Private Equity in Family Firms

A report on private equity investments in
family firms across Europe

from

The Centre for Management Buy-out Research

Rod Ball
Andrew Burrows
Carole Howorth
Oliver Kloeckner
Louise Scholes
Paul Westhead
Mike Wright

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THE CENTRE FOR MANAGEMENT BUY-OUT RESEARCH
FOUNDED BY
Barclays Private Equity
AND
Deloitte.
AT THE
NOTTINGHAM UNIVERSITY BUSINESS SCHOOL

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Contents

Introduction 1

Executive Summary..2

Overview of the Family Firm Buy-out Market 2
Succession in Family Firms 3
Strategic Changes Post Buy-out.. 4
Professionalization, Stewardship and Performance 5

Section 1: Buy-outs/ins in Family Firms – A Statistical Overview 6

Introduction.. 6
Market Overview 7
Deal Size 8
Share of Total Buy-out/in Market.. 10
Company Size by Employment.. 13
Industry Distribution.. 14
Type of Deal 15
PE-Backed Deals 16
Deal Structure 18
PE Multiples... 19
Management Participation 19
Exits 20
Holding Periods 22
Appendix.. 24

Section 2: Succession in Family Businesses through Private Equity Backed Management Buy-outs and Buy-ins 30

Introduction.. 30
Information Asymmetries 30
Succession Planning... 32
Business Sale Negotiation Behaviour 33
Role of Private equity Firms 36

Section 3: Changes in Strategy of Former Family Firms after Management Buy-outs and Buy-ins...38

Introduction.. 38
Implications.. 42

Section 4: Professionalization, Stewardship and Performance: Family Firm Buy-outs..44

Introduction.. 44
Professionalization... 45
The Staying Power of Stewardship.. 48
Linking Professionalization to Firm Performance 49
Implications.. 51

Introduction

The European private equity market (management buy-outs and buy-ins) has grown in prominence over recent years with CMBOR figures showing the numbers of deals conducted rising from 1212 in 1998 to 1436 by the end of 2007. One of the most important features of this market has been the growth in buy-outs of family/private firms from 451 in 1998 to 559 in the past ten years with the combined value of these deals rising from €11.2 billion to €18.3 billion during the same period. This report aims to provide a detailed insight into the issues surrounding buy-outs of family firms using the unique data from the CMBOR database of over 26,000 European buy-outs in addition to three other detailed studies of the family buy-out market.

The first section of this report is based on data from the CMBOR database and gives a detailed breakdown of aggregate market statistics for family buy-out in Europe. This includes data such as the value and volume of buy-outs, employee data, deal pricing and structuring data, industry sector analysis as well as the exiting of family firms.

Section 2 looks at the problems faced by family firms when dealing with succession. In this part of the report issues covered include those surrounding the way that information flows between vendor and acquirer impact the transaction process and the level of planning undertaken by family owners with regard to succession.

In the third part the emphasis is on strategic issues surrounding family firm buy-outs. We examine whether there are distinct differences in the strategy of family businesses post buy-out and relate these to the ownership and governance of the firm pre buy-out.

The final part analyses the changes in managerial style which can occur after a family firm has undergone a buy-out. We examine whether there is a move away from the more family orientated stewardship form of management to an approach characterised by more formal governance with mechanisms of planning and control.

Executive Summary

This report presents the findings from four related studies of buyouts of family firms. The principal findings from each study are as follows:

Overview of the Family Firm Buy-out Market

Buy-outs of family/private firms represent a significant part of the overall buy-out market in Europe. The following data gives an insight into the different aspects of this market with the main findings showing:

- There were 559 European buy-outs of family firms in 2007. The aggregate value of these deals was €18.3 billion.
- The main markets for buy-outs of family firms in 2007 were the UK (272), France (88), Denmark (33) Germany (30) and the Netherlands (27).
- While the average deal size of all buy-outs has been increasing and now stands at €119 million (2007), average deal size for family firms has been much lower and relatively stable and was only €33 million in 2007.
- Since 2000 buy-outs of family firms have represented 23-38% of the overall buy-out market in terms of number of transactions and 6-15% in terms of value.
- In Italy, France, Spain and the UK, buy-outs of family firms make up about one third of the market (measured as a ten-year average).
- In terms of the number of employees, the average size of a family firm at the time of buy-out has varied between 194 and 480 over the past ten years.
- Family firm buy-outs in Germany have on average 794 employees, much more than elsewhere in Europe.
- Buy-outs of family firms have a very similar industry distribution to all buy-outs with Manufacturing, Business Services and TMT being the dominant sectors.
- The proportion of buy-ins compared to all buy-outs/ins involving family firms has steadily increased over the past ten years (in line with the buy-out market as a whole). Over the last three years, half or more of the transactions involving family firms were buy-ins.
- The majority of buy-outs/ins of family firms are PE-backed (10 year average of 62%).
- Price-earnings ratios of buy-outs of family firms are in line with the respective figures for all buy-outs.

- Management teams of buy-outs of family firms hold on average an equity share of 46% after the transaction. This is about 3% higher than the equity stake of management teams of all buy-outs.

- Average time to exit for PE backed buy-outs of family firms is 58 months. This holding period has increased over the last 10 years and is about the same as the respective value for all buy-outs.

- In family firms there were slightly more secondary buy-outs and receiverships and slightly fewer trade sales and IPOs than for buy-outs as a whole.

Succession in Family Firms

Management buy-outs and buy-ins are emerging as an important alternative to inter-generational transfer of ownership in family firms. Based on a survey of 117 buy-outs of private family firms across Europe, the main findings concerning the effect of differences in information sharing between vendors and purchasers on succession planning and deal negotiation are as follows:

- 43% of respondents reported that the vendor and management shared relevant information equally, 21% suggested the vendor controlled all of the information, 21% indicated that the vendor controlled most of the information, 15% suggested that management controlled most or all of the relevant information.

- For over a fifth of respondents there was no succession planning. Only a third of respondents had planned succession two or more years before the event.

- Almost a half (46%) of respondents indicated a mutually agreed price had not been negotiated, amongst which 27% reported the vendor proposed a fixed price that maximised their valuation. A further 11% reported that the vendor had suggested a fair price that was in the best interests of the company.

- There are lower information asymmetry problems if family firm vendors and the existing management team are equally involved in succession planning.

- There is a greater emphasis on returns on shareholder equity where negotiation involves mutually agreed prices.

- Negotiations are less likely to involve a mutually agreed price where the succession process is driven by the vendor.

- A mutually agreed sale price between the vendor and the acquiring management is unlikely if the private equity firm is involved in discussions regarding succession planning.

- The finding that the vendor controlled all or most of the relevant information in MBIs highlights the problem for outside purchasers and suggests the need for caution in the negotiation of these deals.

- The link between private equity firm involvement in discussions about succession and a lower incidence of a mutually agreed price suggests that the experience of private equity firms puts them in a stronger position to negotiate with the vendor than is the case for management.

- The link between management control of the relevant information and a lower likelihood of a mutually agreed price highlights that in some family firms, management are in a stronger position to negotiate succession. This suggests that vendors may need to take independent advice in negotiating the sale process.

Strategic Changes Post Buy-out

This study examines how family firm company characteristics before and after a buy-out determine the degree and focus of strategic changes post buy-out. The characteristics under examination are founders' involvement pre-buy-out, ownership stake of non-family management pre-buy-out, existence of non-family non-executive directors pre-buy-out, management and private equity firm participation in succession planning and leverage after buy-out. Results are based on responses from 108 private family firms across Europe which had a buy-out funded by private equity between 1994 and 2003.

- In general, the strategic objectives of firms post buy-out emphasize improving efficiency and fostering growth and expansion.

- Among the objectives linked to efficiency improvements, increasing net profit and cash flow from operations became the two most important strategic objectives post buy-out.

- Among the objectives linked to growth and expansion, sales growth and long-term profitability were paramount.

- If non-family managers had no equity stake before the buy-out, greater strategic changes were implemented with regard to efficiency gains and to growth and expansion post buy-out.

- In firms without non-family non-executive directors prior to the buy-out, strategic changes were stronger in both efficiency gains and growth/expansion.

- Leverage did not seem to have an effect on changes in strategy after the buy-out.

Professionalization, Stewardship and Performance

This study examines whether management buy-outs (MBOs) and buy-ins (MBIs) of private family firms increase the professionalization of these businesses, whether elements of a family stewardship culture survive, and their impact on firm performance. Eight UK family businesses that underwent an MBO/I in 1998 were tracked up to 2006.

- There was evidence of professionalization prior to buy-out, often as part of the preparation for succession.

- The professionalization of family firms concerns the utilisation of formal governance mechanisms, the utilisation of formal strategic planning and control systems, and the involvement of non-family members on the board as well as the management team.

- The level of professionalization increases following a buy-out. Professionalization is, therefore, a continual process.

- Elements of stewardship were present in all surviving firms. This was demonstrated by an attachment to the firm, a long-term view, and the prioritising of the firm's objectives over personal ones.

- There was an appreciation of the history of the firm and the contribution of long-standing employees.

- The highest performing firms showed a stronger emphasis on strategic planning and specific goal setting and maintained continuity pre and post-MBO/I.

- Neither of the firms that had closed had maintained any elements of stewardship or continuity. However more successful firms removed the negative aspects associated with a family firm such as free-riding, shirking and inequitable treatment.

- Succession through MBO/I can enable the family firm to maintain its independent ownership and sustain the notion of stewardship of the organisation over time, albeit in a metamorphosed state.

- A buy-out may be an important transitory phase to enable necessary professionalization in a family firm that may otherwise be difficult to achieve.

Section 1: Buy-outs/ins in Family Firms – A Statistical Overview

Introduction

Private and Family firms[1] provide a constant and abundant source of potential targets for private equity (PE) companies. Buy-outs/ins of family firms enable the resolution of succession problems and, by rejuvenating strategic management, can improve operating efficiency and enable growth.

This analysis aims to shed light on buy-outs of family firms and for the first time presents statistical data on different aspects of this important part of the buy-out and private equity market.

All data refer to buy-out/in transactions of family firms unless otherwise stated and all data refer to Europe[2] unless otherwise stated.

The following aspects of the market for buy-outs/ins of family firms are covered:

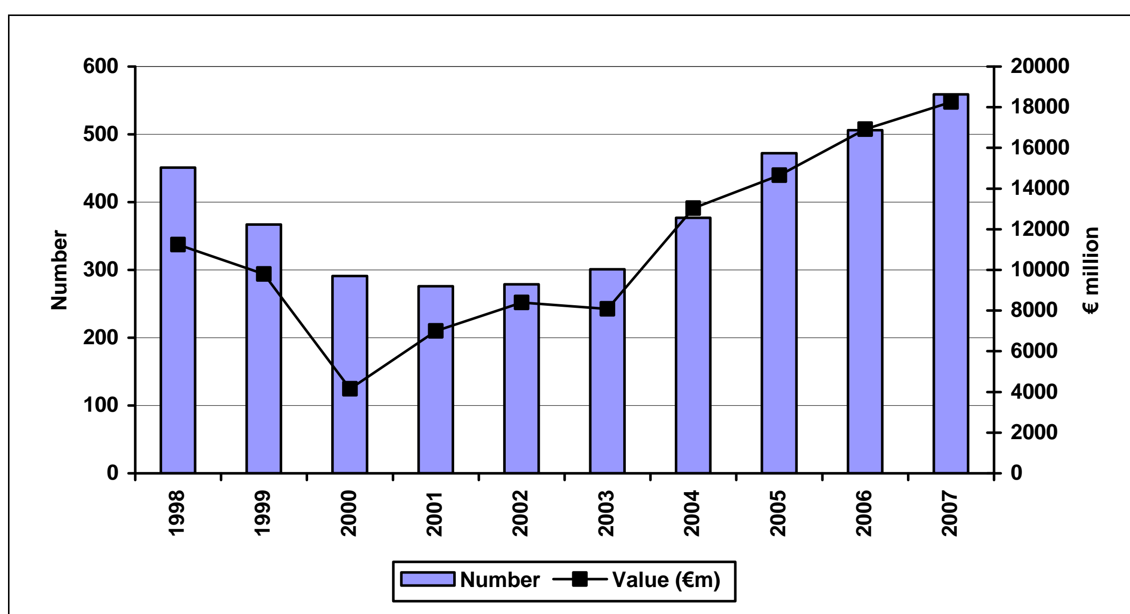
- Market Overview
- Deal Size
- Share of Total Buy-out/in Market
- Company Size by Employment
- Industry Distribution
- Type of Deal
- PE-backed Deals
- Deal Structure
- PE-multiples
- Management Equity Participation
- Holding Period
- Exits

[1] Henceforth referred to as family firms
[2] Europe = Austria, Belgium, Denmark, France, Finland, Germany, Ireland, Italy, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, UK

Market Overview

In 2007, 559 family firm buy-outs and buy-ins were recorded by CMBOR across Europe, amounting to a total value of €18.3 billion. There had been a dip in buy-out activity between 2000 and 2003, which was in line with a somewhat weaker overall buy-out market during that period. Since then buy-out activity in family firms has recovered and the 2007 figure was a new record by number and value (Figure 1.1).

Fig 1.1: Trends of Buy-Outs/Ins in Family Firms



Source: CMBOR/Barclays Private Equity/Deloitte

Table 1.1: Number of Buy-outs/ins in Family Firms

Country Name	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Austria	2	0	1	0	2	3	1	4	3	2
Belgium	5	8	10	5	1	3	5	11	12	13
Denmark	3	4	3	1	2	3	2	8	10	33
Finland	1	3	1	6	2	6	7	10	7	4
France	57	43	45	37	28	43	59	91	73	88
Germany	22	9	10	5	18	9	15	26	39	30
Ireland	5	1	2	2	1	3	3	4	3	3
Italy	20	17	11	7	11	12	11	23	29	26
Netherlands	21	13	11	13	8	10	14	17	24	27
Norway	1	2	0	2	3	3	1	6	5	6
Portugal	0	0	0	1	0	0	0	1	0	3
Spain	15	10	10	7	9	14	13	22	28	23
Sweden	4	5	5	3	6	5	10	9	11	21
Switzerland	16	16	14	8	3	6	7	12	9	8
Total (CE)	**172**	**131**	**123**	**97**	**94**	**120**	**148**	**244**	**253**	**287**
UK	279	236	168	179	185	181	229	228	253	272
Total (inc UK)	**451**	**367**	**291**	**276**	**279**	**301**	**377**	**472**	**506**	**559**

Source: CMBOR/Barclays Private Equity/Deloitte

A comparison of trends by country reveals that the increase in deal numbers has been relatively uniform across most of Europe. Over the past ten years, buy-out activity in terms of number of transactions has increased in most national markets (Table 1.1).

Table 1.2: Value of Buy-outs/ins in Family Firms (€m)

Country Name	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Austria	27	0	80	0	6	103	25	109	81	6
Belgium	219	197	205	1521	3	208	784	830	82	450
Denmark	44	447	70	384	159	93	39	416	599	2546
Finland	10	9	2	59	215	10	22	23	31	26
France	3088	991	644	650	948	1135	3228	2312	1685	3552
Germany	842	1743	258	166	2084	1097	2079	2117	1676	1914
Ireland	62	14	35	10	20	20	45	24	25	90
Italy	547	1426	476	217	277	700	329	1872	1660	1035
Netherlands	696	435	159	62	312	639	711	434	677	316
Norway	3	5	0	220	43	32	300	232	211	29
Portugal	0	0	0	2	0	0	0	25	0	18
Spain	257	444	198	359	339	411	172	526	2389	2703
Sweden	195	59	60	10	228	343	185	508	483	261
Switzerland	908	352	331	24	34	73	260	590	366	224
Total (CE)	**6898**	**6122**	**2518**	**3684**	**4668**	**4864**	**8179**	**10018**	**9965**	**13170**
UK	4346	3679	1637	3313	3736	3220	4858	4643	6957	5088
Total (inc UK)	**11244**	**9801**	**4155**	**6997**	**8404**	**8084**	**13037**	**14661**	**16922**	**18258**

Source: CMBOR/Barclays Private Equity/Deloitte

The total value of family firm buy-outs has fluctuated on an annual basis in many of the European markets and no clear pattern has emerged (Table 1.2). However, due to the rise in number of this type of buy-out the total value reached a new record of £18.3 billion in 2007.

Deal Size

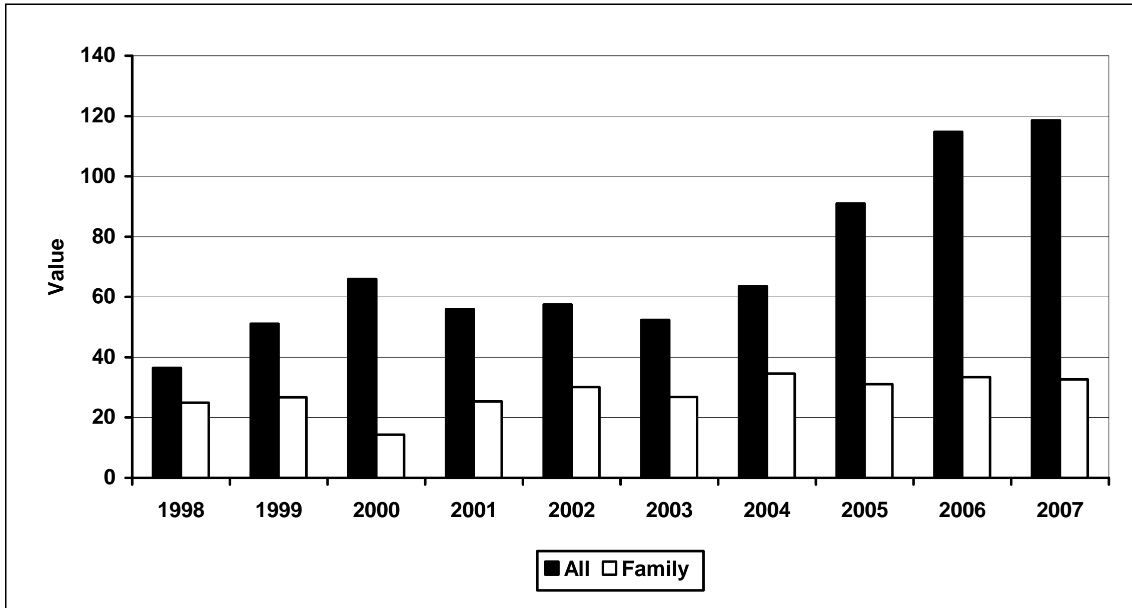
The trend in the average deal size of family buy-outs over the past ten years shows that these deals have remained at a relatively constant level of about €26m while average deal size for all buy-outs has increased significantly from €36m in 1998 to almost €120 million in 2007 (Figure 1.2).

It is clear that the average deal size of buy-outs of family firms is much lower compared to the average deal size of all transactions. This gap has been far more pronounced in recent years as European buy-out market value has soared due to an increase in large public to privates, divestments and secondary buy-outs.

An analysis of the distribution of buy-outs/ins according to their deal size indicates that there are fewer family firms involved in larger transactions of more than €50m than for all buy-outs. In contrast, for deals below €50m there are more family firms involved.

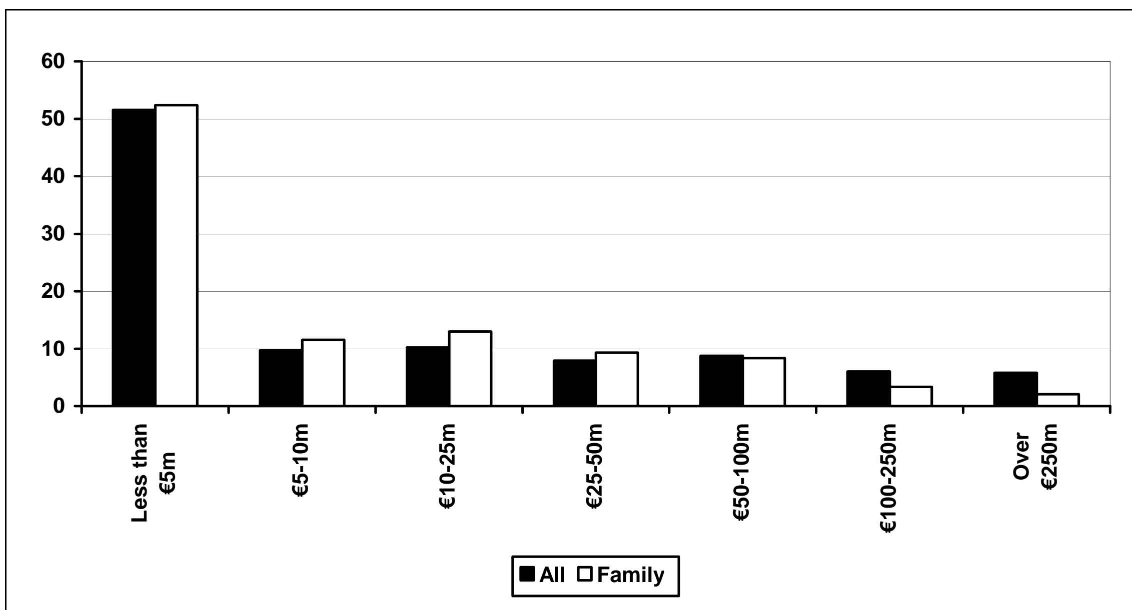
The smallest transaction category involving deals below €5m is dominated by buy-outs of family firms.

Fig 1.2: Average Deal Size for Buy-Outs/Ins (€m)



Source: CMBOR/Barclays Private Equity/Deloitte

Fig 1.3: Buy-Outs/Ins by Average Deal Size - 10 year average (%)



Source: CMBOR/Barclays Private Equity/Deloitte

Table 1.3: Major Buy-Outs/Ins in Family Firms

Company name	Country	Year	Value (€m)
Caudwell Holdings	UK	2006	1627
Louis Dreyfus et cie	France	2007	1450
Telenet Holding	Belgium	2001	1403
Friedrich Grohe	Germany	1999	1372
Beaufour Ipsen	France	1998	1347
Bureau Veritas	France	2004	1332
Linpac/Picnal	UK	2003	1244
Littlewoods/LW Investments	UK	2002	1194
CBR Holding	Germany	2004	1000
Dako	Denmark	2007	970
Iberostar /Turmed/Orizonia	Spain	2006	900
Formula One/Slec/Alpha Prema	UK	2005	840
Piaggio Veicoli	Italy	1999	776
Occidental Hoteles	Spain	2007	706
Matas	Denmark	2007	696
British Car Auction	UK	2006	658 (est)
Balta Group/BG	Belgium	2004	620
Avanza	Spain	2007	600
EWT	Germany	2005	600
Foxtons and Alexander Hall Associates	UK	2007	575
International Management Group (IMG)	UK	2004	559
Altice One	Belgium	2005	525

Source: CMBOR/Barclays Private Equity/Deloitte

The largest buy-outs of family controlled firms are shown in Table 1.3. Caudwell Holdings in the UK is the largest family firm buy-out on record at €1.6 billion. In 2007 Louis Dreyfus was sold in France for over €1.4 billion.

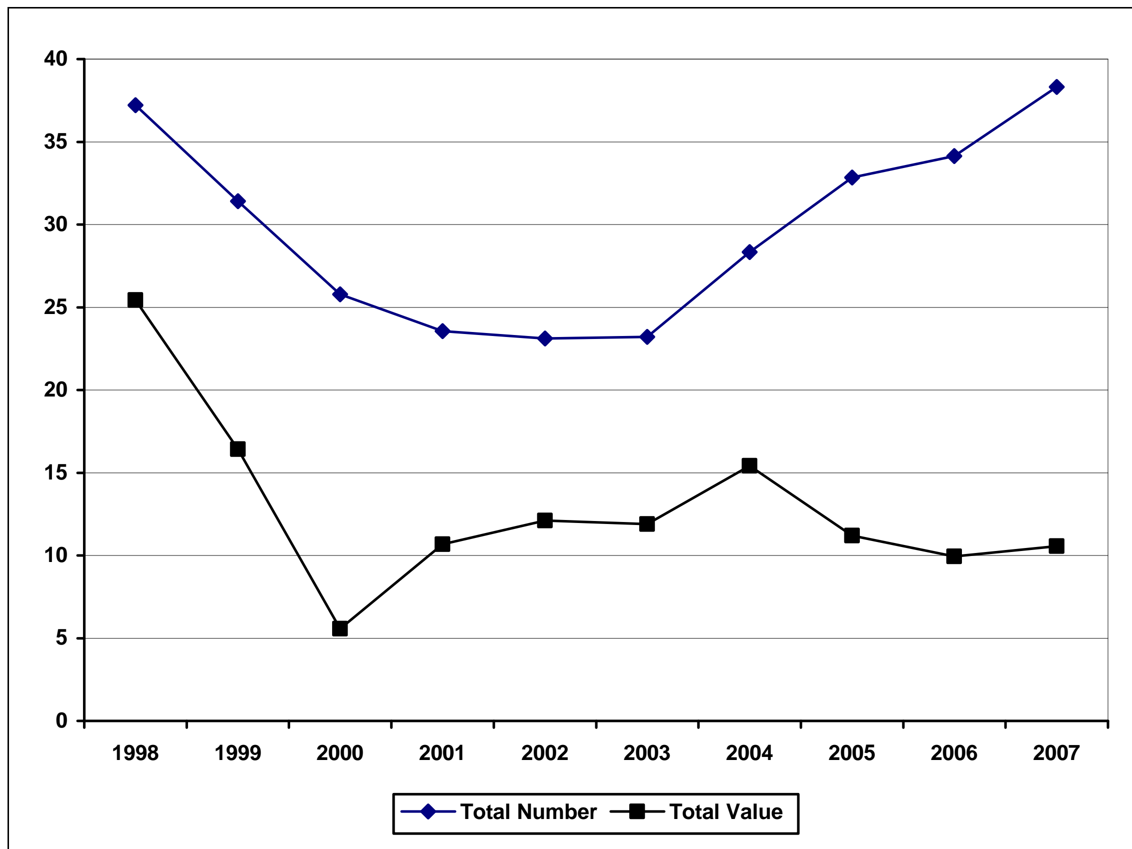
Share of Total Buy-out/in Market

Family firms have been a constant and abundant source of buy-outs/ins. Between 1998 and 2007 about 29% (based on the number of deals) of all buy-outs in Europe were family firm transactions. However, these deals only represent 11% of the total value of all buy-outs over this period, further underlining the fact that buy-outs in family firms are generally much smaller than other types of buy-out.

Over the last 10 years, the proportion of the buy-out market accounted for by family firm deals decreased until 2002 (23.2%) and started to rise again in 2004 to reach 38.3% of deal numbers by the end of 2007 (Figure 1.4).

The proportion of the total market accounted for by family firm buy-outs based on total value also saw a sharp decline from 1998 to 2000. Since then the value of family firm buy-outs has fluctuated between 10 and 15 per cent of total market value.

Fig 1.4: Buy-outs/ins in Family Firms as a Share of all Buy-outs/ins (%)

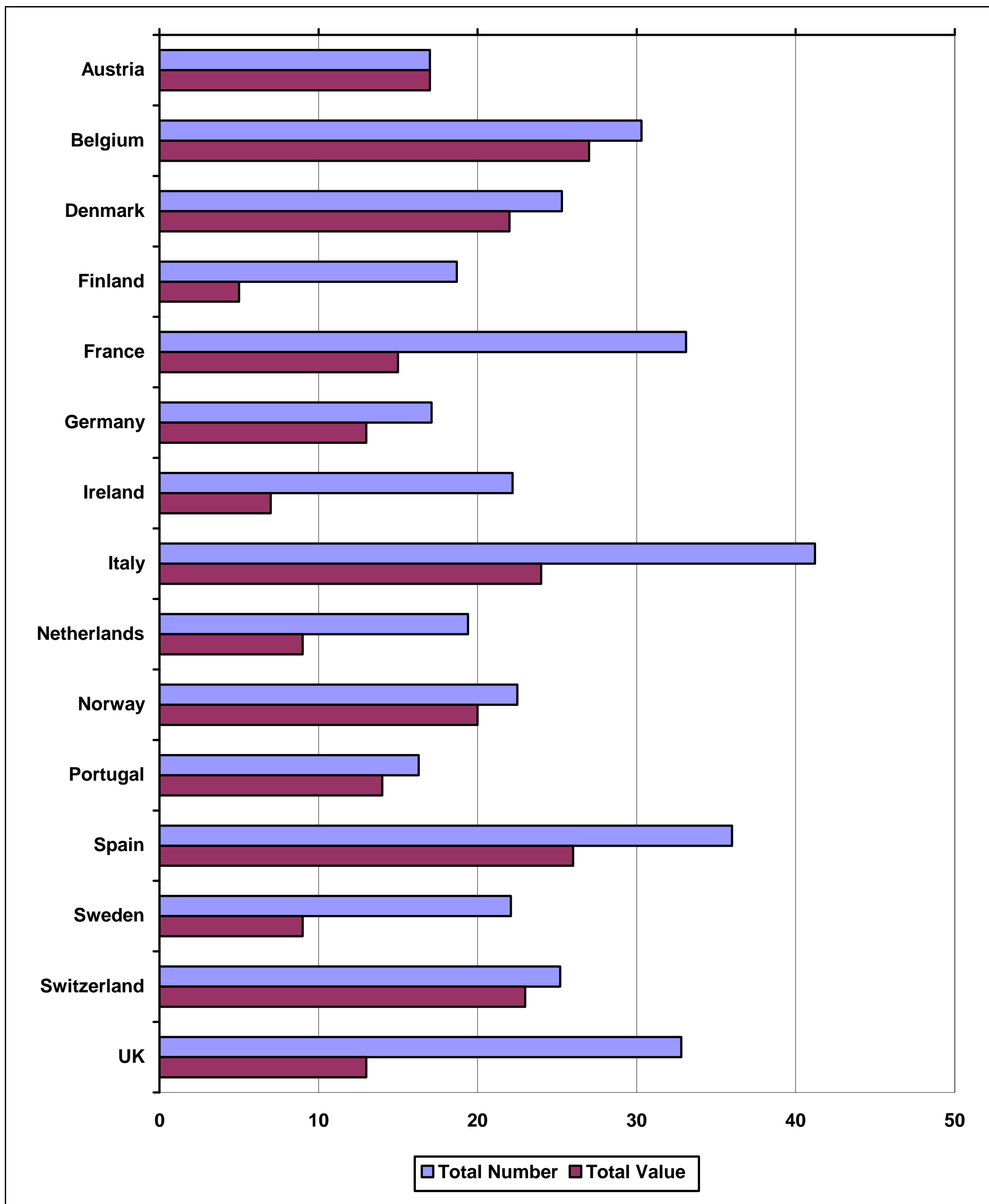


Source: CMBOR/Barclays Private Equity/Deloitte

A national comparison of the ten year averages of the share of the buy-out market attributable to family firm deals shows significant variation between countries. In France, Italy, Spain, and the UK this proportion is a third or more of all transactions in terms of deal numbers. A possible reason might be that these countries contain a considerable stock of family firms, thus fuelling buy-out transactions.

Germany shows a surprisingly low market share given its huge number of family-owned Mittelstand companies. This may be linked to the general poor understanding and possible mistrust of private equity and also the close links German companies have had historically with their local banks (Figure 1.5).

Fig 1.5: Buy-outs/ins in Family Firms as a Share of all Buy-outs/ins - 10 year average (%)



Source: CMBOR/Barclays Private Equity/Deloitte

Company Size by Employment

With regard to company size, as measured by employment levels, a typical family firm buy-out has had between 194 and 480 employees in the last ten years. This number has fallen in recent years after peaking at 480 in 2003 and stood at 233 in 2007 (Table 1.4).

Table 1.4: Average Company Size for Buy-outs/ins in Family Firms

Year	Average number of employees per deal
1998	194
1999	250
2000	232
2001	294
2002	395
2003	480
2004	346
2005	334
2006	353
2007	233

Source: CMBOR/Barclays Private Equity/Deloitte

An analysis of the 10 year average number of employees per company shows that the size of the former family firms varies considerably between European countries. While German family firms have been well above average, UK family firms are generally smaller and below the European average (Table 1.5).

Table 1.5: Average Company Size for Buy-outs/ins in Family Firms – 10 year average

Country name	Average number of employees per deal[3]
Austria	432
Belgium	295
Denmark	333
Finland	437
France	324
Germany	794
Ireland	na
Italy	339
Netherlands	385
Norway	257
Portugal	na
Spain	418
Sweden	477
Switzerland	426
UK	224

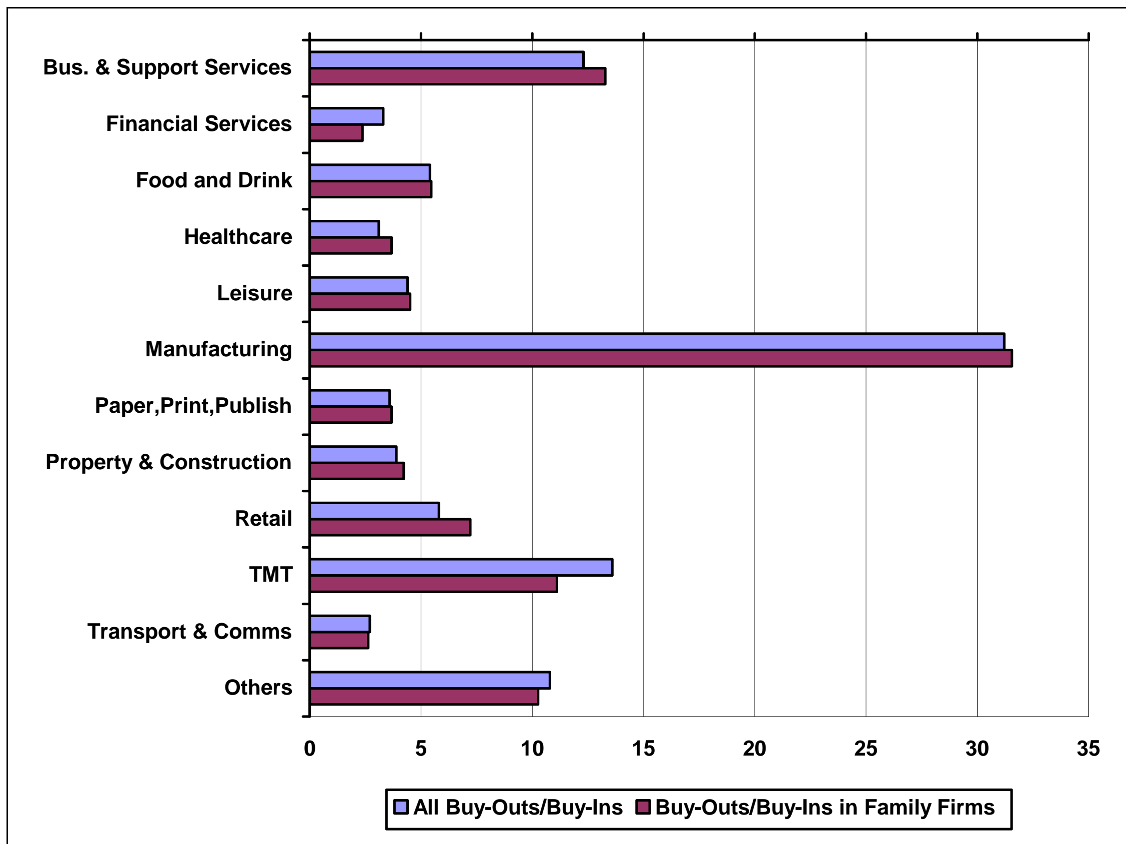
Source: CMBOR/Barclays Private Equity/Deloitte

[3] Numbers for Ireland and Portugal are not given due to limited data.

Industry Distribution

A large proportion of the family firms that undergo a buy-out are operating in the manufacturing, business & support services, and telecommunications media & technology (TMT) sectors. These are also the largest sectors by number for all buy-outs (Figure 1.6).

Fig 1.6: Distribution of Buy-outs/ins by Industry - 10 year average (%)

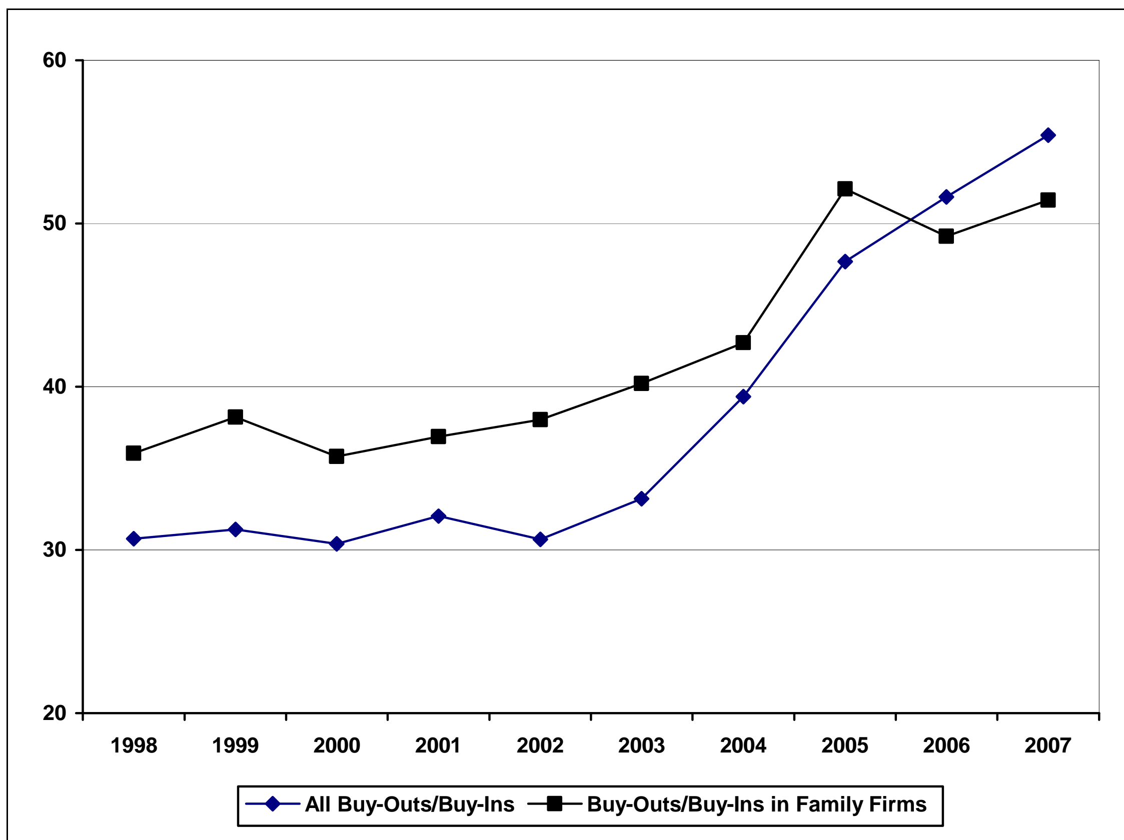


Source: CMBOR/Barclays Private Equity/Deloitte

Type of Deal

Looking solely at the proportion of family firm deals that involved buy-ins (BIMBOs, management and institutional buy-ins), it can be seen that this has increased significantly over recent years. Indeed this phenomenon is mirrored in the overall buy-out market where buy-ins have now become more commonplace for all deal sources over the last two years (Figure 1.7).

Fig 1.7: Buy-ins Relative to all Buy-outs/ins – Number of deals (%)



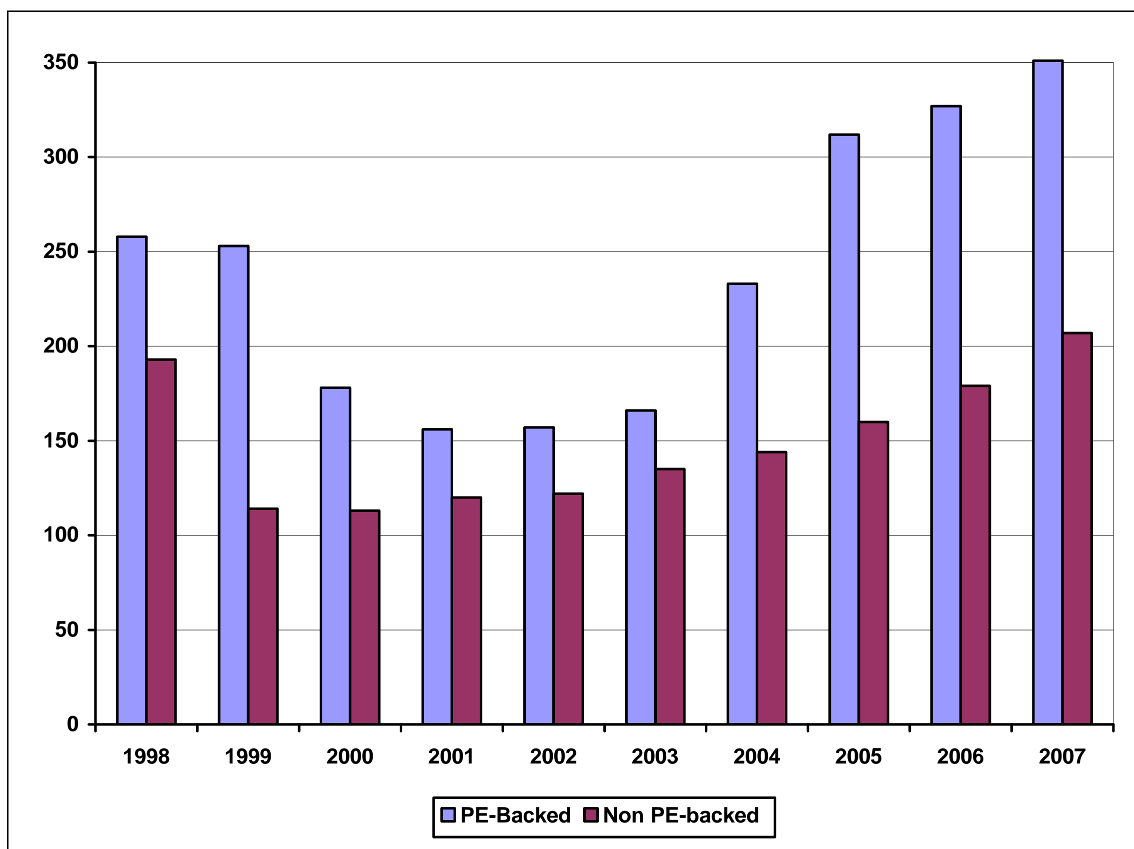
Source: CMBOR/Barclays Private Equity/Deloitte

Until 2006, buy-ins represented a greater share of family firm transactions compared to transactions from all sources. This trend has since reversed and in 2007 all buy-outs had a greater proportion of buy-ins than did family firm transactions.

PE-Backed Deals

Buy-outs can be financed by individuals using their own financial resources along with bank debt or by private equity (PE) firms or a combination. The majority of buy-outs of family firms are backed by a financial sponsor with the ten year average showing that 62% of all buy-outs of family firms were PE backed (Figure 1.8).

Fig 1.8: PE-backed and Non PE-backed Buy-Outs/Ins in Family Firms – Number of deals

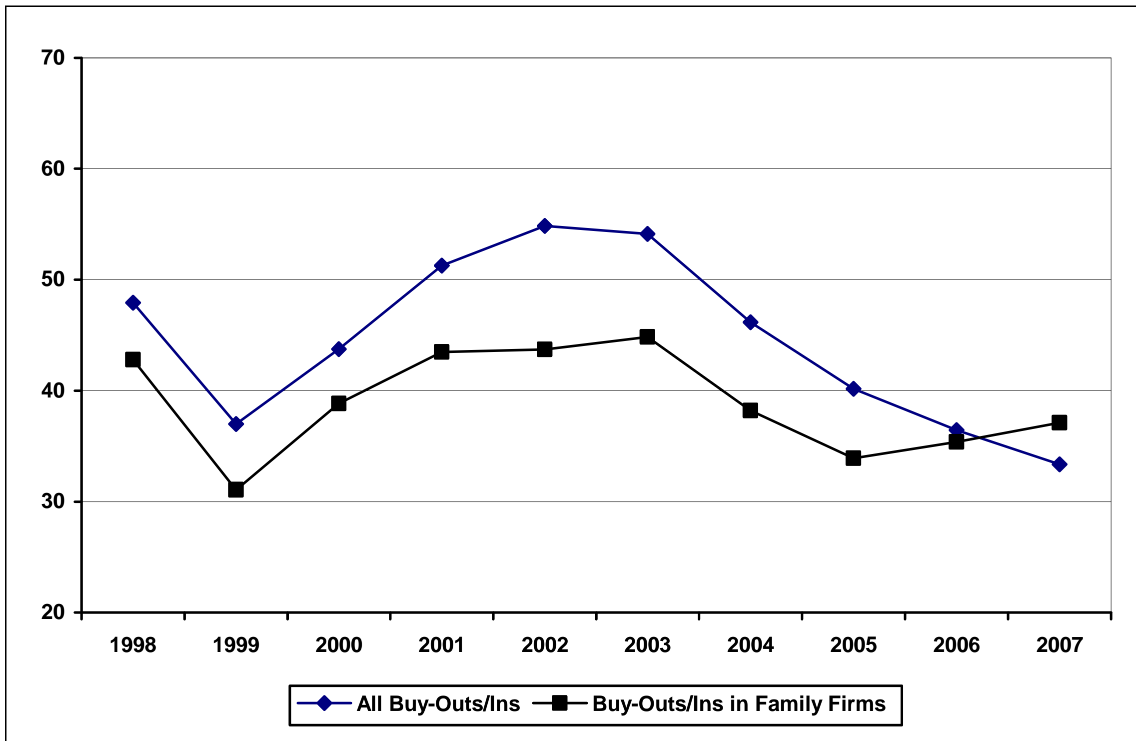


Source: CMBOR/Barclays Private Equity/Deloitte

The proportion of non PE-backed buy-outs of family firms has been lower compared to all buy-outs for the past ten years. This is rather surprising given the generally smaller deal size of buy-outs of family firms. This trend did reverse in 2007 (Figure 1.9).

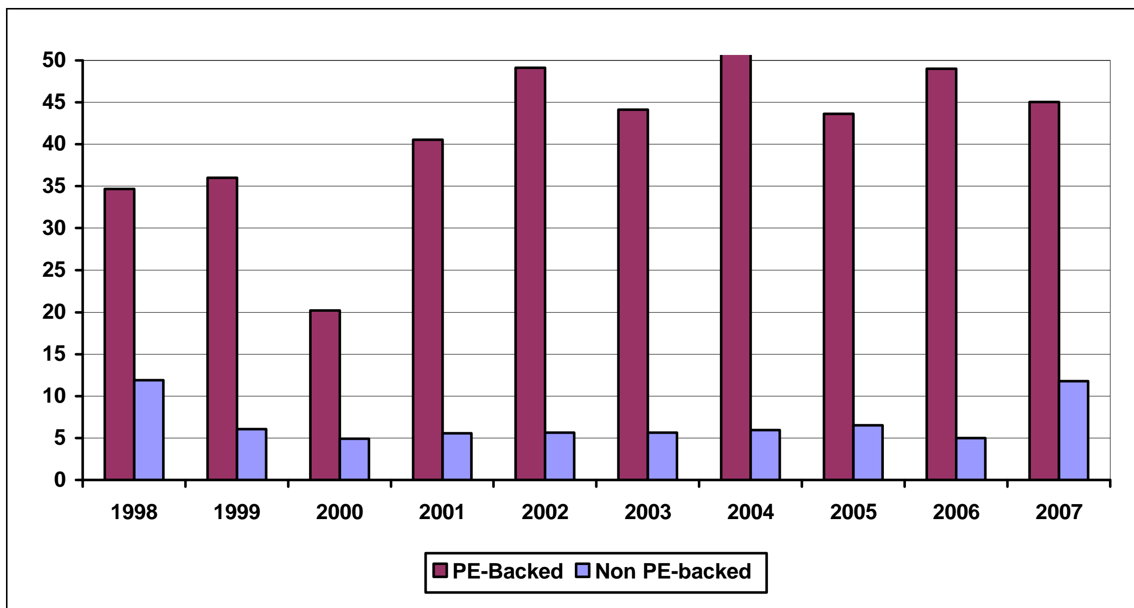
Non PE-backed buy-outs are, though, significantly smaller than PE-backed transactions for family firms. Over the last ten years, the average deal size of non PE-backed family firm buy-outs was about €7m compared with an average deal size of about €41m for PE-backed deals from this source (Figure 1.10).

Fig 1.9: Non PE-backed Buy-Outs/Ins as share of all Buy-Outs/Ins - Number of deals (%)



Source: CMBOR/Barclays Private Equity/Deloitte

Fig 1.10: Average deal size for PE-backed and Non PE-backed Buy-Outs/Ins of Family Firms (€m)

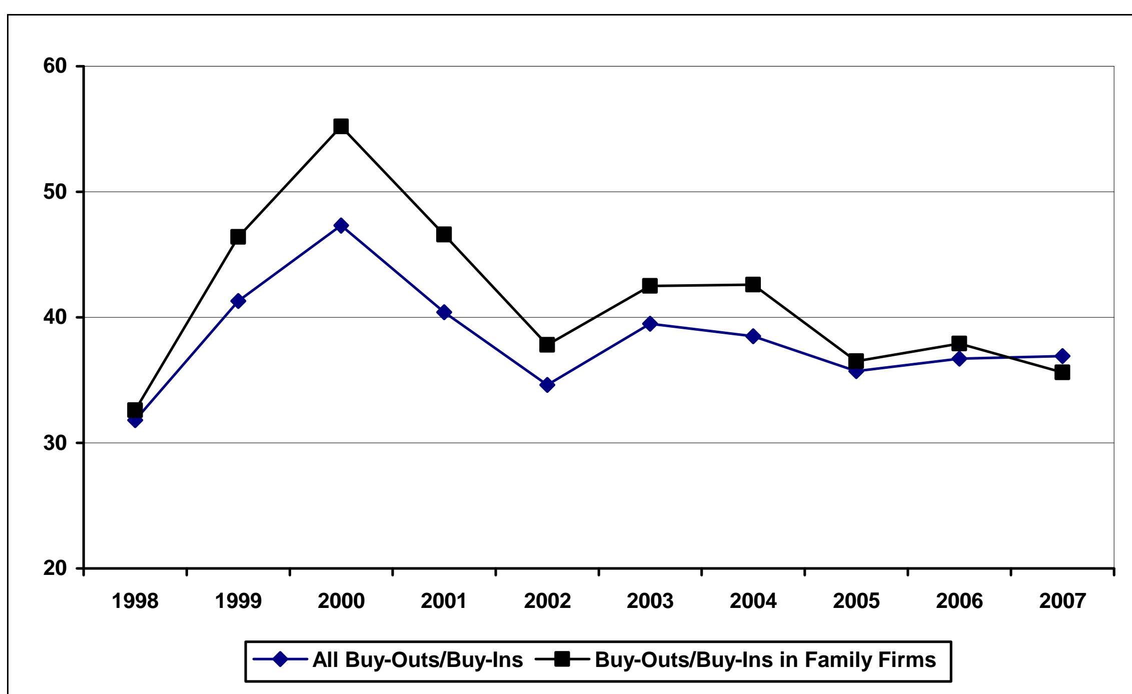


Source: CMBOR/Barclays Private Equity/Deloitte

Deal Structure

Buy-outs of family firms have generally displayed a higher equity component in their deal structures compared to the average for all buy-outs. Over the last ten years the average amount of equity in family firm buyouts was about 3% higher compared to the average of all deals. However, the gap in the level of equity between family firms and all buy-outs has narrowed in recent years and in 2007 the average equity stake in all buy-outs rose above that for family firms (Figure 1.11 & Table 1.6).

Fig 1.11: Average Equity Stake in Buy-outs/ins of Family Firms and all Buy-outs/ins (%)



Source: CMBOR/Barclays Private Equity/Deloitte

Table 1.6: Comparison of Deal Structures of Buy-outs/ins of Family Firms to all Buy-outs/ins - 10 year average (%)

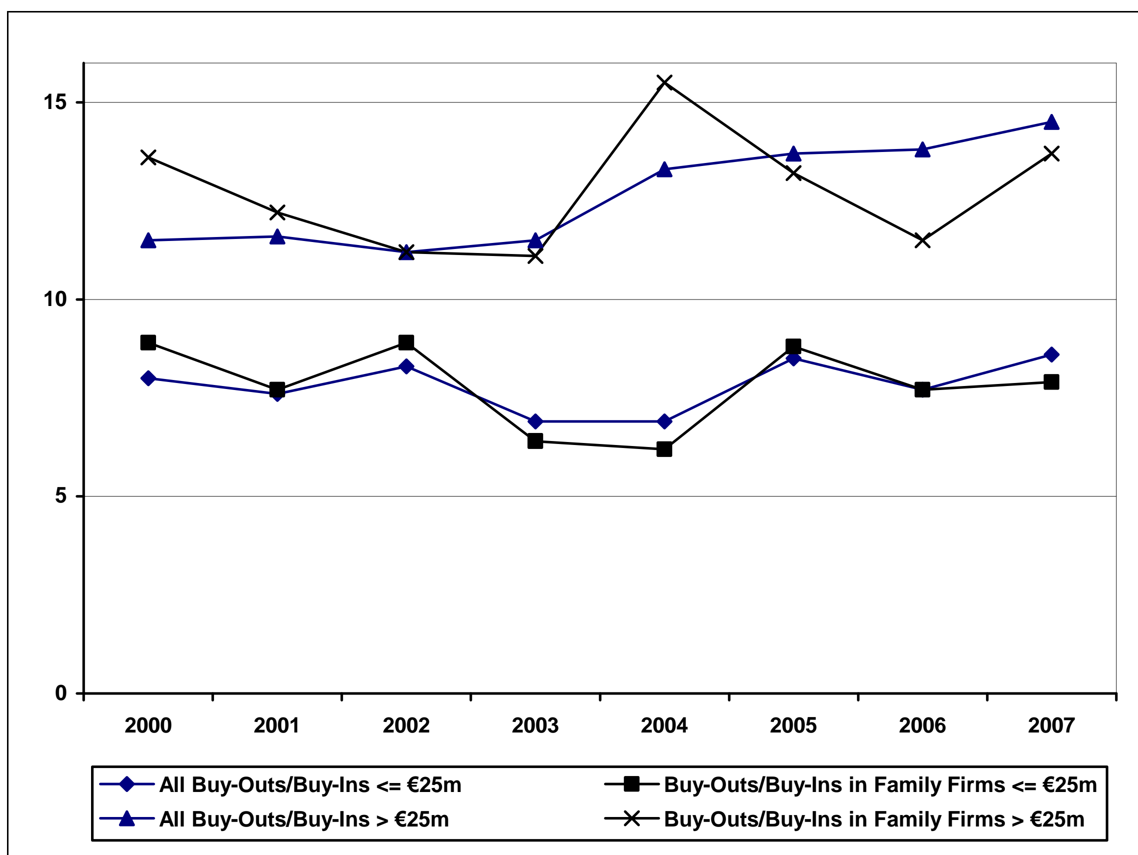
Structure type	All buy-outs/ins	Family firm buy-outs/ins
Equity	38.3	41.4
Mezzanine	5.1	2.7
Debt	48.9	47.3
Loan Note	3.6	5.0
Other Finance	4.6	4.4

Source: CMBOR/Barclays Private Equity/Deloitte

PE Multiples

The PE multiples (ratio of price/earnings before interest and tax) for smaller family buy-out transactions are similar to those for all deals whereas for larger transactions multiples have often diverged. In smaller transactions with a deal value of less than €25m, a size range which is dominated by family firm buy-outs, PE multiples have generally been in a range of between 6 and 8. For large transaction with a deal value of more than €25m, non-family firms recorded higher multiples than family firms except in 2000, 2001 and 2004. In general, non-family firms have had higher multiples in recent years (Figure 1.12).

Fig 1.12: Price/EBIT Multiples for Buy-outs/ins

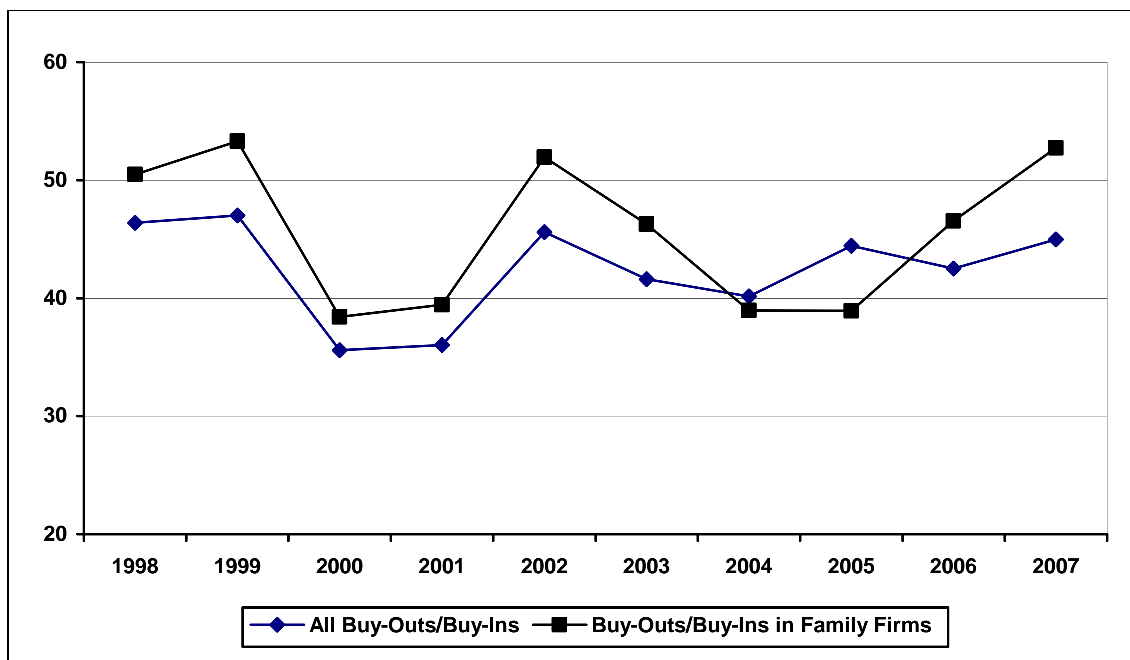


Source: CMBOR/Barclays Private Equity/Deloitte

Management Participation

Management teams in buy-outs of family firms generally hold a larger equity share (10 year average: 46%) compared to management teams in all buy-outs (10 year average: 43%). This is likely to be explained by the smaller average deal size of buy-outs/ins of family firms compared to all buy-outs/ins. (Figure 1.13).

Fig 1.13: Average Management Equity Stake after Buy-outs/ins of Family Firms (%)



Source: CMBOR/Barclays Private Equity/Deloitte

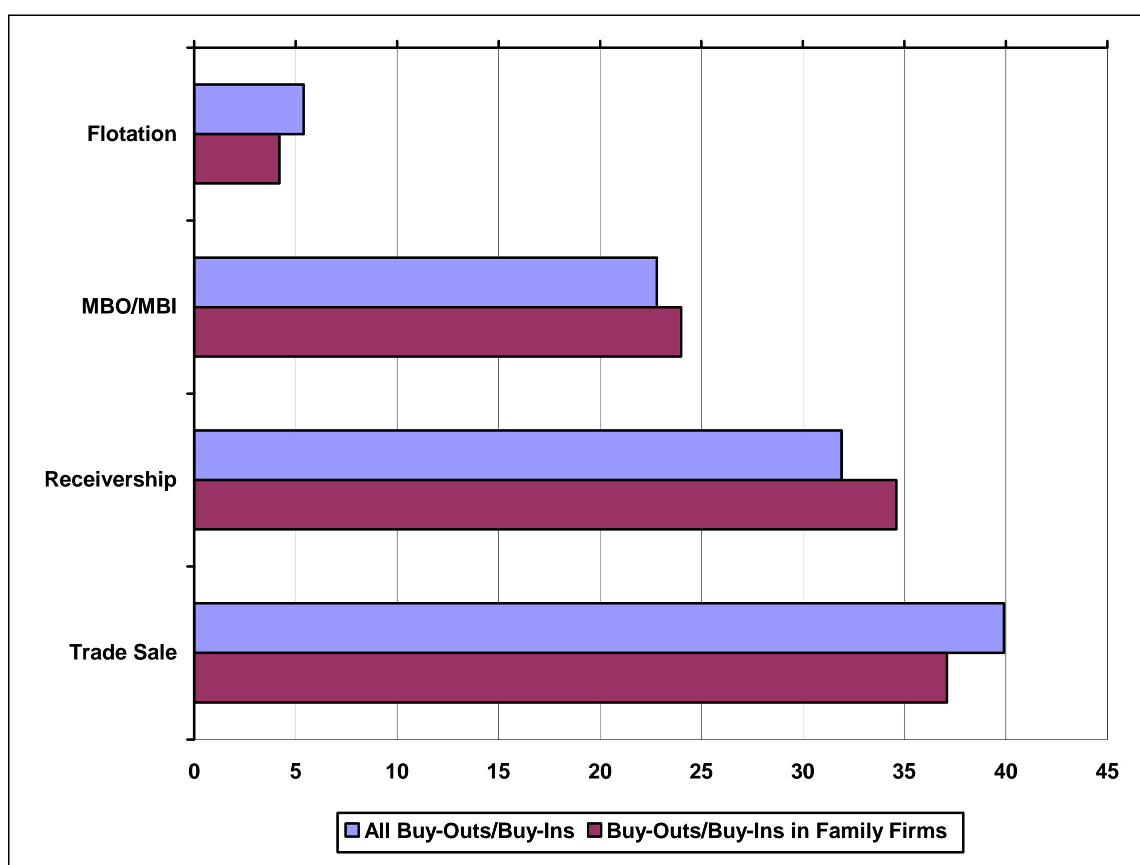
Exits[4]

The overall distribution of exits for buy-outs of family firms is similar to that for all buy-outs. Most portfolio companies are sold to corporate buyers through a trade sale. The second most frequent exit channel is receivership, followed by secondary buy-outs and finally IPO.

Trade sales seem to be somewhat less frequent among family firms compared to other types of buy-out. Receiverships on the other hand are more frequent, possibly reflecting the generally higher failure rate of smaller companies. Secondary buy-outs have become increasingly used as an exit route for all type of buy-out but this route is slightly more popular among family buy-outs than in the buy-out population as a whole. Retention of family goals and values may help to explain this phenomenon. The IPO rate of family firms is relatively low compared to other exit types reflecting both generally smaller firm size and typically more mature sectors (Figure 1.14).

[4] All data in the subsection refer exclusively to UK transactions.

Fig 1.14: Comparison of Distribution of Buy-outs/ins by exit - 10 year average (%)



Source: CMBOR/Barclays Private Equity/Deloitte

Table 1.7: Largest Exits of Buy-outs/ins of Family Firms in Europe

Company name	Exit Type	Country	Year of Exit	Exit Value (€m)
Bureau Veritas	Flotation	France	2007	4100
Arioli	Trade sale	Italy	2001	2485
Telenet Holding	Flotation	Belgium	2005	2100
Beaufour Ipsen	Flotation	France	2005	1840
CBR Holding	Secondary	Germany	2007	1500
Friedrich Grohe	Secondary	Germany	2004	1500
Sulo Group	Trade sale	Germany	2007	1450
ATU	Secondary	Germany	2004	1450
Harris Chemical Europe	Trade sale	UK	1997	1344
Moeller Group	Secondary	Germany	2005	1100
Trader Media Group	Trade Sale	UK	2003	868
Innovex Holdings	Trade sale	UK	1996	864
Benfield	Flotation	UK	2003	832
Techem	Flotation	Germany	2000	778

Source: CMBOR/Barclays Private Equity/Deloitte

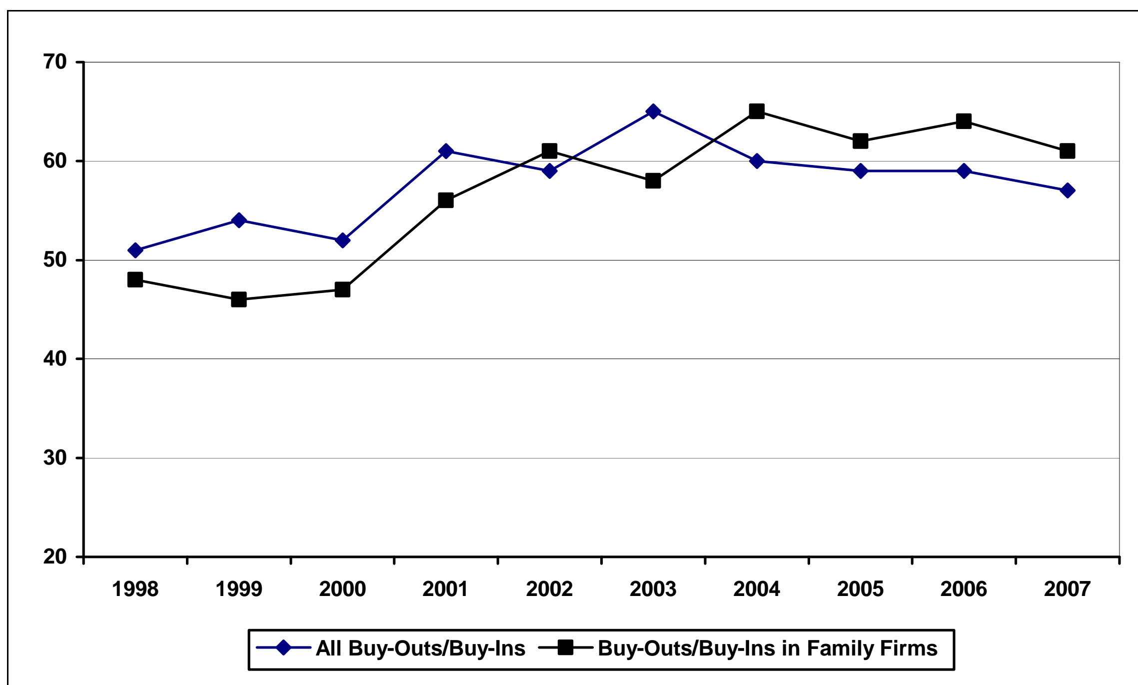
There have been several extremely large exits involving buy-outs of former family firms. The largest of these is Bureau Veritas which joined the stock market in 2007 for €4.1 billion. Arioli is the largest trade sale at €2.5 billion in 2001 with Telenet also joining the stock market for €2.1 billion in 2005 (Table 1.7).

Holding Periods

The average holding period for buy-outs of former family firms that have exited over the past 10 years is 58 months. This is almost identical to the holding period for all buy-outs that have exited which has averaged 56 months since 1998 (Figure 1.15).

A break-down of the average holding period for buy-outs that have exited per country shows that the UK has the longest average time to exit of 60 months for family firm buy-outs. Family firm buy-outs are held for an average of 56 months after the buy-out in France and only 47 months in Germany (Table 1.8).

Fig 1.15: Average Holding Period of Buy-outs/ins (months)



Source: CMBOR/Barclays Private Equity/Deloitte

Table 1.8: Holding Period of Buy-outs/ins
-10 year average (months)

Country	Average holding period. All buy-outs/ins	Average holding period. Buy-outs/ins of family firms	Number of deals. Buy-outs/ins of family firms
Austria	47	48	4
Belgium	40	50	18
Denmark	54	52	11
Finland	57	50	13
France	52	56	139
Germany	46	47	64
Ireland	51	42	6
Italy	46	52	61
Netherlands	53	55	41
Norway	44	40	4
Portugal	52	na	0
Spain	53	55	28
Sweden	58	36	22
Switzerland	47	52	23
UK	62	60	992

Source: CMBOR/Barclays Private Equity/Deloitte

Appendix

Table A1: Number of Family Firm Buy-outs/Buy-ins (% of total number)

Country Name	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Austria	40	0	8	0	11	25	7	29	30	20
Belgium	26	50	53	20	4	14	13	41	39	43
Denmark	23	22	17	8	11	25	14	27	38	67
Finland	6	16	7	26	7	21	25	30	33	15
France	38	29	34	29	22	30	37	40	32	39
Germany	28	17	15	5	17	9	13	20	24	22
Ireland	33	11	15	13	5	21	27	57	19	20
Italy	63	40	35	39	28	27	25	50	54	51
Netherlands	28	20	14	21	12	13	18	19	26	25
Norway	25	25	0	22	25	19	8	38	21	43
Portugal	0	0	0	100	0	0	0	20	0	43
Spain	43	33	36	19	21	27	39	44	52	45
Sweden	17	16	20	6	24	21	26	23	26	43
Switzerland	31	29	25	16	8	19	20	41	32	30
UK	40	36	27	28	29	25	32	33	37	41

Source: CMBOR/Barclays Private Equity/Deloitte

Table A2: Value of Family Firm Buy-outs/Buy-ins (€m) (% of total value)

Country Name	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Austria	28	0	11	0	4	26	16	33	54	0
Belgium	27	8	60	87	1	14	34	20	5	17
Denmark	16	18	5	77	11	10	10	6	4	63
Finland	2	1	0	6	37	1	2	1	3	2
France	51	12	10	10	6	12	26	10	5	13
Germany	16	38	2	2	24	9	11	16	7	7
Ireland	26	1	12	0	0	3	5	3	2	19
Italy	82	48	19	20	8	9	10	11	23	14
Netherlands	19	17	9	1	15	12	9	4	3	3
Norway	14	2	0	15	30	10	70	45	9	2
Portugal	0	0	0	100	0	0	0	34	0	8
Spain	34	26	21	23	16	42	8	6	44	40
Sweden	20	2	2	0	18	15	10	10	5	3
Switzerland	70	35	19	3	1	8	14	50	24	9
UK	19	14	4	11	15	13	16	13	17	8

Source: CMBOR/Barclays Private Equity/Deloitte

Table A3: Value ranges of Family Firm Buy-outs/Buy-ins

Range	1998		1999		2000		2001		2002	
	No.	%	No.	%	No.	%	No.	%	No.	%
Less than €5m	207	46	173	47	150	52	132	48	155	56
€5m - €10m	95	21	53	14	45	15	51	18	25	9
€10m - €25m	66	15	61	17	51	18	38	14	36	13
€25m - €50m	32	7	36	10	21	7	29	11	27	10
€50m - €100m	25	6	27	7	22	8	13	5	23	8
€100m - €250m	17	4	14	4	1	0	8	3	7	3
Over €250m	9	2	3	1	1	0	5	2	6	2

Source: CMBOR/Barclays Private Equity/Deloitte

Range	2003		2004		2005		2006		2007	
	No.	%	No.	%	No.	%	No.	%	No.	%
Less than €5m	171	57	208	55	242	51	260	51	334	60
€5m - €10m	29	10	31	8	42	9	44	9	33	6
€10m - €25m	37	12	46	12	51	11	62	12	56	10
€25m - €50m	21	7	30	8	60	13	52	10	53	9
€50m - €100m	24	8	37	10	49	10	52	10	52	9
€100m - €250m	15	5	14	4	15	3	24	5	15	3
Over €250m	4	1	11	3	13	3	12	2	16	3

Source: CMBOR/Barclays Private Equity/Deloitte

Table A4: Sector Distribution of Family Firm Buy-outs/Buy-ins

Industry Sector	1998		1999		2000		2001		2002	
	No.	%	No.	%	No.	No.	%	No.	%	No.
Bus. & Support Services	52	12	42	11	39	13	39	14	41	15
Financial Services	7	2	7	2	2	1	5	2	7	3
Food and Drink	37	8	20	5	13	4	14	5	15	5
Healthcare	5	1	8	2	10	3	15	5	11	4
Leisure	11	2	17	5	20	7	15	5	12	4
Manufacturing	174	39	122	33	81	28	95	34	78	28
Paper,Print,Publish	21	5	20	5	15	5	6	2	12	4
Property & Construction	22	5	10	3	10	3	9	3	10	4
Retail	28	6	14	4	18	6	18	7	13	5
TMT	41	9	59	16	42	14	30	11	27	10
Transport & Comms	9	2	3	1	7	2	8	3	10	4
Others	44	10	45	12	34	12	22	8	43	15

Source: CMBOR/Barclays Private Equity/Deloitte

Industry Sector	2003		2004		2005		2006		2007	
	No.	%	No.	%	No.	No.	%	No.	%	No.
Bus. & Support Services	43	14	61	16	61	13	60	12	77	14
Financial Services	6	2	12	3	14	3	16	3	16	3
Food and Drink	21	7	14	4	31	7	12	2	35	6
Healthcare	11	4	20	5	26	6	18	4	19	3
Leisure	15	5	16	4	27	6	26	5	16	3
Manufacturing	85	28	99	26	146	31	161	32	183	33
Paper,Print,Publish	10	3	16	4	13	3	16	3	14	3
Property & Construction	5	2	19	5	21	4	30	6	28	5
Retail	31	10	37	10	42	9	44	9	35	6
TMT	34	11	39	10	41	9	56	11	62	11
Transport & Comms	11	4	9	2	14	3	13	3	18	3
Others	29	10	35	9	36	8	54	11	56	10

Source: CMBOR/Barclays Private Equity/Deloitte

Table A5: Number of PE-Backed Buy-outs/Buy-ins of Family Firms

Country	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Austria	2	0	1	0	1	2	1	2	3	0
Belgium	3	8	9	5	0	3	4	11	9	12
Denmark	2	3	2	1	2	2	2	4	9	28
Finland	1	3	1	3	2	5	7	8	4	4
France	21	40	34	32	28	40	53	85	68	79
Germany	12	7	10	4	16	9	15	24	33	26
Ireland	1	1	1	0	0	0	0	2	0	1
Italy	14	16	10	7	11	12	11	23	28	24
Netherlands	8	12	10	7	5	9	13	12	13	13
Norway	0	1	0	2	3	2	1	5	5	6
Portugal	0	0	0	0	0	0	0	1	0	3
Spain	13	8	10	5	9	12	10	21	27	22
Sweden	4	5	5	2	5	5	10	9	11	18
Switzerland	4	7	5	3	2	1	4	5	5	6
UK	173	142	80	85	73	64	102	100	112	109

Source: CMBOR/Barclays Private Equity/Deloitte

Table A6: Number Non PE-Backed Buy-outs/Buy-ins of Family Firms

Country	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Austria	0	0	0	0	1	1	0	2	0	2
Belgium	2	0	1	0	1	0	1	0	3	1
Denmark	1	1	1	0	0	1	0	4	1	5
Finland	0	0	0	3	0	1	0	2	3	0
France	36	3	11	5	0	3	6	6	5	9
Germany	10	2	0	1	2	0	0	2	6	4
Ireland	4	0	1	2	1	3	3	2	3	2
Italy	6	1	1	0	0	0	0	0	1	2
Netherlands	13	1	1	6	3	1	1	5	11	14
Norway	1	1	0	0	0	1	0	1	0	0
Portugal	0	0	0	1	0	0	0	0	0	0
Spain	2	2	0	2	0	2	3	1	1	1
Sweden	0	0	0	1	1	0	0	0	0	3
Switzerland	12	9	9	5	1	5	3	7	4	2
UK	106	94	88	94	112	117	127	128	141	163

Source: CMBOR/Barclays Private Equity/Deloitte

Table A7: Value of PE-Backed Buy-outs/Buy-ins of Family Firms (€m)

Country	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Austria	27	0	80	0	3	100	25	103	81	0
Belgium	214	197	135	1521	0	208	781	830	58	447
Denmark	42	445	68	384	159	91	39	385	584	2540
Finland	10	9	2	52	215	9	22	11	28	26
France	2211	938	574	562	948	1070	3159	2225	1666	2002
Germany	618	1730	258	153	2076	1097	2079	2063	1652	1899
Ireland	20	14	27	0	0	0	0	6	0	70
Italy	436	1422	472	217	277	700	329	1872	1657	982
Netherlands	181	430	154	34	303	589	708	260	644	227
Norway	0	2	0	220	43	30	300	203	211	29
Portugal	0	0	0	0	0	0	0	25	0	18
Spain	247	372	198	353	339	406	164	521	2381	2695
Sweden	195	59	60	10	225	343	185	508	483	177
Switzerland	872	326	304	9	32	15	206	529	354	221
UK	3872	3166	1267	2813	3094	2664	4181	4074	6230	4477

Source: CMBOR/Barclays Private Equity/Deloitte

Table A8: Value of Non PE-Backed Buy-outs/Buy-ins of Family Firms (€m)

Country	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Austria	0	0	0	0	3	3	0	6	0	6
Belgium	5	0	71	0	3	0	3	0	24	3
Denmark	2	2	2	0	0	1	0	31	15	6
Finland	0	0	0	7	0	2	0	12	3	0
France	877	53	70	89	0	65	69	87	19	1550
Germany	224	13	0	13	8	0	0	54	24	15
Ireland	42	0	8	10	20	20	45	18	25	20
Italy	111	5	5	0	0	0	0	0	3	53
Netherlands	515	5	5	29	9	50	3	174	33	89
Norway	3	3	0	0	0	2	0	29	0	0
Portugal	0	0	0	2	0	0	0	0	0	0
Spain	10	72	0	6	0	5	8	4	8	8
Sweden	0	0	0	0	3	0	0	0	0	84
Switzerland	36	25	27	15	2	58	54	61	13	4
UK	474	513	370	500	641	556	678	568	727	611

Source: CMBOR/Barclays Private Equity/Deloitte

Table A9: Value of PE and Non PE-Backed Buy-outs/Buy-ins of Family Firms (€m)

Backing	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
PE-Backed	8946	9111	3599	6325	7713	7323	12178	13617	16027	15810
Non PE-Backed/no.	2298	691	558	670	689	761	859	1045	895	2449
Non PE-Backed/% of all	20	7	13	10	8	9	7	7	5	13

Source: CMBOR/Barclays Private Equity/Deloitte

Table A10: Number of PE and Non PE-Backed Buy-outs/Buy-ins of Family Firms (€m)

Backing	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
PE-Backed	258	253	178	156	157	166	233	312	327	351
Non PE-Backed/no.	193	114	113	120	122	135	144	160	179	208
Non PE-Backed/% of all	43	31	39	43	44	45	38	34	35	37

Source: CMBOR/Barclays Private Equity/Deloitte

Table A11: Average Deal Structures for all MBOs/MBIs

Type of Finance (Average %)	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Equity	32	41	47	40	35	40	39	36	37	37
Mezzanine	5	4	6	5	5	4	6	6	6	5
Debt	48	49	42	46	49	51	50	51	51	53
Loan Note	10	2	2	3	6	2	3	2	3	3
Other Finance	7	6	4	6	6	3	3	5	4	3

Source: CMBOR/Barclays Private Equity/Deloitte

Table A12: Average Deal Structures for MBOs/MBIs of Family Firms

Type of Finance (Average %)	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Equity	33	46	55	47	38	43	43	37	38	36
Mezzanine	3	4	2	2	3	2	3	3	4	3
Debt	48	46	38	44	51	50	47	53	45	52
Loan Note	13	4	2	3	5	3	5	4	7	5
Other Finance	7	5	2	5	3	3	3	4	6	5

Source: CMBOR/Barclays Private Equity/Deloitte

Table A13: Buy-outs/Buy-ins of Family Firms (€m)

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Buy-outs (no.)	289	227	187	174	173	180	216	226	257	271
Buy-outs (value/€m)	7150	6737	2111	3106	3512	3294	3873	5162	5199	6345
Buy-ins (no.)	162	140	104	102	106	121	161	246	249	287
Buy-ins (value/€m)	289	227	187	174	173	180	216	226	257	271
Buy-ins as % of total (by no.)	36	38	36	37	38	40	43	52	49	51
Buy-ins as % of total (by value)	36	31	49	56	58	59	70	65	69	65

Source: CMBOR/Barclays Private Equity/Deloitte

Section 2: Succession in Family Businesses through Private Equity Backed Management Buy-outs and Buy-ins

Introduction

Private firms face major challenges in dealing with succession. Successful transfer of the business to the next generation of family members is often problematical with the majority of family firms failing to plan for generational succession. There may be no suitable family members willing or able to take on the ownership and management of the business. This is an international phenomenon.

An MBO/I can provide a means of realising the majority family firm owner's investment and achieving continued independent ownership of the firm. As shown in the previous section, CMBOR data suggest that almost three tenths (29% over the past decade) of all MBOs and MBIs in Europe relate to the take-over of private family firms. After an MBO/I there is a greater possibility that the firm's identity and ethos will remain the same, both of which are important objectives for family firm owners. An attractive feature of an MBO/I is that the majority of the management team may remain intact. An additional advantage is that members of the family can continue to be involved in the firm.

There is little systematic evidence on the challenges relating to the completion of MBO/Is of private family firms. An important dimension relates to the extent to which information is made available to the parties involved in planning succession and negotiating the deal. Using a sample of 117 MBO/Is located in several European countries, this article examines the following issues:

- Are information asymmetries less prevalent in MBOs of private firms than in MBIs?

- Do flows of information impact the succession planning process relating to MBO/Is of private family firms?

- Do flows of information and the nature of succession planning impact the business sale negotiation process relating to MBO/Is of private family firms?

Information Asymmetries

Information flows between family firm owners and potential MBO/I teams can be affected by the inter-linkages between a family firm's family, ownership group and management group, which may only partially overlap. There may be information asymmetries between the different groups, with family owner-managers having the greatest access to information. There may also be asymmetric information between family-owner managers and managers undertaking an MBO with the former being reluctant to transfer their tacit knowledge to outsiders.

However, inside management who have worked with the key owner-manager of an organisation for some time may have developed relationships that enable them to obtain access to information. Further, incumbent managers who have been employed in an organisation for a considerable period of time may become familiar with the detailed operations of the firm, especially where the key founders/owners of the firm have become more distant from the business.

Conversely, an outside management team will have less access to appropriate flows of information relating to key aspects of the organisation, even though these outside managers may have considerable in-depth industry knowledge. Also, outside management are less likely to have developed relations with the key founders/owners. The owners of the family firm may prefer to sell their equity in the business to managers who they already know and make them privy to a diverse range of information relating to the family firm.

Table 2.1: Information Sharing Reported by MBOs and MBIs

Variable	MBI (n=51)		MBO (n=64)	
	No.	%	No.	%
Vendor controlled all the relevant information: yes	13	25.5	11	17.2
Vendor controlled most of the relevant information: yes	16	31.4	8	*12.5
Vendor & management shared relevant information equally: yes	16	31.4	33	*51.6
Management controlled most of the relevant information: yes	5	9.8	10	15.6
Management controlled all the relevant information: yes	1	1.9	2	3.1

Source: CMBOR/Barclays Private Equity/Deloitte
* difference between MBI and MBO statistically significant.

Information relating to information sharing was gathered from 115 respondents. Some 43%[5] of respondents reported that the vendor and management shared relevant information equally. A further 42% suggested information was not shared equally, of these, 21% suggested the vendor controlled all of the information, whilst a further 21% indicated that the vendor controlled most of the information. Of the remainder, 13% suggested that management controlled most of the information, while the remaining 2% reported that they controlled all the relevant information.

The survey gathered information from 66 MBOs (56%) and 51 MBIs (44%). Two statistically significant differences in information sharing were detected between the MBO and MBI respondents (Table 2.1). A significantly larger proportion of MBO rather than MBI respondents indicated that the 'vendor and management shared relevant information equally' (52% compared with 31%). Conversely, a significantly smaller proportion of MBO than MBI respondents reported that the 'vendor controlled most of the relevant information' (13% compared with 31%).

[5] These and other figures are derived from the number of responses to the questions in the questionnaire.

No statistically significant differences between the two groups were identified with regard to the following three statements: ‘vendor controlled all the relevant information’ (26% compared with 17%), ‘management controlled most of the relevant information (10% compared with 16%), and ‘management controlled all the relevant information (2% compared with 3%). This evidence indicates that private family firms associated with an MBO succession route report lower information asymmetry problems than firms selecting an MBI succession route.

Succession Planning

For over a fifth (21.7%) of respondents, there was no succession planning. In 45.3% of cases, the planning had taken place one year or less before succession. Only 20% of respondents had planned succession two years before the event with a further 13% planning for succession three or more years before the event.

The costs and benefits of different succession routes should be assessed by owners of private family firms. Benefits may accrue to the family and the firm if succession issues are evaluated prior to a succession crisis (eg, the sudden death of a key shareholder). In reality, succession issues can be ignored or neglected for a variety of economic and family reasons. Family firm owners, management and ‘outside’ management and investors (ie, private equity firms) could potentially be involved in the private family firm succession planning process. If this planning is carried out in an atmosphere of mutual trust and respect, balanced succession planning may be the agreed outcome. Here, family firm owners as well as non-family managers and ‘outside’ investors such as private equity investors can discuss and plan a mutually beneficial succession route.

If an MBO succession route is selected, it is reasonable to assume that by virtue of being insiders, existing management may have built up greater knowledge of the business and a relationship of trust with the vendor that leads to them being brought into discussions about succession. Conversely, ‘outside’ management who secure an MBI may not be privy to all appropriate information prior to their purchase of the family firm since they are less well-known and trusted. Respondents were divided into those who had reported that information was shared equally and those where it was not shared equally (Table 2.2).

Table 2.2: Information Sharing and Succession Planning

Variable	Information was not shared equally (n=63)		Information was shared equally (n=48)	
	No.	%	No.	%
Management not involved at all: yes	27	42.9	12	*25.0
Management & vendors discussed succession, process driven by vendor: yes	16	25.4	15	31.3
Management & vendors discussed succession, process evenly balanced: yes	8	12.7	12	*25.0
Management & vendors discussed succession, process driven by mgmt: yes	7	11.1	5	10.4
Management instigated process by approaching vendor with an offer: yes	5	7.9	4	8.3

Source: CMBOR/Barclays Private Equity/Deloitte

* Difference between information sharing and non-information sharing group statistically significant.

A significantly larger proportion of those respondents where ‘information was not shared equally’ (43%) rather than those where ‘information was shared equally’ (25%) stated that management was not involved at all in the succession process.

In contrast, a significantly smaller proportion of respondents where ‘information was not shared equally’ (31%) compared with those where ‘information was shared equally’ (25%) suggested that management and vendors discussed succession in an evenly balanced manner. These findings indicate that the MBO/I succession route will be associated with lower information asymmetry problems if private family firm vendors and the existing management team are equally involved in succession planning.

Table 2.3: The Role of Management in the Succession Planning Process

Variable	MBI (n=50)		MBO (n=62)	
	No.	%	No.	%
Management not involved at all: yes	25	50.0	14	*22.6
Management & vendors discussed succession, process driven by vendor: yes	17	34.0	14	22.6
Management & vendors discussed succession, process evenly balanced: yes	4	8.0	17	*27.4
Management & vendors discussed succession, process driven by mgmt: yes	2	4.0	10	*16.1
Management instigated process by approaching vendor with an offer: yes	2	4.0	7	11.3

Source: CMBOR/Barclays Private Equity/Deloitte
* Difference between MBI and MBO statistically significant.

A significantly larger proportion of MBO rather than MBI respondents indicated that management was not involved at all in succession planning (50% compared with 23%) (Table 2.3). Conversely, significantly smaller proportions of MBO rather than MBI respondents reported that the management and vendors discussed succession in an evenly balanced process (8% compared with 27%), and management and vendors discussed succession in a process driven by management (4% compared with 16%).

Business Sale Negotiation Behaviour

The relationship between the vendor and management team can impact sale negotiation behaviour. When participants have good relationships and are committed to the long-term future of the firm, they may be more likely to work well together and negotiations may involve flexibility, extensive information sharing and two-way communication.

This coordinative negotiation behaviour focuses on joint gains and the maintenance of long-term relationships between the purchasers and the vendors. However, when participants are more interested in short-term personal gains, negotiations may be less productive.

Owner/managers may be reluctant to share information if they are not to have some continued involvement in the business after the MBO/I. In this case, negotiations may involve competitive behaviour where both vendor and purchaser are interested in maximising their own positions, taking a short-term perspective. The vendor typically aims to maximise the price of the firm, whilst the purchaser seeks to reduce the price. Under command behaviour, the vendor may seek to maximise individual gains but may be committed to ensuring the future success of the acquired firm.

It may be difficult to negotiate a mutually agreed price for the private family firm when information is not shared or only partially shared. A paternalistic owner/manager of a family firm may simply offer management a fixed price, which the vendor believes to be a fair price. Conversely, a dominant family firm owner/manager focusing on short-term interests may propose a fixed price that maximises their own (family) gain.

Similarly, if management are not involved equally in discussion about succession, they are less likely to be involved in negotiating a mutually agreed price. Rather, the vendor seems likely to drive the negotiation process by offering management a fixed price that either maximises the vendor's gain or which the vendor perceives to be a 'fair' price, depending on whether the vendor has a short term or long term interest in the future of the business.

Information relating to agreement about price was gathered from 114 respondents. Over half (54%) of the respondents reported that a mutually agreed price was negotiated. More than a quarter (27%) reported the vendor proposed a fixed price that maximised their valuation, and a further 11% reported that the vendor had suggested a fair price that was in the best interests of the company. In addition, 4% reported that the management proposed a fixed price, 3% reported the vendor required management to match an outside bid and 1% suggested that the vendor offered the company to management at a lower price than an external bid.

Table 2.4: Strategic Objectives Cited During the Sale Process Prior to the MBO/I

Variable	No mutually agreed price				Mutually agree price			
	Mean+	No.	Median	S.Dev.	Mean+	No.	Median	S.Dev.
Sales growth	4.24	49	4	0.85	4.10	58	4	0.91
Net profit from operations	4.33	51	5	0.89	4.43	58	5	0.88
Cash flow from operations	4.14	51	4	0.98	4.26	57	5	0.86
Return on shareholder equity	3.10	51	3	1.27	3.61	56	4	*1.12
Capital restructuring	2.26	50	2	1.29	2.21	56	2	1.20
Short-term profitability	3.25	51	3	1.37	3.11	56	3	1.30
Long-term profitability	4.12	51	5	1.11	4.14	57	4	0.99
Market value increment	3.04	50	3	1.37	3.67	57	4	*1.39
Market share expansion	3.14	51	3	1.31	3.40	57	4	1.15
To accumulate family wealth	3.30	50	3	1.30	3.13	55	3	1.56
To increase employment	2.14	50	2	1.09	2.14	56	2	1.00

Source: CMBOR/Barclays Private Equity/Deloitte

+ Mean calculation based on a 5-point scale from 1 = very low importance to 5 = very high importance

* Difference between no mutually agreed price group and mutually agreed price group statistically significant.

Information was gathered with regard to 11 strategic objectives relating to the sale process prior to the MBO/I. The 'degree of importance' respondents attached to each of the strategic objectives was measured on a scale where 'very low importance' = 1; 'moderate importance' = 3; and 'very high importance' = 5. Respondents were divided into those that reported that no mutually agreed price had been agreed and those that stated a mutually agreed price was the case (Table 2.4).

The following statements were scored on average 4.0 or more by both types of respondents: 'sales growth', 'net profit from operations', 'cash flow from operations' and 'long-term profitability'. Respondents who stated that a mutually agreed price had been struck were significantly more likely to report 'return on shareholder equity' (means of 3.6 and 3.1 for 'mutually agreed price' and 'no-mutually agreed price' respondents, respectively) and 'market value increment' (means of 3.7 and 3.0 for 'mutually agreed price' and 'no-mutually agreed price' respondents, respectively).

These findings indicate that coordinative forms of negotiation behaviour between family firm owner(s) and management teams occur if they are both committed to the future of the private family firm and they consider joint as opposed to individual gains.

Table 2.5: Information Sharing and the Sale Process

Variable	**No mutually agreed price (n=52)**		**Mutually agreed price (n=61)**	
	No.	**%**	**No.**	**%**
Vendor controlled all the relevant information: yes	12	23.1	11	18.0
Vendor controlled most of the relevant information: yes	11	21.2	13	21.3
Vendor & management shared relevant information equally: yes	19	36.5	30	49.2
Management controlled most of the relevant information: yes	10	19.2	4	*6.6
Management controlled all the relevant information: yes	0	0.0	3	4.9

Source: CMBOR/Barclays Private Equity/Deloitte
* Difference between no mutually agreed price group and mutually agreed price group statistically significant.

Five statements relating to information sharing and the sale process were gathered. Again respondents were divided into those reporting that no mutually agreed price had been achieved and those suggesting that there had been a mutually agreed price (Table 2.5). A significantly smaller proportion of 'mutually agreed price' respondents (7%) rather than 'no mutually agreed price' respondents (19%) suggested that the management controlled most of the relevant information.

These findings provide some indication that a mutually agreed sale price between the vendors and management teams is unlikely if information surrounding the private family firm is not equally shared, especially where it is management that controls most of the relevant information.

Table 2.6: The Role of the Management with Regard to the Sale Process

Variable	No mutually agreed price (n=52)		Mutually agreed price (n=58)	
	No.	%	No.	%
Management not involved at all: yes	16	30.8	22	37.9
Management & vendors discussed succession, process driven by vendor: yes	18	34.6	12	*20.7
Management & vendors discussed succession, process evenly balanced: yes	8	15.4	13	22.4
Management & vendors discussed succession, process driven by mgmt: yes	7	13.5	5	8.6
Management instigated process by approaching vendor with an offer: yes	3	5.7	6	10.4

Source: CMBOR/Barclays Private Equity/Deloitte
* Difference between no mutually agreed price group and mutually agreed price group statistically significant.

Five statements relating to the role of management in discussing succession and the sales process were gathered (Table 2.6). A smaller proportion of respondents who reported that a 'mutually agreed price' was arrived at (21%) rather than those where there was 'no mutually agreed price' (35%) suggested that the management and vendors discussed succession in a process driven by vendor.

These findings indicate that a mutually agreed sale price between the vendor and the acquirer is unlikely if succession planning issues are not discussed equally between them.

Role of Private equity Firms

The involvement of a private equity firm in discussions about succession may impact whether a mutually agreed price is achieved. The experience of private equity firms in negotiating buy-outs and buy-ins may put them in a stronger position to negotiate with the vendor than is the case for management, for whom the buy-out is likely to the first time they have engaged in such negotiations. Where a vendor attempts to propose a price that is in their own interest, a private equity firm may be in a stronger position than management to challenge it. Management may be concerned that if they challenge a dominant owner they could risk losing the deal and possibly their jobs.

Table 2.7: The role of the Private Equity Provider (PEP) with Regard to the Sale Process

Variable	No mutually agreed price (n=50)		Mutually agreed price (n=58)	
	No.	%	No.	%
Private equity provider (PEP) not involved at all: yes	15	30.0	29	*50.0
Vendor approached PEP to discuss succession: yes	9	18.0	8	13.8
PEP discussed succession with management: yes	9	18.0	10	17.2
PEP discussed succession with the vendor and the management: yes	13	26.0	7	*12.1
PEP made proactive approach to vendor before succession: yes	4	8.0	4	6.9

Source: CMBOR/Barclays Private Equity/Deloitte
* Difference between no mutually agreed price group and mutually agreed price group statistically significant.

Where management are in a stronger position to drive the succession and negotiation process, for example where the vendor is less involved in running the business, they may be able to bring in the private equity firm to help negotiate a price that is more advantageous to them. In contrast, where the private equity firm is not involved in discussions about succession, it may be more likely that a mutually agreed price is arrived at.

Five statements relating to the role of the private equity provider in discussing succession and the sale process were gathered (Table 2.7). Again respondents were divided into those reporting that no mutually agreed price had been achieved and those suggesting that there had been a mutually agreed price.

A larger proportion of 'mutually agreed price' respondents (50%) rather than 'no mutually agreed price' respondents (30%) suggested that the private equity provider was not involved at all in discussing succession. Conversely, a significantly smaller proportion of 'mutually agreed price' respondents (12%) rather than 'no mutually agreed price' respondents (26%) suggested that the 'private equity provider discussed succession with the vendor and the management'.

These findings indicate that a mutually agreed sale price between the vendor and the acquiring management is unlikely if the private equity firm is involved in discussions regarding succession planning.

Section 3: Changes in Strategy of Former Family Firms after Management Buy-outs and Buy-ins

Introduction

The typical family firm has traditionally been assumed to be owned and managed by a concentrated group of family members where the firm's objectives are closely linked to family objectives. Families typically do not regard their firms as mere "economic units" pursuing the goal of profit maximization. Instead, families also strive for non-economic goals. As a result, the "tightness of grip" of a family over its firm adds an important dimension to the analysis of the strategies of family firms.

Survival is an issue of outstanding importance for family firms. The succession process in these firms is therefore a much debated area. Management buy-outs (MBO) and buy-ins (MBI), hence forth 'buy-out', are an important succession option that introduces new ownership and governance structures in the form of managerial equity ownership, commitment and pressure to service debt, and in many cases ownership and active involvement by private equity firms. These changes may be expected to lead to different goals and strategies in the former family firm compared to the previous ownership regime and these strategic changes may influence firm survival or failure.

The change in strategy is motivated by one of the following two themes: Firstly, the firm may have been underperforming and new strategies must be adopted in order to correct this (efficiency buy-out). Secondly, the new owners will have the freedom to pursue their own interests in terms of business direction and/or diversification (growth/expansion buy-out). The presence of founder, shareholding non-family managers or non-family non-executive directors on the board may have different effects on the buy-out process and on the business strategies adopted before and after the buy-out. Changes in strategy are also due to the ownership and governance of the firm before the buy-out and whether these changes are influenced by a new financial structure and the need to meet resultant servicing costs.

This background raises three important questions:

- Are changes in the strategy of former private family firms affected by the ownership of the firm before the buy-out?

- Are changes in the strategy of former private family firms affected by the governance of the firm before the buy-out?

- What is the effect of new funding structures adopted after the buy-out on the strategic direction of these former private family firms?

These questions are examined using a novel hand-collected representative questionnaire survey of 108 private family firms across Europe which had a buy-out funded by private equity between 1994 and 2003.

Firms' strategy has been compared before and after the buy-out. Strategies were distinguished as either efficiency related or growth/expansion related. Respondents were asked to provide data on certain company characteristics concerning ownership and management. They were also asked to indicate changes of 11 strategic themes before and after the buy-out. Data on gearing was obtained from Amadeus and Fame.

Ownership

When the family firm had been founded by the previous owners the changes in strategy post buy-out are generally more numerous and more significant than when the firm had been purchased or inherited by the pre-buy-out owners (Table 3.1). This implies that the founder/owner has been dominant in terms of deciding company strategy and that once she/he relinquishes ownership the management are free to make the changes they deem necessary for the survival and growth of the firm.

Several changes in strategy were common to firms that were founded or non-founded by the previous owners. While both types of firms showed strategic changes with regard to an increased emphasis on returns from operations and capital restructuring, founded firms also indicated a change in strategy with regard to net sales growth, long-term profitability and market share expansion. The emphasis is therefore on growth/expansion after buy-out rather than efficiency improvements.

Table 3.1: Importance of Business Strategy Before and After the Buy-out in Relation to Pre-Buy-out Ownership

Business Strategy	Founder still involved in business[1]					Non-family management holding equity stake[1]			
	Yes		No			Yes		No	
	B	A	B	A		B	A	B	A
Improving efficiency									
Net profit from operations	5.0	5.0**	4.0	5.0*		5.0	5.0	5.0	5.0**
Cash flow from operations	4.5	5.0**	4.0	5.0**		5.0	5.0#	4.0	5.0**
Return on shareholder equity	3.0	4.0**	4.0	4.0*		4.0	5.0**	3.0	4.0**
Capital restructuring	2.0	3.0**	2.0	3.0*		2.0	3.0*	2.0	3.0**
Short-term profitability	3.0	4.0#	3.0	3.0		3.0	4.0	3.0	4.0**
Future Growth and Expansion									
Sales growth	4.5	5.0*	4.0	4.0		4.5	5.0	4.0	5.0*
Long-term profitability	5.0	5.0**	4.0	4.0		4.5	5.0*	4.0	5.0*
Market value increment	4.0	5.0**	3.0	4.0**		4.0	4.5	3.0	5.0**
Market share expansion	4.0	4.0**	4.0	4.0		3.0	3.0	4.0	4.0**
Other									
To accumulate family wealth	4.0.	3.0**	3.0	2.0#		3.0	3.0*	3.5	2.5**
To increase employment	2.0	2.0	2.0	2.0		2.0	2.0	2.0	2.0

Responses from the questionnaire on strategic change before and after the buy-out. Measured on a likert scale of 1 (very low importance) to 5 (very high importance).

[1]Each cell contains the median value of response before (B) and after (A) the buy-out and the significance of the difference in column A (# $p<0.1$ * $p<0.05$; ** $p<0.01$).

Strategic changes after a buy-out of a family firm were greater, if the firm's founder was still present at the time of the buy-out. There are three possible explanations for this finding: Firstly, founders may not provide adequate leadership as firms need to transition into more advanced growth phases. Secondly, founders may also be unable to adjust their decision-making style where changes in the market environment suggest a need to change strategy. Thirdly, successful founders may also become overly conservative in an effort to preserve the wealth they have created even thought the firm may have growth opportunities.

The changes in firm strategy were more numerous and more significant when there were no non-family managers with ownership stakes. This finding indicates that management who had some ownership stake were potentially able to influence strategic direction before the buy-out and that major changes after the buy-out were not necessary. If the managers of the family firm were not family members and did not hold equity stakes before the buy-out, their influence on strategic direction before the buy-out might have been very limited since the ultimate decision might have rested with the owners. These non-family managers without equity stakes were only able to effect change once the buy-out has taken place and they have become the new owners.

Several changes in strategy were common to firms with and without non-family management with equity stakes. Those strategies specific to firms without non-family managers with equity stakes were net profit, short-term profitability, sales growth, market value increment and market share expansion. Thus the two different strategies of growth/expansion and efficiency improvements are fairly equally important with only a slight emphasis on growth/expansion.

Governance

The governance of the family firm before the buy-out could be in the hands of non-executive directors (NEDs) that did not belong to the family (Table 3.2). The results indicate that more strategic changes are associated with the absence of non-family NEDs before the buy-out. If NEDs before the buy-out were not family members their advice should be more financially oriented (as opposed to family oriented).

If good advice had been given before the buy-out and some changes had already been implemented major strategic changes may not be necessary post buy-out.

In the absence of pre-buy-out non-family NEDs, the new owners were able to implement their ideas post-buy-out primarily in terms of growth and expansion. This could indicate that firms with NEDs were more effective and did not need to change their strategy so much post buy-out. The changes were in terms of both efficiency gains and growth/expansion.

Table 3.2: Importance of Business Strategy Before and After the Buy-out in Relation to Pre-Buy-out Governance

Business Strategy	Existence of non-family non-executive directors[1]				Management involved in succession planning[1]				Private equity firm involved in succession planning[1]			
	Yes		No		Yes		No		Yes		No	
	B	A	B	A	B	A	B	A	B	A	B	A
Improving efficiency												
Net profit from operations	5.0	5.0*	5.0	5.0*	4.0	5.0**	5.0	5.0	4.0	5.0**	5.0	5.0
Cash flow from operations	4.0	5.0*	4.0	5.0**	4.0	5.0**	5.0	5.0**	4.0	5.0**	4.5	5.0**
Return on shareholder equity	3.0	4.0#	3.0	4.0**	4.0	4.0**	3.0	4.0*	3.0	4.5**	4.0	4.0
Capital restructuring	2.0	3.0	2.0	3.0**	2.0	3.0**	2.0	3.0*	2.0	3.0**	2.0	2.0
Short-term profitability	3.0	4.0	3.0	4.0#	3.0	3.0	3.0	4.0	3.0	3.0	3.0	4.0
Future Growth and Expansion												
Sales growth	4.0	5.0#	4.0	5.0#	4.0	5.0*	4.0	4.0	4.0	5.0#	4.0	4.0
Long-term profitability	4.0	5.0	4.0	5.0**	4.0	5.0**	5.0	5.0	4.5	5.0*	4.0	5.0#
Market value increment	4.0	5.0*	4.0	5.0**	4.0	4.0**	4.0	5.0*	4.0	5.0**	3.0	4.0
Market share expansion	3.0	4.0	3.0	4.0**	4.0	4.0	3.0	4.0*	4.0	4.0*	3.0	3.0#
Other												
To accumulate family wealth	3.0	3.0	3.0	3.0**	2.5	3.0*	4.0	3.0*	3.0	2.0**	3.5	3.0
To increase employment	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0

Responses from the questionnaire on strategic change before and after the buy-out. Measured on a likert scale of 1 (very low importance) to 5 (very high importance).
[1]Each cell contains the median value of response before (B) and after (A) the buy-out and the significance of the difference in column A (# p<0.1 * p<0.05; ** p<0.01).

Governance can also be applied at the time of succession planning, although it has been shown that many firms fail to plan for succession at all. The study presented in the previous section indicated that about 60% of the family firms questioned underwent succession planning in the period of up to two years before the event. Nevertheless, if succession was planned, management before the buy-out as well as the financing private equity firm might participate in this planning and thus influence the strategic changes in the aftermath of the buy-out.

When management before the buy-out was involved in succession planning, strategic changes were stronger compared to succession planning without the management's involvement. Management's involvement in succession planning might have enabled them to articulate possibilities for new strategies and to place themselves in an advantageous position to influence the mode of succession, i.e. through a buy-out. To convince financiers they needed to have a clear strategy that would lead to the generation of significant gains.

Changes with regard to both dimensions, efficiency and growth/expansion, were stronger if management participated in succession planning.

When a private equity firm participated in succession planning, strategic changes were substantially greater than without participation of a private equity firm. As a precondition for investment of a private equity firm in the buy-out, they needed to perceive that there would be upside gains from investing in the deal.

Given the expertise of these firms and their access to information regarding opportunities, they showed strategic changes in improving efficiency and growth/expansion.

Debt

Debt is thought to discourage managers from diversifying and behaving in a self-serving way as cash flows have to be used to service the debt. In this way, opportunism by management can be controlled. In a buy-out therefore, not only do former managers become owners, but if the debt is large they could be forced to concentrate on improving the efficiency of the existing business rather than to expand it through innovation. However, in contrast to these arguments, we find that there was no difference in debt levels (measured as gearing) between firms who stated that a business strategy became more important after the buy-out and those who stated that the strategy either remained equally important or became less important.

Implications

In light of these results, buy-outs have a very strong impact on the strategy of former family firms. But this impact varies according to certain ownership and management characteristics before the buy-out.

If the founder of the firm is still involved in the business at the buy-out, stronger strategic changes will be towards growth and expansion of the company compared to a firm where the founder left before the buy-out. This might indicate that a firm in which the founder is still involved does not offer a large potential for efficiency gains, whereas inherited or bought companies obviously displayed some operational slack.

If non-family managers had no equity stake before the buy-out, greater strategic changes were implemented with regard to efficiency gains and to growth and expansion compared to firms, where the non-family managers held an equity stake. This suggests that non-family managers with equity stakes already address these issues and, thus, no change in strategy is necessary.

In firms without non-family non-executive directors prior to the buy-out, strategic changes were stronger in both efficiency gains and growth/expansion compared to companies with non-family non-executive directors.

The tighter control of non-family non-executive directors seems to have led to the right strategy already before the buy-out.

The involvement of management or of a private equity firm in the family's succession planning resulted in a stronger strategic change with regard to efficiency improvements and growth/expansion after the buy-out compared to firms where these parties did not participate in succession planning.

Although the degree and type of strategic change might be expected to be related to gearing, results did not support this expectation.

Table 3.3: Summary of Strategic Influences

Actor	Role	Influence before buy-out	Influence after buy-out	Strategic direction post buy-out
Founder	Ownership	yes	no	Growth/expansion
Management with equity (non family)	Ownership	yes	yes	Efficiency improvements And growth/expansion
Non executive director (non family)	Governance	yes	unknown	Growth/expansion
Management involved in succession planning	Governance	no	yes	Efficiency improvements And growth/expansion
Private equity involved in succession planning	Governance	no	yes	Efficiency improvements

Section 4: Professionalization, Stewardship and Performance: Family Firm Buy-outs

Introduction

Across Europe, about three tenths of buy-outs involve family owned firms. Part of the reason for preferring a buy-out as a family firm succession route is that it enables the continuation of the firm as an independent business. But to what extent is the family firm ethos maintained and does it matter?

Professionalization is an important stage for entrepreneurs who aim to grow their firms. Professionalization concerns the utilisation of formal governance mechanisms, the utilisation of formal strategic planning and control systems, and the involvement of non-family members on the board and in the management team. Family-managed firms are often viewed as being less ‘professional’ because of the intertwining of family and business objectives and values.

As noted in the previous section, many private family firms pursue non-financial objectives. Managers in a family firm may act as stewards and seek to protect the assets of the firm rather than to pursue interests that maximise their own personal gain. Family firms may also display positive attributes in terms of loyalty, long-term commitment and trust that professionalization may undermine. The introduction of professional governance and management structures and systems may reduce potential conflicts of interest between family and non-family owners and managers that lead to improved performance.

Succession presents a juncture where the continuity of family and the professionalization of the family firm potentially collide. Management buy-outs (MBOs) and buy-ins (MBIs) of private family firms have the potential to introduce a greater degree of professionalization and stimulate the removal of at least some family members from the business.

MBOs of private firms usually involve incumbent managers taking over responsibility from the former owner-manager(s) and may present an opportunity to either release the entrepreneurial aspirations of second tier non-family management where founders and family had ceased to be entrepreneurial.

MBIs are a distinct move towards professionalization associated with a new ‘professional’ management buy-in team. However, if negative aspects of a family organisational culture remain deeply embedded, subsequent firm performance may be retarded.

This background raises three important questions:

- Do former private family firms exhibit more professionalization post-MBO/I?

- Do former private family firms exhibit characteristics associated with a stewardship perspective post-MBO/I?

- What (if any) professionalization and stewardship factors are associated with superior performing MBO/Is?

These questions were examined by looking at eight former private family firms that underwent MBO/Is in 1998 and which were then tracked over the period to 2006 (Table 4.1). To preserve anonymity, responding firms have been given fictitious names.

Professionalization

In both DISPENSERS and PLANTS, which involved the introduction of an external managing director, the managing directors talked about professionalising the firm in terms of making improvements that reflected their experience in larger companies (i.e., decentralising control). Respondents in DISPENSERS drew attention to the need to “clean up lots of things”.

In several cases, where changes led to tightening up of slack, there was resistance from some employees. DUMPS had difficulties in introducing performance related bonuses. PIPES’ employees had previously enjoyed a very relaxed attitude to work: “in the afternoons they’d fill in crosswords and play Scrabble…I think if everyone was honest they’d say they’d like it to be as it was before, but as it was before wasn’t really in the real world”. Following the MBI this was tightened up and bonuses were linked to performance rather than provided automatically.

Post-MBO/I, evidence of change associated with the elements of professionalization was present in 5 cases. Following the MBI, PIPES introduced several systems associated with professionalization. Management and stock control systems as well as computerised invoicing were introduced. Prior to the MBI most operations had centred on the owner manager but the informal approach he adopted was a luxury that could no longer be afforded:

“.. [Owner manager] would come in historically at 5 o’clock in the morning, he’d just wander around the warehouse, if the bin was empty… he’d just order a pallet load of those fittings and then he could forget about it for six months which was nice and easy in the days when we had plenty of cash to do it. So we are struggling to come to terms with that now, we have to be a bit more conscious of what we are spending and therefore we’ll probably be doing more paperwork because we are placing a lot more orders but at much smaller quantities. Without knowing your stock the only time they’d know what their profit was, was whenever they did a stock take…they certainly did no more than two a year…. Now [venture capitalist (VC)] need a copy of management accounts every month, we are developing a system” (PIPES, finance director, 2001).

Table 4.1: Description of Cases

Name	TROLLEYS	PLANTS	PIPES	DUMPS	FILMPACKS	DISPENSERS	BOXES	LOCKS
Industry	Engineering	Horticulture	Merchant	Construction	Packaging	Hygiene service	Paper/print	Engineering
Founded	1979	1972	Pre-1928	1979	1973	1950	1963	1965
Turnover £m 1998* : 2005	6	24:30.4	4 : 18.2**	20 : n.a.	06:47.5	8.5 : n.a.	2.5 : not known	4.6 : 3.8
Employees 1998 : 2005/6	65 : 60	300 : 221	30 : 75	114 : n.a.	81 : 388	120 : n.a.	45:25:00	120 : 99
Deal finance	VC (captive)	VC (captive)	VC (independent)	VC (captive)	VC (captive)	VC (independent)	Debt	Debt
Ownership changes since 1998	MBO lead and VC bought out 2001. Other MBO member bought out 2003.	MBO team xc 1 bought out in 2001. 2 VCs bought out in 2004/6. 76% owned by MD; 24% by FD.	MBI team bought out by new managementteam in 2000. Bought by competitor in 2006.	Closed in 2003.	Bought by multinational media group in 2001.	Last tranche of shares bought in 2000. Closed in 2001.	2nd MBO in 2006	Former owner's minority shares bought in 2006
Control changes	New board structure 2004.	MD replaced in 1999. Director resignations in 2000, 2001. 2003 & 2004.	New board structure in 2000, 2006. Changes in directors in 2005 & 2007.	Changes in directors in 1999, 2002 & 2004. MD resigned in 2003.	Changes in directors in 1999, 2001, 2003, 2004 & 2006.	Chair pre-MBO resigned in 2000. Dir ectors resigned in 2001.	MD retired in 2002. New board structure in 2006.	
Family involvement	Continuing. 50/50 owned by son & daughter of founder	Until 2000.	Until 2000.	None since MBI.	None since MBO.	Until 2000.	None in firm. Family own business' premises.	Family on board until 2006. 12.5% in trust for family.
MBO team involvement	2 of 4 in original team	FD was 1 of 4 in original team.	All MBI team resigned by 2000.	MBI lead resigned in 2003. One involved till liquidation.	Last member of MBO team resigned in 2006.	All team involved up to closure.	1 of 4 first MBO team in 2nd MBO.	All original team still involved in similar roles.
Major strategic changes	Overseas manufacture. Restructured. New rentals company.	New products.	New branches. Change regional to national focus.	Restructured. Subsidiaries and holdings company. 1 subsidiary sold out of receivership.	Change of name in 2003. New markets and products.		New markets.	Restructured. Subsidiary and holdings company New markets and products.
Interviewed 2006?	MD	MD and employee	Financial Controller	No	No	No	MD	MD

Notes**:** *Last complete financial year pre-MBO/I. **2006 data because 2005 not available. n.a. = not available. MD = Managing Director; FD = Financial Director.

Some aspects of professionalization were evident pre-MBO/I as means of preparing for a buy-out. DISPENSERS introduced more changes when a new managing director / chief executive officer (MD / CEO) was recruited with the intention of leading an MBO. The MD/CEO of DUMPS suggested that structures and systems were put in place as part of grooming the firm for the MBI. In all cases, the MBO/I provided a boost to the process of professionalization. LOCKS had many of the structures and systems associated with professionalization pre-MBO. Following the MBO, there was an increase in decentralisation, changes in the management structure, and the formalisation of governance roles.

In three cases, entrepreneurial management was the norm pre-MBO/I. PLANTS and PIPES both operated as ‘one-man bands’ with a great deal of knowledge residing with the founder (or his son). Both cases suffered difficulties due to the poor management skills of the second-generation family members, and their wish to be involved post-MBO/I. These firms brought in external managing directors two years post-MBO/I and in both cases it was the trigger for higher levels of professionalization. FILMPACKS had also operated as a ‘one-man band’ but here, the introduction of new management team members caused conflict pre-MBO. The latter external managers fought against the entrepreneurial style of management, and forced an MBO. The founder had little control or involvement post-MBO.

LOCKS and BOXES exhibited many of the elements associated with entrepreneurial management, family orientation, informal decision-making process alongside dimensions of professionalization pre-MBO but to a lesser extent post-MBO. DUMPS also showed aspects of both entrepreneurial and professional management pre-MBI. Here, the entrepreneurial aspects dominated and professionalization was associated with ‘window dressing’ prior to the MBI. Entrepreneurial aspects were more deeply embedded within the firm’s culture.

TROLLEYS adopted more of the elements associated with entrepreneurial management. Pre-MBO, the firm already had a reasonable level of professionalization with regard to planning, accounting and control systems. However, the firm had a paternalistic style of leadership. Post-MBO, there was a move from paternalism towards more participation. Since then, the two family members have bought out the other two members of the MBO team. By 2006, the firm had the informality, ad hoc planning and centrality associated with entrepreneurial management.

All four cases still in private ownership had moved towards a more centralised style of management over time since the buy-out. The only original member remaining from the PLANTS MBO team is the finance director. The MD of LOCKS owns 60% of the equity and is now the majority owner. Further, the former family owner’s role had reduced following the MBO, whilst the dominance of the MD had increased. Interviews highlighted the persistence of centralised management alongside the formal governance and systems associated with professionalization.

The Staying Power of Stewardship

A considerable amount of stewardship was present post buy-out and beyond. Employees at PIPES showed a strong attachment to the firm's identity, even though a large national company had bought the firm. The financial controller stated: "What we don't want for them to do is to come along in 12 months time and say 'right we're going to put [name of parent company] above the door now." The centralisation of management highlighted in the surviving privately-held firms appeared to be associated with a strong attachment to the firm, and a long-term view as illustrated in the following quote: "For me, it's a long-term thing you know. I've worked here pretty much since I left college and… it's my life, sort of thing. I love it. So, you know, I'm here for the long haul" (BOXES, internal MD).

Interviewees who were brought in as external MDs, in contrast, showed less attachment to the firm in comparison to founders and to 'internal' MDs. Respondents in the two firms that had closed reported a distinct short-term view and a dominance of personal objectives. The MD of DISPENSERS stated that: "This company will over the next few years grow to about twenty million… in probably about 2 years time we'll have a company which we'll be able to sell". The MD of DUMPS intended selling the company via a trade sale within five years, intimating that his most important motivations were controlling his own company and financial rewards. These responses highlight a lack of attachment to their firms.

In contrast to the surviving firms, the closed firms showed little need for continuity. When asked what he would do differently next time, the MD of DISPENSERS said he would "get rid of the whole management team on day one". He stressed the difficulties of getting people to agree the changes he wanted.

In 2006, respondents in two cases talked about the growing importance of the family in the business. The MD of PLANTS suggested that the firm was becoming more like a family business again: "So I own 76% of the business and the Finance Director owns 24%. ….over the last seven years, we've removed [VC] as a shareholder… and it's almost come full circle back to being almost like the family business again… but with a different culture". The private equity backer had brought in the latter MD when the MBO led by a second generation family member was struggling. By 2006, there were no original family members formally involved in the firm. PLANTS incorporated the structures and systems associated with professionalization whilst allowing aspects of a family culture to resurface.

TROLLEYS returned to family ownership and is now run by the son and daughter of the pre-MBO owners. The new MD explained that disaccord had arisen between the former family owners and the non-family members of the MBO. Though it would fit all definitions of a family business, there were tensions surrounding the perception of TROLLEYS as being a family business: "I think it'll have a family business feel to it I think, but would it be a family? I don't actually class it as a family business". This could be related to the need to be seen to be different from their parents' generation.

In 2006, the MD suggested that the world moved too fast now to be a family business and stated: "The business from when we bought it off my dad in 98, is completely different… We're still doing the same thing but we're going about what we do in a different way". In contrast, the previous non-family MD was more accepting of the 'family' label as illustrated by the following quote: "It's always been a family-type firm, we try to make things formal when we have to … we try and make it relaxed and hope people enjoy themselves".

So, it seems that in former private family firms, elements of stewardship (i.e., attachment to the firm, long-term view, etc.) remain post MBO/I but also that elements of a family culture will re-emerge post MBO/I after the professionalization of management.

Linking Professionalization to Firm Performance

There were clear distinctions between the firms in terms of turnover and employment growth and financial performance post-MBO/I. Two firms had a distinct growth trajectory throughout the 8 years, four firms reported variable performance and two firms closed between the first and second interviews.

Two firms (FILMPACKS and PIPES) had grown enormously post- MBO/I. They were both sold after the MBO/I and provided successful exits for the MBO/I teams. FILMPACKS was sold in 2001 to a multinational media group. PIPES was bought by a national competitor in 2006. The firm had been groomed for a trade sale by growing turnover and profits, raising its profile, and opening branches in strategic locations close to national competitors. Both high growth firms were associated with a move from entrepreneurial to professional management. Earlier discussion also showed that PIPES retained some aspects of a stewardship culture.

Four firms cited varying performance across the period of 8 years. TROLLEYS, PLANTS, LOCKS and BOXES reported periods of growth and decline in sales and profits. The performance of TROLLEYS peaked in 2000 and 2004. Since 2004, profitability has declined in absolute and relative terms. The performance of PLANTS declined following the MBO but since 2001 an upward trend has been reported. The MBO was viewed as a disaster and in 1999 the VCs pushed the management team to advertise for a new MD. Changes in performance in these firms appear to follow changes in the management team.

The MBO of LOCKS was the smoothest of all the cases and the professionalization process appears to have followed a similar steady trajectory. There was evidence of formalising roles and structures around the time of the MBO. The firm has a very centralised leadership style, albeit with continuing family involvement. The sales turnover generated by LOCKS was fairly constant but the profitability has been more variable. A decline in 2004 was due to changes in demand and obsolescence of the main product, which had been predicted but came earlier than planned. The firm reported steady growth and sufficient profitability to pay off debts early but with a reduction in employees. The current MD was a member of the original MBO team at the age of 22. In, 2006, he led a secondary MBO.

Compared to the original MBO team he exhibits more innovative behaviour and has exploited several opportunities with regard to new markets, products and routes to market.

BOXES reported a steady increase in professionalization alongside some aspects of entrepreneurial management. Both rounds of interviews suggest that members of the first MBO team were generally not innovative. They were reluctant owner managers who undertook the MBO to secure their jobs and the future of the firm.

Two cases went into receivership. DUMPS closed in 2003, with one company from the group then bought out of receivership. This trading company is not connected with any of the former owners or managers of DUMPS. DUMPS reported growing sales turnover up to 2003 and positive operating profits every year except 2003. High leverage and interest charges led to losses after tax every year from 2000 to 2003.

It can be inferred from the financial results that this firm closed due to the highly leveraged MBI and insufficient liquidity to service the debt. The problems may stem from the MBI process and the deal itself. There had been high levels of information asymmetry in the MBI process, to the extent that the agreed price was adjusted down by £0.5 million post-MBI. There was little knowledge transfer as the vendor had no involvement post-MBI and the leading sales team had been poached by a customer just after the MBI.

DISPENSERS closed in 2001 and the company was liquidated. This was a highly leveraged MBO with gearing of 3,108% in 1998, most of which was short-term debt. The liquidity ratio was consistently low at 0.5. Turnover remained fairly constant at £9 million post-MBO. Expectations on MBO were that the company would grow to £20 million turnover in four years, and would then be sold through a trade sale. In contrast to DUMPS, the MBO of DISPENSERS was strategically planned and knowledge transfer occurred over a few years prior to the MBO. A CEO was brought in with the stated purpose of leading a MBO.

Both closed firms had MBO/I teams that reported high levels of optimism and short-term goals of substantially increasing their individual personal wealth. Both acquiring MDs of these companies did not trust previous owners and managers. Both firms increased the level of professionalization post-MBO/I but neither firm exhibited any elements of a stewardship culture.

So, it seems that in former private family firms, superior firm performance post MBO/I is positively associated with maintaining a balance between entrepreneurial and professional styles of management. In former private family firms, the rejection of elements of stewardship post MBO/I is negatively associated with superior firm performance.

Implications

The most striking finding is that succession through an MBO/I can provide a mechanism whereby the former private family firm not only maintains its independent ownership but where the culture of stewardship can be sustained, albeit in a metamorphosed state in a professionalised firm. An MBO/I may, therefore, be an important transitory phase that facilitates professionalization.

Professionalised MBO/I firms may also include aspects of entrepreneurial management. The introduction of elements of professionalization is relative and a progression. There is a need to balance the best aspects of both professionalization and stewardship cultures within family firms with regard to the family firm succession context. Succession through MBO/I may provide a juncture at which the status quo can be reconfigured which may otherwise have been more difficult to achieve. Nevertheless, there was some resistance to being seen as a family firm, perhaps because this label would indicate that the business was less professional.

The sustainability of elements of stewardship can underpin a firm's long-term strategy. Failure to acknowledge this and the over-emphasis on governance issues may lead to a misunderstanding of the motivations of firms, and inappropriate advice. Attempts to move fully to a professionalised approach may risk losing more intangible benefits of stewardship such as commitment and loyalty, which may make an important contribution to performance.