A NEW APPROACH TO MANAGING A SUCCESSFUL GENERATIONAL SHIFT: A CASE STUDY OF ILLY CAFFÈ

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Abstract

It is a matter of fact that the family businesses share common characteristics and face common problems, among which the generational shift is widely recognized to be the most relevant. In the last years, there has been a growing interest in the study of family firms but a little attention still has been paid to succession planning, and only a few studies tried to identify and assess which factors have a positive influence on a successful generational shift. This paper aims to identify, using a qualitative method applied to an Italian case study (Illy Caffè), which key factors can manage in a successful way the generation transition.

1. INTRODUCTION

The backbone of the Italian production system is represented by SMEs which make up 76% of the total enterprises and of these 86% are micro-enterprises (turnover of less than € 2 million) (AIDAF, 2017) and in the majority of Italian SMEs, there is the significant presence of family businesses that alone account for more than 85% of the total Italian companies (AIDAF, 2017). Generally, the academic and professional researches on family business open with the assertion that fewer than 30% of family businesses are passed on the second generation and only 10% make it to the third generation. Therefore, a long-term commitment to continue the enterprise as a family business is often nothing else than a dream of the founder. One the main aspect of literature on family business is the generational shift that is the transfer of business from one generation to another. In this regard, most of the authors have shown how the generational shift in family businesses is a moment of discontinuity in the government actionable to condition, positively or negatively, the continuity of the business system. Each generation of a family business carries different priorities when it comes to ownership, governance, management and future strategy. When priorities are not aligned or come into direct opposition, it can threaten the stability of the business and the family as well. The prevailing literature favors a pessimistic view of the entrepreneurial succession, even defined as "if it were a crisis to be overcome" (Dyck et al., 2002, p. 145), this view is corroborated by the aforementioned dramatic data on the survival of the Italian companies. In some cases, it has recognized that succession "can be, on the one hand, a formidable opportunity for revitalization and relaunch of business development, but also, on the other hand, a source of insurmountable difficulties for the fate of the company" (Boldizzoni et al., 2000). Many studies seek to identify succession as a threat that the subjects involved, such as the entrepreneur, the company and the family, various capacities and different forms called to deal with, protecting oneself from a series of errors to be avoided at the end of "limiting damage". Prior researches suggest that generational continuity is a logical necessity that is found in all organizational systems, including businesses and families, which must be planned on time and carefully managed by companies and families more prosperous and consolidated (Murray, 2003). We hold the view that a generational shift is a process, not an event (Chittoor & Das, 2007). Thus, attention to the process of family business succession is warranted. However, family businesses and succession are often investigated exclusively from the perspective of ownership (Lansberg, 1999; Sten, 2001). This could lead to misleading considerations. In fact, there are many cases where the ownership of the business is no longer in charge of the family, but family is still strongly involved in the day-to-day management. This is not a failure surely although the family hasn't the ownership. This paper aims to investigate how a successful succession can be managed from the perspective of the whole family business system as a dynamic entity not only on planning the operational aspect of transferring managerial and leadership roles and power. Our research question is: *How does the whole family business system manage a successful generational transition?*

To gain insight and be able to offer an explanation, we used a single case study (Yin, 1994). The case study chosen is Illy Caffè due to their generational shift can be defined "revolutionary" because the archetypal form and structure that upheld the previous generation's involvement with the business is totally changed and turn into a deeply different and new archetypal form and structures. Our study aim to analyzing Illy Caffè from a particular perspective: the influence of the family and its values in commercial success. In parallel, the history of the Illy family will be analyzed and how it has transformed a retail business into a well-known multinational group. Our study makes two contributions to the literature. First, by drawing on the system perspective, we show how family management can positively affect profitability beyond the founder generation. Second, we contribute to the family business literature by analyzing empirically how a family firm can manage successfully its generational transition, in particular investigating if there are some conditions that might be considered as best practices necessary to shift from an archetypal form of ownership to an innovative governance.

The remaining part of this paper is organized as follows: Section 2 outlines the main literature; Section 3 explains the methodology used for our analysis; Section 4 presents the findings; Section 5 discusses the results, implications and concludes.

2. LITERATURE REVIEW

The scientific literature review points out three main players in the transition of a family business: the individual (founder/successor), the family and the business. The interaction of these players leads to a successful or not successful generational shift. The pursuit of generational continuity must be faced with appropriate tools, able to act on the different variables at stake (enterprise, family, internal and external environment), to manage the generation transition as a phase of development of the company, not only from the point of income view, but also in terms of expanding the company's know-how, new alliances, opportunities, to push the range innovation, the diversification of channels and markets, re-launching and revitalizing short and long-term strategies. The exit or failure of a large number of family businesses could be avoided by using an effective governance mechanism, such as a board of directors. Murray (2003), based on longitudinal case study analysis, indicates that the transition periods contains a sequence of phases and each phase has a distinct task that the whole family enterprise system needs to address and this process requires between three to eight year to complete. Lambrecht (2005) asserts that the transfer of the family business to following generations is a lifelong, continuing process; planning the succession is necessary but not a sufficient condition because succession is not about transfer the business from one generation to the next generation repeated in a discontinuous time intervals (on average of 25 years like the duration of one generation. It is about a continuous to further generations, indeed. Sciascia et al. (2014), using a regression model, show a positive significant relationship between family management and profitability exists at later generational stages. Their findings may help to address the conflicting results in the literature, which do not account for the contingency role of a generational stage that may change the family managers' goals and shift the firm from financial goals to non-financial goals over time. About governance tools, formal and informal meeting, rules and protocols are used. For example, Ward and Handy (1988) argue firmly with 3rd or 4th generation family owner seems more likely to have outsider boards (an outside board is a board with at least 2 outsiders). According to Schwartz and Barnes (1991), the family business of the 4th and subsequent generations is more likely to have outside boards (an outside board is a board with at least 1 outsider). Regarding the governance tools, Fiegener et al. (2000) asserts a larger board representation by family directors in multi-generational enterprises; Bammens et al. (2008) indicate a convex generational evolution in the need for board advice, and rise over the generations in the need for a board control; the number of family directors seems to increase over the generations. Adding further generations brings the need for even more improvement: Van den Berghe and Carchon (2002) assert the higher family member ratio in board of directors 3rd generation than in 1st and 2nd generation; Westhead et al. (2002) points out multigenerational companies have, on average, more directors than 1st generation; furthermore, a larger proportion of multi-generation (19%) rather than 1st generation company (9%) employ a non-executive director.

According to Mustakallio et al. (2002), there is a significant positive correlation between generation and the use of family institutions. For example, Cabrera-Suarez and Santana-Martìn (2002) assert the presence of a board increase as in line with generations; the average percentage of family directors augments with successive generations; the average percentage of external directors that are family members rises with successive generations, there's a convex trend in occurrence of CEO-duality; a larger proportion of firms in 3rd generations do not pay their board members and with regards to family governance informal meetings increase in importance from the 2nd generation and the presence of formal mechanism family protocols rises with the passing generations. About the succession planning, Sonfield and Lusser (2004) argue that the 1st generation firs do less succession planning than the 2nd and 3rd generations.

It needs to take in account that a large part of research on family firms is based on the investigation of family firms' goals and the diversity of topics related to family firms goals (Della Piana et al., 2017). Particular attention is reserved for the family firms' goals setting process and the mechanisms through which family firms' goals are formed and how outcomes are achieved (Williams et al., 2018). The behavioural theorists have suggested that firms have a variety of non-economic as well as economic goals (Argote & Greve, 2007; Cyert & March, 1963). Chrisman et al. (2012), highlight that some kinds of goals originate from the emotional value of family properties (Astrachan & Jaskiewicz, 2008; Zellweger & Astrachan, 2008), from the importance of family social capital (Arregle et al., 2007; Pearson et al., 2008) and by the emphasis on the creation and preservation of the family socio-emotional wealth (Gomez-Mejia et al., 2007).

The stakeholder theory (Freeman, 2010; Mitchell et al., 1997), starting from the assumption that family firms have the family as unique and powerful stakeholders, supports the importance of family-centered non-economic goals and provides a complementary view in the identification of non-economic goals such as 'family harmony' and 'social status'. Additionally, Berrone et al., (2012) pointed out that altruism, fairness, justice, and generosity represent the main goals of family firms. This heterogeneity among family firms' goals is due to the distinctive values and socio-cultural characteristics of the subject involved in the decision-making process. According to Williams et al. (2018), the presence of an owning-family and its control over the business represents a significant family firms' goal antecedent. A definition of firms' goal is given by Kotlar and De Massis (2013, p. 1264-1265), "defining the goals adopted by an organization requires specifying who is able to influence firm decision, the element that may affect their individual goals and, more importantly, the processes through which the individual preferences are translated into organizational policy and action". The two authors considering the differences among the types of family firms and organizational members introduced taxonomy of four main goal categories: economic, non-economic, family, non-family.

In our analysis, we follow the taxonomy developed by Kotlar and De Massis. The first goals category is Family-Centred Non-Economic goals (FC-NE). These types of goals may change over time and reflect the attitudes, values, perceptions, and intentions of the family firm's coalition members. The main Family-Centred Non-Economic goals are family harmony, the family's social status, and its reputation, as well as the family identity linkage. The second category of goals is Family-Centred Economic goals (FC-E). In this category, the interest of the family consists exclusively in the maintenance of family control over the firm and the preservation of wealth created by all family's members throughout the history. The third category of goals is Non-Family-Centred Non-Economic goals (NFC-NE). These types of goals, such as the improvement and conservation of good relationships with internal and external stakeholder. The fourth category of goals is Non-Family-Centred Economic goals (NFC-EC). These types of goals, which include different indicators of economic performance (i.e. growth, survival, and the profit), are not explicitly oriented to the family and are strictly related to the economic aspects of the business.

Clearly, there is a need to identify first these goals and assess how they are perceived with respect to all the others in order to have a fuller understanding of the vision that family businesses have about their own growth.

3. METHOD

We used a single case study approach (Yin, 1994; Eisenhardt, 1989). According to De Massis and Kotlar (2014), case studies are a powerful methodology that can be used in a rigorous, creative and wide-ranging variety of ways to advance family business research. We adopt this type of methodology for a few reasons. First, a case study is suitable for examining processes (Gephart, 2004) and addressing "how" and "why" questions (Yin, 1994; Eisenhardt, 1989). Second, because our phenomenon of interest (generational shift) is contextually anchored and involves social and business dimensions. Finally, the exploratory (rather than confirmatory) nature of our study also suggests the need for a qualitative approach. It also should take into account that study research is an appropriate approach with which to gain a more fine-grained understanding of the differences within the heterogeneous population of family firms (De Massis & Kotlar, 2014). We followed the triangulation based on mixing data sources types (i.e. Begley, 1996; Denzin, 1978; Farquhar & Michels, 2016; Olsen, 2004): financial reports, newspapers, web site information and interview with Daria Illy (CEO Mitaca) member of 4th Illy's generation. According to De Massis and Kotlar (2014), the triangulation of evidence derived from multiple data sources is particularly important for family business researches, that's why there's a difficult to separate the aspect entirely related to the family from those are strictly and specifically related to the business decision.

4. RESULTS

Illy Caffè is a well-known worldwide large corporation. It started as a colonial retail shop and in a few years, it turned into an international firm. It led by the fourth generation and the Illy brand is a synonym of the best quality coffee Arabica. The Trieste-based company has built with consistency and determination the success of the brand faithful to the concept of "uniqueness" effectively summarized by the company motto "One brand, one blend" that has always guided the Illy group's mission: the same blend of Arabica coffee is used for all markets, domestic and international, focusing on the quality of the product as a strong point. In order to preserve the success achieved, Illy Caffè has hired outsider managers, it means no family members that can pave the way for business and still leave open the chance of a future family member. Appointing outsider management has brought the business to a new higher thank to new skills and experience. Illy Caffè is one of the first Italian family businesses that adopted a Family Pact, a non-legally binding document that defines roles, relationships, and structure within the family business, protocols for resolving disputes and decision making, remuneration, employment and changes in the family and succession plans for the business and family wealth. It needs to mention that Illy

Caffè has pursued over the years a sustainable business model that generates competitive advantages for the company by combining economic and financial targets with social and environmental goals. The main driver of Illy group is the creation of value for all of the stakeholders involved, along with the entire length of the supply chain.

The first generational shift. Illy Caffè's roots sink in the early '30s when Francesco Illy started in 1933 business activity for the marketing of coffee and cocoa. He turned in a few times a little drugstore into a company. In 1947 Francesco began the first generational shift with the entry into the company of Ernesto Illy, son of Francesco, graduate in Chemistry, who in 1956 becomes co-owner and administrator of the company until he assumed the office of president (1963 – 2005). Despite the growing success, Ernesto remains faithful to family values, stating that "ethics is the compass of our behavior"; therefore, ethics must not only mark the business but also the culture and activity of the companies themselves.

The second generational shift. With the entry into the company of Andrea Illy, son of Ernesto, begins a radical process of reviewing management and eliminating obstacles to growth due to excessive interference of the family in the business management that effectively limited the decision-making space of management. External managers are hired outside the family with imported past experiences, coming from different production sectors, which bring a wealth of skills considered strategic for the company; moreover, training programs are introduced at different levels.

The Illy group maintains, in its governance and ownership structure, the appearance of a family business opening up, at the same time, to contributions outside the family of high level. With the adoption of the family pact, an internal reorganization process is started, oriented first of all to the enhancement of management, especially first and second line, and to the formalization of all company roles. The adoption of a family pact was also due to avoid the formation of a "shadow organization chart" of a family nature as Daria Illy said during her latest interview.

The Illy family pact is the document that sets the rules for access to the company, no family member can access managerial positions if not adequately trained and motivated (for example, knowledge of languages and adequate training is provided professional at other companies, not even in the sector), assigns tasks and responsibilities, a sort of "constitutional paper" of the Illy group that helps to protect business continuity, for the benefit of future generations. The document is the subject of a ten-year review shared by all the adult members of the family.

Andrea Illy introduces the Strategic Committee, an organ formed by the CEO and all the company's front line managers, who are entrusted with the task of making the most relevant decisions and formalizing them in strategic plans. Therefore, the Board has been left with a more controlling role and validation of the aforementioned choices. The downside of these choices is represented by the sharp decrease in the degree of flexibility and informality that characterized the company before Andrea Illy took over the reins of the company.

Lastly, there is the "Family Council", an informal and organizational informal body, which includes all the members of the Illy family and for those who are of age without a company task, participation as "auditors" is envisaged. Thanks to the changes introduced by Andrea, Illy Caffè assumes the typical characteristics of a company with a more entrepreneurial character and highly oriented to the enhancement of knowledge and innovation: the greater involvement of management has prevented the know-how available within the company was lost, rather than recombined, fully exploiting the company's innovative potential.

The third and fourth generational shifts. On December 2016 the brothers Riccardo and Francesco Illy, sons of Andrea, resign from the Board of Directors, giving life to the fourth generational shift. Andrea transfers his baton to his daughter Daria, who has been in the company for some time after his personal training experience, while Francesco makes room for Licerio Degrassi, CFO of the Illy Group holding company, who will be the trainer for the new generations of Illy preparing them for the role of shareholders. In January 2017 also the revision of the family pact starts and it is a fundamental turning point. The Trieste group is controlled by the 4 brothers Francesco, Riccardo, Anna, and Andrea (the third generation) and their mother Anna Rossi.

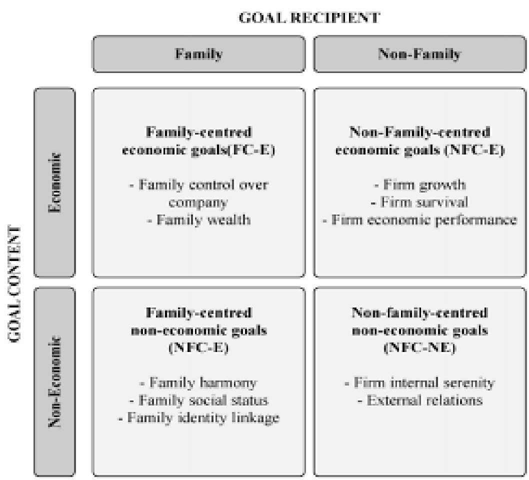
Currently, the ownership structure is divided as follows: Riccardo, Anna, and Andrea each have 23.10% of the holding company, Francesco 20.70% and the remaining 10% belongs to the mother and is divided into 2.5% shares in bare ownership to the 4 children. Riccardo proceeded to transfer the company with the assignment to the only daughter Daria of the bare ownership of the entire package held. The other three brothers have not yet proceeded with the corporate transfer. The 4 Illy brothers have more than one descendant (3 daughters Andrea, 3 daughters and 1 son Francesco, a daughter Anna) and taking into account that each family branch has 1 share with the right to vote, in order to ensure governability, the most appropriate choice is the establishment of a holding company for each business branch that then expresses a single decision and a single representative. The management review process continues, since May 2017, for the first time, Illy Caffè has an unfamiliar AD, Massimiliano Pogliani (former Saeco and Nespresso), and the same choice was made at the holding level where, from October 2017, an external CEO, Federico Marescotti, was appointed. The governance model adopted by the Illy group envisages respect for the complete autonomy of the individual companies belonging to the group and, at the same time, allows the creation and exploitation of inter-group synergies.

5. DISCUSSION AND CONCLUSIONS

The case study analyzed can highlight seven conditions that can we would consider as best practices on generational shift. They are:

1. Distinguish the "family" from the "company": it helps to avoid family concerns or issues have a negative influence on the business;
2. Apply a governance system suitable to guarantee the pursuit of strategic objectives: having a Board of Directors and a defined management team with specific roles and responsibilities assures to run the business in a business decision-making mode;
3. Evaluate the "competence" more than "belonging": a successful generational shift involves evaluating efforts and outcome of performance, not only the relation with family;
4. Define and formalize the shared rules for managing change: the family must find a way to manage the change and how it might impact the family and the business itself;
5. Provide sufficient assets to cope with unforeseen situations: it's a matter of fact that every business should have a plan in place to deal with unforeseen situations especially during a transition;
6. Plan the succession process and the objective to be achieved: implementing a succession plan without the necessary goals and objectives it can lead dire consequences for the business, disagreements, low staff morale and a decline in productivity and profitability;
7. Involve "third parties" who do not belong to the family: can bring important know-how and further professionalization of the family business as well.

Figure 1. Members' goals in family firms



Note: Adapted from Kotlar and De Massis, 2013, p. 1272

Furthermore, the analysis of the Illy Caffè, allows to assert that the company forms part of the third category of Kotlar and De Massis' taxonomy namely Non-Family-Centred Economic goals (NFC-E) as depicted in the Figure 1.

The growth of Illy Caffè is mainly due to innovation and internationalization both perceived as strategic current goals for the growth of the firm. According to Della Piana et al. (2017), an internationalization-based growth assumes greater importance in relation to the future goals, and Illy Caffè strategy confirms that, while the family values drive the long term vision of the business and the family involvement in the ownership.

This study obviously is not free from limitations; nevertheless, these offer some opportunities for future research. We maintain these best practices that need further preparations and verifications to test if our results hold in other geographical settings, i.e. European and not European firms, or if the cultural factors influence the generational shift. It also should take in account the different aspects of family business and the family in business such as culture, strategy, commitment, and social relationship, and how they can be applied successfully to effectively and efficiently manage the generational change. The effects of family management may also be influenced by the institutional environment in which the firms operate. We suggest the substitution of family managers with non-family managers to professionalizing a family firm. Indeed, we cannot exclude that family firms with family members can be professionally and adequately managed.

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