GENERATIONAL CHANGE FOR DOOR DISTRIBUTORS | PART 1

5 Keys to Succession Success

SOFTWARE for Hardware®

5 KEYS TO SUCCESS SERIES

CONTENTS

INTRODUCTION

Door, frame and hardware distributors today face two types of generational change. First, family owned distributors across the industry face the milestone of transitioning the leadership of their business to a son, daughter, or other younger person. While succession of the family business is never easy, this new millennial generation presents challenges not seen decades ago. Second, distributors face the daily reality of older employees retiring and the need to hire replacement new generation staff. The work style, career mindset, and value system of these new "millennial" employees differs vastly from the departing "baby boomers".

To properly address this broad topic of generational change, Software for Hardware presents a two-part research publication. ***5 Keys to Succession Success*** presents the research and recommendations on how to survive and thrive a family business through transition to the next generation. This research includes the common reasons family owned businesses fail in the second generation.

To help door distributor business owners avoid transition failure, this paper presents the 5 key action items that will greatly increase the likelihood of business success in second generation and beyond. Part 2, "***5 Keys to Success with Millennials***, presents research and recommendations relative to hiring and managing the new generation.

Software for Hardware regularly publishes "***5 Keys to Success***" white papers on relevant topics to help door distributors operate more efficient and profitable businesses. All white papers can be downloaded at *www.softwareforhardware.com*. Feedback on this paper, or any topic ideas for future Software for Hardware "***5 Keys to Success***" white papers, please send us your feedback at *info@softwareforhardware.com*.

"...how to survive and thrive a family business through transition to the next generation."

NEXT GENERATION SUCCESSION

According to the U.S. Bureau of the Census, 2011, *90% of U.S. businesses are family owned*. Family owned businesses account for 68% of the nation's gross domestic product (GDP) and generate 78% of new job growth in the economy. These statistics also hold true in the door, frame, and hardware industry and may even be conservative estimates. In addition, the research data indicates that family owned businesses operate at a 6.7% higher profitability level than non-family owned businesses. By any measure, preserving the family owned business for the future is a significantly important driver for the health of the U.S. economy.

The phenomenon of family owned businesses transitioning to the next generation is a rapidly accelerating trend. In fact, the U.S. Census Bureau reports that 10,000 baby boomers retire every day. The U.S. Federal Reserve projects that the trend will continue to increase through 2028.

Those in the door industry know this trend firsthand. Observers at the annual DHI Conference note the increasing prevalence of grey hair on most attendees. Industry vendors that talk to door distributors remark similarly.

"Software for Hardware supports hundreds of door, frame and hardware distributors nationwide. We regularly assist distributors in the transition to the next generation. In fact, "next generation" business owners are our largest new customer segment." ~ Lisa Oxman, President, Software for Hardware

Failure Statistics

The process of succession, handing down the business to the next generation, would seem a natural and low risk process. Unfortunately, the statistics suggest otherwise. While hard to believe, 70% of family run businesses fail under 2nd generation leadership and an astounding 88% will fail in the third generation. Numerous sources including: U.S. Census Bureau, Deloitte Consulting, PwC, and IBM confirm these alarming statistics.

70% of family run businesses fail under 2nd generation leadership ~ U.S. Dept. of Commerce, 2016

These statistics appear surprising, but the risk of next generation business failure has long been known. Wealthy industrialist Andrew Carnegie often said, "Shirtsleeves to shirtsleeves in three generations." Even in the early 1900s, Carnegie understood that wealth rarely survived successive generations. The first generation worked in shirtsleeves to build the wealth and by the third generation, the grandchildren were back laboring in shirtsleeves with fortunes lost. Centuries prior to Carnegie, a Chinese proverb stated the same, "Wealth never survives three generations."

"Shirtsleeves to shirtsleeves in three generations."
~ Andrew Carnegie

But, many businesses find even greater success in next generations. For example, within the door, frame, hardware industry, the Hager Companies, a family run business, now operates under the 6th generation of the Hager family. The Hager Company business began in 1848 and thrives today largely because the family leaders continue to focus on pride, integrity and what's best for the next generation.

"...the Hager Companies, a family run business, now operates under the 6th generation..." ~ Hager Cos

Hager Companies proves that family businesses can succeed in the second generation and beyond. Successful second generation businesses avoid common failure pitfalls and focus on a few "rules of thumbs" for success. The pitfalls to failure fall into two categories: personal dynamics and business practices. Let's first examine the business practices that impede the successful transition of a family business to the next generation.

Business Practices Leading to Succession Failure

"There's always a place here for you."

Several common business practices become points of succession failure. George Stalk Jr., a senior advisor with Boston Consulting Group, and expert on family business succession, identified several common business practices that lead to succession failure in the second and third generations.

Common Failure #1 – "There's always a place here for you." While an admirable sentiment, this common policy of family businesses can lead to failure. As stated earlier in this paper, millennials seek different life goals and assuming leadership of the family business may no longer rank as a top priority. When the owner affords the child the family business as a fallback option, the millennial child often assumes the role only after exhausting more exciting alternatives. The child joins the family business as the "fall-back" and does so with less commitment, desire, and preparation. This practice of "leaving the door open" for family members also disrespects long-time non-family employees who may have earned the opportunity to lead. When the child returns, valued employees often choose to leave the company.

Common Failure #2 – Confusing the value of tradition with the need for business progress. Just because Dad did it "old school" doesn't mean all of his antiquated business processes should remain in place. Businesses that survive many generations, like Hager Companies, do so by adapting and adopting new and more efficient ways to conduct business.

Common Failure #3 – Fear of Taking Risk. It is human nature, especially in assuming a new leadership role, to avoid risk, avoid conflict, and avoid change. In the typical scenario where no true succession planning occurred, the new generation may assume leadership with little time to think and prepare. As a result, it becomes a very stressful situation and normal human behavior is to eliminate as much risk as possible. This risk avoidance can seriously impact the long-term growth of the company.

Planning and Personal Dynamics

One of the largest reasons why so many businesses fail in the next generation is simply a lack of planning. As the all-time great UCLA basketball coach John Wooden often said, "Failing to plan is planning to fail." Rich Sorenson, Professor and Chair of Family Business at University of St. Thomas shares Coach Wooden's sentiment. Professor Sorenson has studied family owned businesses and comments, "Generational succession planning becomes so difficult because it raises many hard to face and emotional questions." Bottom line, succession planning demands a process that looks toward the inevitable departure of the head of the family. Family members often find this topic difficult to discuss. Discussing succession touches on subjects such as: retirement, respect,

expectations, ambitions, and often deep emotions all rolled into one conversation.

Furthermore, most businesses don't even entertain conversations on the topic until far too late. According to the National Bureau of Economic Research Family Business Alliance (2016), 43% of family-owned business have no succession plan. However, 75% of these same business owners fully expect to pass their business to the next generation. Obviously, a gap exists as family members choose to avoid a potentially emotionally charged conversation. But, without planning, the result becomes a time sensitive situation that can lead to more emotional, strained relationships and legal actions.

This lack of succession planning extends beyond small family businesses and includes large family owned corporations as well. A Harvard Business Review study in 2012 showed that 41% of large family owned corporations do not have a CEO succession plan. 29% of Board members reported they are uncomfortable raising and discussing the subject of succession.

> ***"Failing to plan is planning to fail."*** ~ John Wooden
> UCLA Basketball Coach, Basketball Hall of Fame, Presidential Medal of Freedom

Joe Fahey, PNC Director of Business Succession Planning, suggests as a rule of thumb, a 10 year succession planning window. This allow for years leading into the handoff and years for the departing leader to remain onboard and comfortably transition. While seeming excessive, the pre-years provide the selected family member time to learn the business and train for any new skills needed to perform the leadership role. The long timeframe also comforts the departing leader to transition out slowly and adapt to a new lifestyle.

Another personal dynamic which commonly leads to second generation failure is that many families grow faster than their business. The owner/founder may have many children but most small family run businesses simply cannot support hiring every child. Regardless, the owner certainly wishes to please each child and avoid an explosively uncomfortable family dynamic of picking one child over others to join the business. Hence, the owner welcomes all the children which can burden the business with unsustainable salary expenses.

5 KEYS TO SUCCESSION SUCCESS

With so many factors at play working against successful succession, the 70% failure rate of the second generation certainly becomes more believable. But as the Bible states, ***"Let not your heart be troubled."*** Proven keys to succession success exist!

Key #1 – Succession Plan

As stated earlier, most business don't discuss or document a plan for succession. Simply discussing, planning, and documenting action items will dramatically increase the success of the new generation leader. Professor John Davis, of MIT Management Executive Program, studied hundreds of family businesses and their success or failure in continuing operations into the second generation. Professor Davis concluded that simply having a plan, any plan, dramatically increases success. Prof. Davis determined that the most successful plans contained elements of growth initiatives, talent development and staff unity.

Succession Success = Growth + Talent + Unity

Key #2 – Growth Initiatives

While seeming obvious, every business seeks growth, but as *Common Failure #3* states, new leaders in new situations often seek to avoid risk which in turn reduces growth opportunities. The risk aversion reaction is completely understandable as the new leader experiences a large amount of change in a short period of time. Plus, with many businesses having no documented succession plan to guide the new leader, stress increases, and new growth initiatives further reduce. A good succession plan outlines growth initiatives and keeps the company moving forward.

Key #3 – Talent Development

Just because the second generation child now sits in the big chair, by no means bestows the child with the necessary experience and skills to succeed. Companies that succeed in transitioning to the next generation typically invest in training and skill development for the new leaders and for the entire staff. During the transition, the upcoming new generation leader must spend the necessary time to learn the business, learn the skills, and then comfortably occupy the big chair.

Key #4 – Staff Unity

Largely overlooked, creating an environment of loyalty and teamwork enables the staff to quickly accept the new leader and continue their dedication to the company. In a family run business, over years and decades, the staff becomes personally invested in the founder. When the child assumes leadership, the staff often loses that longtime trusted figure who earned their loyalty. However, the transition can happen if the organization adheres to values larger than just the founder. Hager Companies for example, adheres to values of pride and integrity which remain core to the company, and the staff, regardless of which family member leads the company. In fact, the Hager Companies tagline, "One Family, One Brand, One Vision" also points to values beyond any individual leader or generation. Unity benefits the new leader in creating a rally cry, a belief in a larger principal and a point of loyalty to orient the new leadership team.

Key #5 – Resources

Professor Davis recommends a corollary to his success plan formula. The corollary contends that [Growth + Talent + Unity] requires a foundation of necessary resources. For example, growth initiatives don't simply happen because the owner writes it on paper or discusses it in a meeting. Growth happens when the company dedicates the focus and invests in the resources needed to make the initiative a reality. As the saying goes, "Talk is cheap." The new leader must focus on implementing structural and resources investments that will support growth initiatives, talent development, and staff unity. Technology investments can be successful resource investments during generational transition.

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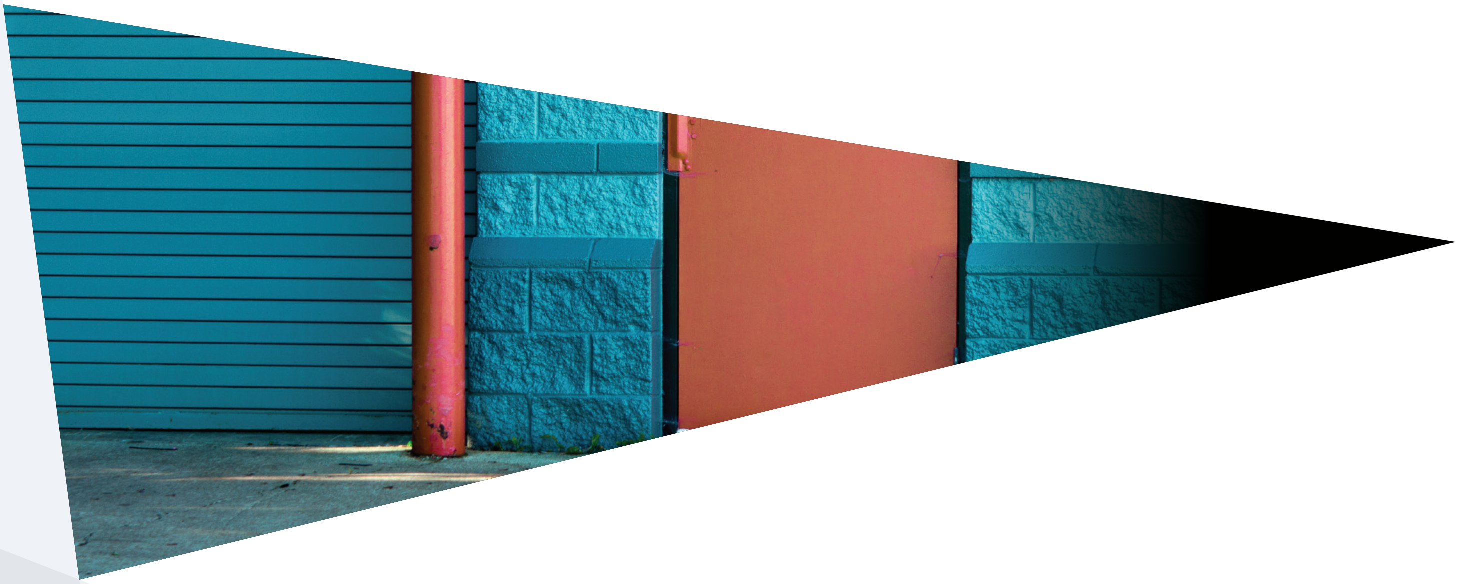

5 KEYS TO SUCCESSION SUCCESS

CONCLUSION

This white paper presented data and recommendations on family owned business succession including both the pitfalls and the keys to success. Unfortunately, research shows that 70% of businesses fail under second generation leadership and only 12% survive to the third generation. Research shows that having a documented succession plan, multi-year in scope, remains critical. That plan should contain a formula for next generation success which includes new initiatives for business growth, talent development, staff unity and adoption of new technology. These actions tremendously boost the success rate of a business transitioning to next generations.

Distributors across North America contact Software for Hardware seeking new technology and advice to help manage these transitions and position their business to operate more efficiently and profitably. If you find yourself facing a similar reality, please visit us at *www.softwareforhardware.com* or contact us at *info@softwareforhardware.com*.

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ABOUT SOFTWARE FOR HARDWARE, LLC

Based in Atlanta, GA since 1996, Software for Hardware provides software to commercial door, frame and hardware distributors across the U.S. and Canada. Nearly 1,000 door industry professionals rely on Software for Hardware to improve their business efficiency, client responsiveness, and bottom line profitability. As a result, Software for Hardware has become the fastest growing software company in the industry and the software of choice for door distributors.

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