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FAMILY BUSINESS - BLOG

Exiting the Family Firm – Are You Ready to Make the Break?

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Exiting the family firm is perhaps the most difficult decision a family will ever have to take. Sometimes the exit forces are so strong, this is the only path forward, but there is life after sale.

There is no doubt that family firms are starting to dominate global business. But they're not short of challenges to ensure their longevity. [Late last year](#), I spoke of family assets and roadblocks which determine the options available to the family in terms of ownership and governance. There are many options to ensure a path of success, but occasionally, a family has to cut its losses and move on. When there is a combination of 1) declining strategic value of the assets that built the company and 2) increasing roadblocks, this is the right time to investigate exit options. Some exits are swift and definitive, others can take years as we saw in the case of the Cadbury family's exit from the business in another of my [earlier posts](#).

Sometimes the industry will force a family to sell the business as was witnessed in the luxury sector when luxury conglomerates such as LVMH, formed from the merger of Louis Vuitton with Moët Hennessy and Kering, formerly Pinault-Printemps-Redoute (PPR), bought many luxury family businesses. Fendi, Givenchy, Kenzo, Saint Laurent and Burberry have all taken the decision to exit their businesses because

the globalised market place required upscaling more than they were able to cope with if they remained a family-run concern. At other times, however, there are less pressing factors which can cause an exit decision to be ignored for too long.

The entrepreneur's plight

Looking at the exit process from an entrepreneur's perspective, it is easy to see how the tough questions concerning exiting the business are often postponed because of the difficult psychological aspects associated with retirement. The example of Herbert H. Haft, an American entrepreneur, demonstrates how a business empire was dragged down and ruined by the family that had built it. Having successfully built a thriving empire over four decades in the mid-to-late 20th century, Haft earned \$250 million when the firm was bought out. Going into business in 1977 with his eldest son, Robert, the pair went on to build Crown Books which was the third largest book store in the U.S. And yet, in 1993 Robert gave an interview with the Wall Street Journal where he claimed that his father was about to retire without actually having discussed the topic with him, which resulted in Robert being fired the day after the interview was published.

A very public family feud ensued which brought about Herbert appointing his other son, Ronald, as CEO of the group. However, after only one year in charge, he was fired by his father over a disagreement about real estate and this culminated in a full-blown legal battle between Herbert and all the other family members.

As a result of the disharmony, Crown books fell into decline and filed for bankruptcy in 2001. Two failed online health companies later (the first started by Robert; the second started by Herbert which were in direct competition with each other) together with Herbert's deathbed marriage at the age of 83 to his long-time companion which cut the children out of his will, saw the end of Herbert's fortune and family harmony. From the outside it's not easy to understand how all this happened.

It's never too early to start planning

The Haft family debacle underlines the difficulty for entrepreneurs of reaching the exit decision and the irrational path they may take. In interviews that I conducted with almost 2,800 owner-managers of family businesses who were planning to exit the business at some point in the next decade, the numbers who were actively preparing the exit process speak for themselves. For those who plan to exit within the next two years, 10 percent have not started planning for exit yet, half have finalised their exit plans and 40 percent are still in the planning process. For those who plan to exit from two to five years hence, almost one-third have not started planning yet and only one quarter have finalised their plans.

If you are starting out on the exit planning process, there are a number of key issues which must be addressed. These include the timing, the exit model, and what the family will do afterwards. It can never be too early to start thinking about the future and what potential exit models could be right for your business.

Exit models explained

Several models exist for families wishing to exit their business: a management buyout (MBO), a management buy-in (MBI), selling to a strategic buyer who could be a competitor, or selling to a private equity fund. The simplest model is the management buy-out because this is typically the outcome of a long process where the existing senior managers and the owners have been talking and planning for some time. The advantages to this model are many: the new owners know the business inside out and the loss of family assets is smaller as incumbent senior managers can exploit the same business and political networks and will already have a deep understanding of the family values underpinning the business model.

The management buy-in is more challenging because the family sells to one or more outside investors who typically will have no relationship already established with the firm. Thus the new owner-managers' business strategies will be less anchored in the previous strategy and over time there may be changes.

A third exit model is to sell to a strategic buyer – a firm or owner-manager that sees the firm as a strategic asset to add to its existing assets with the aim of expanding. It could be a local competitor who knows the family and the business well or a national competitor who is looking to consolidate its industry position. Alternatively it could be a foreign player that wants to establish its presence in the country.

This type of model has its own challenges. The first is to be ready for sale when the right buyer arrives. Most families assume they can choose the timing of their exit. While in principle this is true, a buyer may not be ready when they want to exit; on the other hand the family may not be ready when the right buyer does appear and it can be a costly mistake if the buyer chooses to purchase a competitor instead, thus intensifying the competition.

A fourth exit model is to sell to a private equity fund or a similar financial investor, which can appear attractive to many families because they think they will get a good price for the business but very few family firms ever get this option. Private equity firms buy up firms of a certain size, within certain industries, and with a clear potential for expansion. In reality, this is only an option for a select few family firms.

Life after sale

For those companies that have successfully manoeuvred the exit process, in whichever form it takes, life after sale is a new challenge. It may sound easy no longer having a business to run and having lots of cash to finance a comfortable life, but suddenly the glue that had tied the family together is gone and it is not clear what replaces it.

The most common and simplistic model is to split the surplus of the sale and let family members continue their lives, however, a more ambitious strategy for good communicators is to stay together and invest the proceeds in new ventures – in effect the family becomes a private equity investor. These future ventures can be structured through the creation of a family office although this set-up will demand a certain amount of wealth given the expense of operating such an office.

Selling the business doesn't have to mean the end of the road, and if ever there was a good time to start planning, that time is now as you set off with your family business map in hand.



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