounts of liquid wealth through misjudged investments made by family members

Things that may help:

- Prepare the family emotionally for life before, during and after sale of all or part of the business
- Design a wealth management strategy to achieve the right balance between individual and business needs and risks and returns
- Agree a clear and fair distribution policy within the family to avoid conflict over 'who gets what' in the future

Talk to Coutts

- About wealth succession and developing a wealth management strategy

Results of a recent pulse survey by Coutts among Asian family business owners suggest that over two-thirds are considering a liquidity event for some or all of their businesses.

	Strongly disagree	Slightly disagree	Neither disagree nor agree	Slightly agree	Strongly agree
We are considering wealth creation strategies (e.g. trade sales and IPOs) for some or all of the business	8%	0%	25%	48%	19%

Source: Coutts' survey of Asian family business owners attending Family Business Forums in April and June 2012.

| 08 | TREND 8: TRANSFER OF SOCIAL CAPITAL

Family business owners are grappling with how best to transfer social capital/networks to the next generation.

Professors of management and social studies have been teaching the importance of social capital and social networks in achieving corporate and personal success for some time now. Historically referred to in Chinese society as Guanxi networks, they are characterised by strong interpersonal social and business connections built on mutual commitment, trust and obligation.

It's not just the combination of formal and informal business networks of customers, suppliers, staff and bankers that the current generation will have nurtured over long periods of time. It has just as much to do with long standing political, religious, social and other connections. These contacts can be as valuable as anything on their companies' balance sheets. According to Professor Kevin Au, they can also represent the power base of the family business.

Passing these contacts on to the next generation can be essential in sustaining the unique identity of a family business, but it is not easy to answer questions of how, when and who to. Social capital is traditionally transferred to the heir apparent. Many families in China and Hong Kong rule out non-family members. In some cases it may not be possible to transfer these connections at all.

"Some of the families I've come across in China, are consciously making efforts to grow the social capital of the next generation owners. Because, as they say, if our managers are the ones with the most social capital, why would they stay with us instead of starting up their own business?" notes Dr Annelie Karlsson.

Dr Roger King thinks that these families are correct to take this stance. "Social capital is the one thing you should keep within the family." He notes that for certain types of businesses in Asia, social capital is the only source of differentiation there is between businesses.

If connections are to be transferred to another family member, then families need to decide who this is, recognising that there is likely to be a preference for dealing with the member of the family who has ultimate power long-term. Encouraging the next generation to create their own networks through their university, clubs or social media contacts is equally important.

Potential family risks:

- Lack of understanding by the next generation of the vision for the business and the importance of social capital to this
- Damage to relationships with customers, suppliers and key influencers, if succession is not planned
- Risks of transferring harmful social/business networks

Things that may help:

- Ensure the next generation understand the importance of social/business networks to the business
- Consider having more than one family member involved in the most important business relationships
- Encourage the next generation to join Chambers of Commerce, trade associations and professional organisations

Talk to Coutts

- About developing a programme for the next generation to learn about the family business

"A great gap gradually emerged in my heart during the initial periods after entering our firm. I always felt that no more than 10% of my knowledge learned from classes abroad can be used in my work, this puzzled me heavily. Later, father-in-law told me that, 'now what you need to learn is 'sociology', only when you master it, two or three years later, and effectively integrate it with your academic management knowledge, can you indeed become a qualified general manager.'" – the founder's daughter-in-law

(Source: The succession process in Chinese family firms: A guanxi perspective, Junsheng Dou, Shengxiao Li)

COUTTS INSTITUTE

The Coutts Institute provides specialist family business and philanthropy advice. We support clients and their families wherever they are located, including the UK, Russia CIS, Switzerland, Asia, and the Middle East. We also run a programme of family business and philanthropy forums on current issues and produce a series of family business and philanthropy handbooks and thought leadership pieces. In addition, clients benefit from access to the Knowledge Exchange, an online platform consisting of topical research and video interviews. www.coutts.com/knowledge.

Family Business

The key to a healthy family business is careful planning and open communication. Our family business experts are an invaluable resource when clients are tackling issues such as family governance, ownership succession and leadership development. In addition to Coutts family business advisory services, the Coutts Forums for Family Business Owners and Coutts family business publications provide important connections and insights.

Philanthropy

At Coutts we recognise there is no single way to conduct philanthropy, and the options open to those who want to make a difference are more varied and exciting than ever. Our philanthropy experts provide clients with essential advice, education and research in areas such as creating a giving strategy, giving as a family and preparing the next generation to give. In addition to Coutts philanthropy advisory services, Coutts Forums for Philanthropy and Coutts philanthropy publications, Coutts provides a 'one-stop-shop' for trust, tax and estate planning, managing charitable endowments and charity banking.

To find out more about the Coutts Institute, please contact your Private Banker or visit www.coutts.com/private-banking/coutts-institute

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"For a family governance to work, it must be able to act for all rather than in the narrow self-interest of a few family members. It must be sufficiently flexible to the family complexity as it grows. Challenges and opportunities are always ahead. Without the family's total commitment, both the family and the family business cannot perpetuate over generations. The eight trends contained in this paper are faced by enterprising families every day." Mr Eddy Lee, Director, Lee Kum Kee Company Ltd.

"Coutts insightful report & thoughtful advice will definitely benefit the consider-to-retire and the consider-to-succeed generations of many family businesses like ours, Asian or not." Mr John Mok, Co-Founder & Chairman of AML Holdings Ltd, Chairman of SME Committee of HKIoD, Technopreneurship Mentor and Angel Investor.

"This publication is about how to succeed as a Chinese family business owner. It highlights the importance of respecting the family's heritage, establishing close communication and defining clear family roles. It also addresses the need to professionalise the business, the requirement for proper training and mentorship of the next generation by experienced business leaders and the importance of social capital as an asset." Dr Wong Kam Shing, Managing Director, Kowloon Watch Company Ltd.

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