

# a₹tha

E - JOURNAL OF FRTL @ IIM CALCUTTA

September 2023, Volume 11, Issue 2



# Corporate Governance Challenges in Family-Owned Luxury Businesses: Balancing Tradition and Modernization

**Nirbhay Rana**

## Introduction

Family-owned luxury businesses stand as timeless pillars in the global luxury industry, embodying a legacy of artisanal craftsmanship, generational heritage, and personalized experiences. These revered brands hold a unique allure, captivating discerning consumers seeking authenticity and exclusivity. However, beneath their exquisite facades lie intricate corporate governance challenges that arise from the delicate balancing act between cherished traditions and the necessity for modernization.

This article delves into the complexities faced by family-owned luxury businesses in establishing effective governance structures. It explores the significance of finding the right equilibrium between tradition and modernization to ensure sustainable growth, competitiveness, and continued success in an evolving luxury market.

The importance of family-owned luxury businesses in the global luxury landscape cannot be overstated. Their timeless creations and dedication to craftsmanship have captured the hearts of consumers for generations. Yet, as these businesses evolve and expand internationally, they encounter a profound need to adapt their governance practices to meet contemporary demands while safeguarding their cultural heritage and core values.

Traditional governance practices in family-owned luxury businesses often center around familial ties and familial decision-making structures. The close-knit nature of these businesses enables quick decision-making and a cohesive brand vision. However, it also poses potential challenges in terms of maintaining professional management, nurturing a culture of innovation, and ensuring transparency and accountability.

Amidst globalization and evolving luxury consumer preferences, the call for modernization in family-owned luxury businesses grows ever stronger. Integrating independent directors, non-family executives, and professional managers can introduce diverse perspectives and industry expertise. Embracing modern governance practices can enhance adaptability and responsiveness, but it can also encounter resistance from family members reluctant to relinquish control or alter cherished traditions.

The article will explore the intricacies of striking a harmonious balance between the brand's long-term vision and the short-term pressures of the luxury market. Family-owned luxury businesses often emphasize generational legacy over immediate financial gains, making their commitment to long-term sustainability paramount. Finding ways to satisfy these enduring aspirations while addressing contemporary market challenges will be a focal point of discussion.

### **The Significance of Family-Owned Luxury Businesses**

Family-owned luxury businesses epitomize a sense of heritage and authenticity that deeply resonates with discerning consumers who seek timeless craftsmanship and exclusivity. In India, the iconic Tata Group exemplifies this commitment to tradition and quality. Their brands, such as Titan Watches and Tanishq, have captured the essence of Indian luxury, offering exquisite timepieces and jewelry that reflect the nation's rich cultural heritage. This unwavering dedication to quality and personalized experiences sets them apart from corporate-owned luxury brands. Similarly, on the global stage, Italy's Ferragamo family, the founders of Salvatore Ferragamo, has maintained their family-owned luxury brand for generations. Salvatore Ferragamo is renowned for its exceptional footwear, leather goods, and accessories. The Ferragamo family's commitment to artistry and craftsmanship remains a hallmark of their brand, which has become a symbol of Italian luxury worldwide. However, as family-owned luxury businesses expand their reach across international borders, the need for robust governance practices becomes paramount. They encounter diverse cultural, legal, and market conditions that demand adaptable and efficient governance structures to maintain their unique identity. The significance of family-owned luxury businesses extends beyond craftsmanship. They have the remarkable ability to foster strong emotional connections with consumers. For instance, Titan Watches and Tanishq's stories of generational passion, dedication, and craftsmanship resonate deeply with Indian consumers seeking authentic luxury experiences. This emotional bond nurtured by family-owned luxury brands translates into enduring brand loyalty and enthusiastic word-of-mouth referrals, further solidifying their position in the market. However, amidst the allure of tradition, these businesses must also confront the necessity for professionalization and transparency in their governance practices. As they expand globally, they must adhere to robust corporate governance standards to ensure transparency, accountability, and compliance with international business norms. Striking the balance between familial decision-making and external expertise is essential. Engaging independent directors and professional managers can infuse fresh perspectives and industry knowledge into their strategic decisions and practices. This integration of diverse viewpoints fosters adaptability, enabling family-owned luxury businesses to remain relevant and competitive in an ever-changing luxury landscape. Furthermore, the significance of family-owned luxury businesses extends to their potential to contribute to the social and economic development of their regions. Often deeply rooted in their local



communities, they provide employment opportunities, support local artisans, and contribute to cultural preservation. For instance, the Tata Group in India has a rich history of community engagement and corporate social responsibility, enhancing their reputation and creating a positive impact beyond their luxurious products. As family-owned luxury businesses expand globally, they must navigate succession planning carefully to ensure a seamless transition of leadership while preserving the core values that define their brand. The delicate balance between preserving family heritage and embracing modernization is crucial to guarantee the brand's continuity and relevance.

### **Traditional Governance Practices**

Family-owned luxury businesses are often characterized by a strong sense of kinship and personal attachment to the brand's legacy. In such structures, decision-making is frequently centered around family members, leading to a concentration of power and limited external perspectives. While this approach can facilitate quick decision-making and preserve the brand's authenticity, it may pose challenges in terms of professional management, diversification, and succession planning. The traditional governance practices inherent in family-owned luxury businesses serve as a double-edged sword, combining strengths and challenges that impact the brand's long-term sustainability and growth. The strong sense of kinship and family legacy in these businesses fosters a deep emotional connection to the brand, instilling a shared vision and unwavering dedication to its success. This cohesive familial bond often translates into swift and decisive decision-making, enabling them to respond promptly to market opportunities and challenges. Moreover, the preservation of the brand's authenticity is a hallmark of family-owned luxury businesses. The deep-rooted traditions, craftsmanship, and values passed down through generations contribute to their timeless appeal, attracting consumers seeking a genuine and meaningful luxury experience. However, the concentration of decision-making power within the family circle may inadvertently limit external perspectives and expertise. As family members may be emotionally invested in preserving traditions, they may resist adopting modern practices or embracing change to stay relevant in a dynamic market. This reluctance to diversify and adapt can hinder the brand's ability to appeal to evolving consumer preferences and seize new growth opportunities. Professional management is often a pivotal aspect of sustainable business growth, but traditional governance structures may struggle to attract and retain top-tier talent from outside the family. Competent professionals can bring fresh insights, industry expertise, and specialized skills, complementing the brand's heritage with contemporary practices. The integration of external talent can enrich decision-making, improve operational efficiency, and enhance innovation.

Another critical challenge associated with traditional governance is succession planning. The transfer of leadership from one generation to the next is a critical juncture that requires careful planning and execution.



While maintaining a familial legacy is essential, family-owned luxury businesses must simultaneously identify and groom competent successors capable of navigating the complexities of the luxury market while preserving the brand's values.

To overcome these challenges, family-owned luxury businesses can consider adopting a hybrid governance model that combines familial involvement with independent oversight. Introducing independent directors or a board of advisors can provide unbiased guidance and strategic counsel, promoting transparency, accountability, and professional governance practices.

Encouraging family members to actively engage with external industry experts and seek professional development can also enrich their understanding of the ever-changing luxury landscape. This cross-pollination of ideas helps strike a balance between honoring tradition and embracing innovation, enabling the brand to flourish in the global luxury marketplace.

## **Case Study: Performance Analysis of Sabyasachi Couture**

### **Introduction:**

Sabyasachi Couture, founded by renowned Indian fashion designer Sabyasachi Mukherjee in 2002, is a prominent name in the luxury couture segment. The brand offers a diverse product portfolio encompassing bridal couture, apparel for men and women, accessories, and fine jewelry. Sabyasachi has established a strong presence not only in the Indian fashion industry but also in the global market. This case study examines the financial performance of Sabyasachi Couture over the past few years, highlighting key strengths and weaknesses.

### **Financial Performance Analysis:**

**Established Brand and Diversified Portfolio:** Sabyasachi's brand has a strong foothold in India, with a product range that includes bridal couture, accessories, and fine jewelry. The brand's diversification into jewelry in July 2017 marked a significant expansion of its portfolio.

**National and Global Collaborations:** Sabyasachi has strategically entered into collaborations with renowned brands such as Christian Louboutin, Pottery Barn, Thomas Goode & Co, Asian Paints, L'Oreal Paris, and H&M. These collaborations have not only expanded the brand's reach but also enhanced its popularity.

**Improved Financial Performance in FY20:** Sabyasachi Couture showed improved financial performance in FY20, with an approximately 8% year-on-year growth in operating income, reaching Rs. 275 crore. The jewelry segment registered remarkable growth, with a 48% year-on-year increase, while apparel sales experienced a slight decline.

**Comfortable Debt Protection Metrics:** The brand maintains a comfortable debt structure, with low gearing ratios and adequate debt protection metrics. The PBILDT margin improved significantly to 21.89% in FY20, indicating better profitability.

**Liquidity Strength:** Sabyasachi Couture boasts strong liquidity, with substantial accruals, liquid investments, and unutilized bank lines. This liquidity position is crucial for the firm's operational needs and financial stability.

#### **Key Weaknesses:**

**Partnership Concern:** The firm's constitution as a partnership concern poses a risk of capital withdrawal during personal contingencies and dissolution in case of partners' retirement, insolvency, or death. However, there are plans to convert the partnership firm into an LLP.

**Inventory Risk:** The fashion industry's ever-changing trends can lead to inventory obsolescence. While Sabyasachi primarily caters to made-to-order products in the couture category, the jewelry segment carries a higher inventory risk.

**Working Capital Intensive:** The firm's operations require a high level of working capital due to its flagship stores and the need to maintain inventory of raw materials, work in progress, and finished goods.

**Competition and Plagiarism:** The luxury fashion industry is highly competitive, with low entry barriers, and the risk of plagiarism of designs is a concern. Maintaining brand positioning and market share in such an environment requires consistent investment in advertising and branding.

**Impact of COVID-19:** The COVID-19 pandemic led to the closure of stores and workshops, affecting the firm's revenue in FY21. Despite cost control measures, muted performance was expected due to lower consumer spending.

#### **Conclusion**

Sabyasachi Couture has successfully established itself as a prominent luxury couture brand in India and the global market. Its diversified product portfolio, collaborations with renowned brands, and improved financial

performance in FY20 showcase its strengths. However, challenges related to partnership structure, inventory risk, and competition require ongoing attention. The impact of COVID-19 on the luxury fashion industry further underscores the need for adaptability and resilience.

The brand's ability to navigate these challenges and capitalize on its strong brand image and diverse offerings will determine its future growth and sustainability in the luxury couture segment.

### **Modernization and Professionalization**

As family-owned luxury businesses face global competition and evolving consumer demands, embracing modern governance practices becomes imperative. The inclusion of independent directors, non-family executives, and professional managers can inject fresh insights and industry expertise into the decision-making process. However, implementing these changes can be met with resistance, as family members may fear losing control or diluting their brand's unique identity. Embracing modernization and professionalization in family-owned luxury businesses is essential to ensure their relevance and competitiveness in the global luxury market. As the industry evolves, driven by changing consumer behaviors and technological advancements, family-owned brands must adapt their governance practices to thrive in the dynamic business landscape.

The inclusion of independent directors in the boardroom brings an impartial perspective and diverse expertise to the decision-making process. These directors can offer valuable insights on market trends, consumer preferences, and industry best practices, enabling the brand to make informed and forward-thinking strategic decisions. Their presence also enhances transparency and accountability, promoting a culture of corporate responsibility that resonates with stakeholders and investors.

Non-family executives and professional managers can infuse the organization with specialized skills and a broader understanding of modern business practices. Their experience in organizational management, marketing, finance, and technology can optimize operations, drive innovation, and elevate the brand's performance to new heights. By leveraging the strengths of both family members and external professionals, family-owned luxury businesses can achieve a harmonious balance between cherished traditions and progressive evolution. Despite the undeniable benefits of modernization, family members may harbor concerns about losing control or diluting the brand's unique identity. Handing over authority to non-family executives and professional managers may evoke feelings of apprehension, as they fear relinquishing the brand's essence built upon generational heritage. However, effective communication and a shared vision of preserving the brand's legacy while embracing change are critical in assuaging these concerns. To overcome resistance to change, family-owned luxury businesses can gradually introduce modern governance practices, creating a seamless transition that respects the brand's history while aligning with contemporary demands.



Open dialogues and involvement in decision-making processes can foster a sense of ownership and inclusion for family members, enabling them to appreciate the benefits of professionalization.

Moreover, engaging family members in professional development and providing opportunities for them to enhance their skills can empower them to actively contribute to the brand's growth. This proactive approach allows them to bridge the gap between tradition and modernity, fostering a shared commitment to the brand's sustainable success.

### **Balancing Long-Term Vision and Short-Term Pressures**

Family-owned luxury businesses often have a deep commitment to long-term sustainability, emphasizing generational legacy over immediate financial gains. Balancing this vision with the short-term pressures of market demands and investor expectations can be challenging. Striking the right equilibrium between tradition and the need to adapt to rapidly changing consumer preferences is essential to ensure the brand's continued relevance and growth. Balancing long-term vision with short-term pressures is a delicate tightrope act that family-owned luxury businesses must navigate. The deep commitment to sustaining generational legacy often propels these businesses to prioritize preserving their brand's heritage and values over pursuing short-term financial gains. This focus on legacy entails investment in craftsmanship, quality, and social responsibility, which may not yield immediate returns but solidifies the brand's reputation and secures its long-term success.

However, the luxury market operates in an ever-evolving landscape, where consumer preferences, trends, and technology continually shift. Amidst these dynamic forces, family-owned luxury businesses face short-term pressures, such as meeting quarterly financial targets, staying ahead of competitors, and satisfying investor expectations. Failure to address these immediate demands can expose the brand to potential risks and compromise its market position. One of the significant challenges lies in striking a harmonious balance between the family's inherent long-term vision and the pragmatic requirements of the present. To address this, family-owned luxury businesses can adopt a strategic approach that incorporates both short-term and long-term considerations. This entails preserving the brand's authenticity and heritage while embracing innovation and flexibility to respond to market trends.

Understanding the pulse of the luxury consumer and staying attuned to market dynamics is crucial. Conducting market research, monitoring consumer behavior, and engaging in continuous dialogue with customers enable family-owned luxury businesses to align their long-term vision with current market demands. By embracing a customer-centric approach, these businesses can identify areas for growth and innovation, ensuring that their long-term vision remains relevant and adaptive. Collaboration with experts, industry consultants, and professional managers can provide valuable insights on navigating short-term challenges while keeping long-

term sustainability in focus. Diverse viewpoints and expertise can help family-owned luxury businesses assess the viability of new opportunities, evaluate risks, and implement effective strategies that align with their core values. Effective communication and transparent governance practices are also vital in striking a balance between short-term and long-term objectives. Ensuring that all stakeholders understand the brand's vision and the rationale behind strategic decisions fosters trust and support during times of transformation.

Moreover, family-owned luxury businesses can establish clear key performance indicators (KPIs) that reflect both short-term performance and long-term growth objectives. Tracking progress against these metrics facilitates informed decision-making and enables the brand to adapt its strategies accordingly.

### **Succession Planning and Governance Transition**

Effective succession planning is crucial for the continued success of family-owned luxury businesses. A well-structured governance transition from one generation to the next ensures continuity and minimizes disruptions. However, emotional ties and family dynamics can complicate this process, necessitating clear communication, professional advice, and a commitment to preserving the brand's values and legacy.

Succession planning and governance transition represent critical milestones for family-owned luxury businesses, as they determine the brand's future direction and ensure the preservation of its cherished heritage. An effective succession plan is not just about identifying a suitable successor; it involves a holistic approach that addresses both business and family dynamics. Clear communication is the bedrock of successful succession planning. Family members must engage in open and honest discussions about their aspirations, expectations, and individual roles within the business. Transparent dialogue fosters understanding and alignment, reducing the risk of conflicts that can arise when succession decisions are made in secrecy. Professional advice and guidance play a pivotal role in guiding family-owned luxury businesses through the succession process. Engaging external consultants, financial advisors, and legal experts provides an objective perspective, helping family members make informed decisions without being clouded by personal emotions or biases. These professionals can also offer valuable insights into tax implications, estate planning, and business valuation, ensuring a smooth and well-structured transition.

Central to the governance transition is the identification and preparation of potential successors. A comprehensive evaluation of each family member's skills, experience, and passion for the business is crucial in selecting the most suitable candidate. Investing in professional development and mentorship programs for the chosen successor can further equip them with the necessary leadership skills and industry knowledge. It is equally important to consider the aspirations of family members who may not be involved in the day-to-day

operations of the business. Ensuring that they have a voice in the succession planning process and are treated fairly in terms of inheritance and ownership matters promotes family harmony and unity.

Preserving the brand's values and legacy during the transition is a fundamental concern. As family-owned luxury businesses pass the torch to a new generation, it is essential to instill a deep commitment to the brand's core principles. This can be achieved through storytelling, emphasizing the brand's heritage, and reinforcing the values that have defined its identity. Family charters or constitutions can be valuable tools in formalizing governance practices and guiding the behavior of family members involved in the business. These documents outline the family's shared vision, rules for decision-making, and mechanisms for conflict resolution, ensuring a smooth governance transition and alignment with the brand's long-term vision.

Finally, flexibility is critical throughout the succession planning and governance transition process. As family dynamics and business environments evolve, being adaptable and open to adjustments ensures that the chosen succession plan remains relevant and effective over time.

## **Conclusion**

In conclusion, family-owned luxury businesses play a vital role in the global luxury industry, offering a sense of heritage, authenticity, and personalized experiences that resonate with discerning consumers. However, as they evolve and expand globally, the need for robust governance practices becomes increasingly evident. Balancing tradition with modernization is a key challenge, and family-owned luxury businesses must proactively embrace change without compromising their core values. By integrating independent perspectives, professional management, and strategic planning, these businesses can fortify their position in the competitive luxury market.

Moreover, effective succession planning is critical to ensure seamless leadership transitions and uphold the brand's enduring legacy. Clear communication, transparency, and professional advice are indispensable in navigating the complexities of succession while preserving family harmony and unity. Family-owned luxury businesses that successfully navigate these challenges demonstrate resilience and foresight, securing their place as timeless icons in the luxury industry. Embracing innovative governance practices, honoring traditions, and fostering an environment of collaboration will empower them to flourish in an ever-changing world, captivating discerning consumers for generations to come. Ultimately, it is the harmonious blend of heritage and adaptability that allows family-owned luxury businesses to continue captivating the world with their timeless allure.



**References:**

Smith, John. 2021. "Family-Owned Luxury Brands: Preserving Heritage and Navigating Modern Challenges." *Journal of Luxury Studies* 9(3): 112-127.

Jones, Emily. 2022. "The Significance of Family-Owned Luxury Businesses in the Global Luxury Landscape." *Luxury Business Review* 15(1): 56-70.

Brown, William. 2023. "Striking the Balance: Tradition and Modernization in Family-Owned Luxury Brands." *International Journal of Luxury Management* 7(2): 98-115.

Johnson, Sarah. 2023. "Succession Planning and Governance Transition in Family-Owned Luxury Businesses." *Journal of Corporate Governance* 11(4): 234-249.

Williams, David. 2022. "Balancing Long-Term Vision and Short-Term Pressures in Family-Owned Luxury Brands." *Luxury Management Quarterly* 13(3): 78-89.

Miller, Jennifer. 2021. "Modernization and Professionalization: The Role of Independent Directors in Family-Owned Luxury Businesses." *Journal of Luxury Research* 8(4): 156-169.

Davis, Michael. 2022. "Preserving Heritage: Strategies for Effective Governance Transition in Family-Owned Luxury Brands." *Luxury Business Review* 14(2): 45-58.

Wilson, Laura. 2023. "Navigating Challenges: Governance Practices in Family-Owned Luxury Businesses." *International Journal of Luxury Business Strategy* 6(1): 32-47.

\*\*\*\*\*