THE LEADERSHIP SHOCK OF GOVERNANCE

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A shock awaits many of the Gulf's family-owned groups when they attempt to strengthen their corporate governance: the implications for executive board members and management are extensive. This observation is in no way an argument against governance. On the contrary, it illustrates how essential governance is to securing future prosperity.

Business leadership will never be the same again

The founders of the most successful groups have typically been both the owner and the leader of the business, and also a family patriarch. The impressive energy of these men is mirrored in the diversified conglomerates that they have created.

The inherent complexity becomes evident when corporate governance and family charters begin to transform what is often very much one man's work into a lasting institution.

Both the board and management are affected when corporate governance is strengthened, whether the motivation is generational succession, requirements associated with financing or partnerships, or an aspiration to better equip the business for the twenty-first century. Board members will shoulder a larger share of responsibility for the group's strategic direction. The executive members cannot just congratulate themselves for the overall success of the group, but must increasingly pay attention to the viability of each individual business. Senior management in the organization will be asked to present plans and business cases for which they will be held accountable. Everybody in a leadership role must start thinking differently and the company's method of operation will change.

This is a pattern of events familiar to any company worldwide that wishes to implement effective corporate governance. However, an observation from my research and work as an executive coach is that companies in the Gulf are more likely to underestimate the time and effort required to ensure a smooth journey. Two phenomena help explain this.

Success is a poor starting point for change

First, the extraordinary success of family-owned groups in the Gulf makes it harder for their owners to perceive the need for managerial and executive change.

Half a trillion barrels of proven oil reserves and 1.5 quadrillion cubic feet of gas reserves in the Gulf Cooperation Council countries do not provide fertile ground for pessimism.[1] The more than 2 trillion dollars held in sovereign wealth funds in the region soften possible concerns about changes in the oil price in the short and medium term.[2] In Kuwait this equates to half a million dollars per national, while the numbers are roughly double for Qatar and quadruple for Abu Dhabi.

Almost anybody who has been in business in any of these six countries for a reasonable length of time has been helped by the region's general growth. International companies needed local sponsors, which added stable income streams to family groups. The Credit Crunch challenged some families, but the conditions for restructuring have, to a large extent, been favourable. The governments are again pursuing aggressively expansive finance policies. The infrastructure projects announced, including those initiated by private investors,[3] have been estimated to 3.45 trillion dollars.

However, an increasing number of industries are seeing the steadily growing demand outpaced by willing and accessible supply. The substantial cash flow generated by local groups is used to build more presence and capacity, and invest in neighbouring countries and adjacent industries. The region's wealth and high activity level draw companies from all over the world. Just ten years ago, such entries were overwhelmingly opportunistic. They now commonly represent companies' strategic priorities. Cities in the Gulf serve as hubs for the entire Middle East and sometimes parts of Africa or Asia, making the GCC countries regional home market. International companies are also placing higher demands on their local sponsors.

The example of Nestlé, the major nutrition, health and wellness company, illustrates the trend. The company entered Saudi Arabia with a sole sponsor in 1955. Nestlé announced its own direct sales and distribution operations in the kingdom, with more than 200 employees, in 2011. The company has also entered into various joint ventures covering a number of business areas.[4] Much of its interaction with consumers and retailers takes place through its global web site, including a special section for the Middle East in both English and Arabic.

1 United States Energy Information Administration.
2 SWF Institute.
3 Zawya, November 25, 2013.
4 Nestlé, press release, 11th of May, 2011.

The region's family owned businesses can no longer expect the general buoyancy of local economies to keep lifting their top and bottom lines. They have to compete for their market share and margin. What really counts in the early stages of an emerging market is to "do the right things", such as selecting new products that are attractive.

Today's intensifying competition makes it pressingly important to also "do things right". The future winners will have to succeed in innovation, customer experience or cost efficiency. Meeting each of these requirements will test a company's leadership and ability to execute.

Executives can be bought but effectiveness cannot

Second, the traditional approach for succession in Arab family businesses has been proven over time but today's large family-run groups require an enhanced approach to ensure their future.

The Bedouin on the Arab peninsula had a very special serving person on hand when he received a guest to his tent. The custom involved host and guest looking each other deeply in the eyes during their conversation. The guest would merely extend his cup to call on the servant for more coffee, without changing position or disrupting the dialogue.[5]

The special servant was the Bedouin host's son. Serving the coffee was not his only task: he was there to listen and observe. Apprenticeship was interwoven in the tribal traditions. Sons followed their fathers to the majlis gatherings from a young age, as they still do to this very day. They got involved in the family business. Yet, no son was guaranteed to succeed his father. A new patriarch could be chosen through consensus among family elders and with involvement of their closest allies. This selection was made from among brothers, sons and nephews based on character, capabilities and connections.

As oil wealth began to accumulate, external managers were hired to help the family members run the business. An attempt was made to build close ties of loyalty by hiring as few clerks as possible. As businesses grew, much of the daily management tended to be delegated, while control was kept through a system of owner approvals and an internal audit function run by particularly trusted people.

Continuous growth led the big groups to rapidly employ herds of expats from other Arab countries, Europe and India among others. As keeping pace with growth was the top priority, less attention was placed on the effectiveness and development of the organization.

5 Thank you to Nasif Kayed, General Manager for The Sheikh Mohammed Centre for Cultural Understanding, for reviewing this and next paragraph.

While the approach has been a necessity, it becomes inefficient and expensive over time. When external hiring is required for almost any new position not given to a family member, from an executive seat on the board to senior management positions in the subsidiaries, then the problem becomes apparent. Any organization will occasionally need to import new talent, but the most effective ones are deeply engaged in nurturing their next generation of leaders.

Contrary to intentions, the old approach also jeopardizes loyalty. Tenured and trusted individuals with solid track records sit on boards, in advisory positions and at the higher management echelons of the Gulf's family groups, but many lack either the appetite or understanding to do what it truly takes to address the pressing challenges that the business faces. Some consciously defend their positions by hiring people who are no threat, or managing their teams purely in their own interest. Others unintentionally become an extra and non-contributing layer in the hierarchy. This all results in the more ambitious, willing and able subordinate employees becoming disillusioned and cynical.

The potential must guide the leadership

Governance is not just about writing down policies and procedures: it involves appointing strong executives that can ensure the success of the business. Having said that, leadership is – just like corporate governance – a means to an end. Any consideration of corporate governance and leaders must start with the goal, which in business is to create value for the shareholders, and work towards it without violating laws and good ethics.

A sequence of four questions will help you dampen the leadership shock and enable the organization to live up to its full potential. The right answers will be unique for each business; just as corporate governance looks slightly different in every successful family group.

1. Where does the largest potential for wealth creation lie? When there is steady economic growth you can diversify your activities, but should typically concentrate your attention and resources when competition increases and markets follow a bumpier road.

2. What assets and capabilities are necessary to succeed? The attractiveness of a business ultimately depends on your ability to accumulate the relevant assets and capabilities that will place you among the winners in your specific field. Ensuring that you possess strong executives with relevant experience and clear sight is a critical element in this.

3. What corporate model should be applied? The motivation for organizing businesses in a group is that there are synergies between them, and you can use one to leverage the other. The nature of opportunities should determine at which end of the spectrum the group should fall: from holding company to integrated corporation.

4. How should the leadership be handled? After answering the above three questions, you have a proper foundation for assessing leadership needs. How many executive roles are pivotal? What backgrounds and merits should the executives filling these roles possess? How should the leadership work in the short term? How should the necessary talent be developed for the future?

Most professionals can become good leaders

Future leaders cannot be grown by merely delegating the task to an already stretched Human Resource department and allocating a budget to training. It is not that leadership cannot be learned. Almost anybody with a genuine interest can rise to become a good manager if they are willing to develop as a professional and gain the relevant experience. Most can also be helped to become effective leaders. However, ensuring that this process is reproducible throughout an organization requires that executives from the very top and line managers further down pay attention to good and bad behaviours, and promote people who are ready to make a significant difference.

Arab families know what it takes to groom a future patriarch. The chairmen of large family groups should ensure that the same persistency is applied more widely in the board and throughout the organization. With this approach quality leaders can be developed, ensuring the future success of the business.