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Executive Summary of AUB Observatory – XIV edition
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Introduction

The AUB Observatory, promoted by AIDAF (Italian Association of Family Businesses), AIDAF-EY Chair in Family Business Strategy (Bocconi University), UniCredit, with the support of the Italian Stock Exchange, the Angelini Foundation and the Chamber of Commerce of Milan, Monza-Brianza and Lodi, **monitors all Italian companies that have exceeded the turnover threshold of 20 million euro.**

The content of the XIV edition of the AUB Observatory

The mail goal of the XIV edition of the AUB Observatory, entitled "**Diversity in the governance structures of Italian family businesses**" is to show a detailed analysis of governance structures in order to investigate the current level of diversity reached by family firms in their governance structures. Moreover, the XIV edition offers useful insights regarding:

- A comparison of the **governance structures**, also in terms of diversity, of the **top 1,000 family groups** in Italy, Germany, France and Spain;
- The evolution of the financial **performance** of family firms up to 2021 (and the first half of 2022 for listed companies), carrying on the comparison began with the XIII edition of the Observatory between the "Covid crisis" and the 2008-09 crisis;
- The review of the ownership structures of **listed** firms on the European markets controlled by Euronext and some first comparisons on governance structures;
- An analysis updated to 2021 on the evolution of the **governance structures of Italian listed companies**;
- The diffusion of the **buy-back** tool between 2013 and 2021.

We present in this executive summary the most significant results. More detailed results will be available from January, 31, 2023 in the analytical chapters of the XIV edition of the AUB Observatory at the following link: Presentazione XIV edizione Osservatorio AUB.

1. Presence and performance of Italian family firms

Diffusion

The XIV edition of the AUB Observatory confirms the great importance of **family businesses, representing 65% (equal to 11,635) of the total number of Italian companies**, without differences from the previous edition.

In order to avoid duplication of data, subsidiaries have been eliminated in the case of single-business groups and parent companies (often financial holding companies) in the case of multi-business groups. As a result, the AUB Observatory analyzes the structure and performance of **8,589 family groups**.

Revenue growth rate

In 2021, **family firms recorded a "rebound" in revenues of more than 20%**, higher than that of non-family businesses. The same trend was confirmed in the first half of 2022 (where data are available only for listed companies).

Marche, Lombardy and Liguria are among the regions with the highest revenue growth rate.

In term of sectors, **Metal Products, Rubber and Plastic, Chemical and Furniture** have the highest revenue growth rates. By contrast, sectors with the lowest growth rates include Fashion, Pharmaceutics and Mechanics.

Net profitability rate (ROE)

In 2021, **the net profitability of family firms exceeded the value of 2019** (ROE 2021 equal to 13.6% vs 13.0% in 20219). The same trend was confirmed in the first semester of 2022 where data is available only for **listed companies** (ROE 2022 of 8.3% vs ROE 2019 of 6.9%).

Geographically, **the performance of some large southern regions such as Calabria, Campania and Sicily are interesting**, confirming the ability of family firms in those regions to develop attractive business models.

From the industry perspective, **all sectors show an improvement in net profitability** except Paper and printing and Pharmaceutics (the latter, however, maintains double-digit performance). **Electronics, Means of transportation, Fashion and Furniture** show the highest rates in terms of net profitability.

Employment

The improvements in profitability are combined with increases in **employment**, which, for all family companies, **grew by 3.8% from 2019 to 2021**.

Financial strength

The average financial strength of all Italian family firms improved by more than 20% compared to 2019: the debt ratio (total assets/equity) fell from 5.0 to a value of 4.0. A similar improvement is seen in the NFP/EBITDA ratio, which decreased from 4.6 in 2019 to 4.0 in 2021. The percentage of family firms with negative NFP (cash and cash equivalents exceeding financial liabilities) improved by about 6 points compared to 2019, and the percentage of family companies with problematic financial situation decreased by 6 points from 30% to 24%.

The comparison with the situation at the end of 2011 shows an improvement even more noticeable: the percentage of family firms with a negative NFP improved by more than 10 points, and the percentage of family businesses with a problematic financial situation has decreased by 14 points from 38% to 24%.

The improvement in the financial strength of family firms is also confirmed by **listed companies in the first semester of 2022** where the debt ratio and NFP/EBITDA rates remain below those of the first semester of 2019 ("pre Covid").

2. Diversity in the governance structures of Italian family firms

The XIV edition of the AUB Observatory devotes specific attention to a very important topic for the future development of family firms: diversity on Boards of Directors (BoDs) in terms of:

- **Age**: at least 1 board member under 40 and no more than 1 member over 70;
- **Gender**: at least 33% of female board members;
- **Family membership**: at least 1 non-family member.

The topic is important because the results of the AUB Observatory **confirm a positive and statistically significant correlation between BoD diversity and performance of family firms** in terms of revenue growth, net profitability, EBITDA margin, debt ratio and NFP/EBITDA ratio, **and the strength of these relationships are of not marginal magnitude.**

In the face of this evidence, **Italian family firms still struggle to make a transition to more advanced governance models**. Among family firms with a BoD: [1]

- only 26.4% of companies have at least one board member under the age of 40 (ten years ago it was 46.6%, although the comparison should take into account the progressive aging of the Italian population as detected by ISTAT);
- only 37.6% of firms have a share of the least represented gender (women) above 33% (an improvement of only 3% compared to ten years ago);
- 60.1% of the firms have at least one non-family board member (ten years ago it was 54.3%).

In total, only **344 family firms out of a total of 8,589 family groups meet all of the diversity requirements outlined above**. Therefore, if the achievement of better results is related to a greater level of diversity and, at the same time, many family firms still show low levels of diversity, **it is needed the legislative push to accelerate the path with some reward mechanisms**. For this reason, it will be important to follow in the next months the law proposal developed by AIDAF.

Looking at the level of diversity by region, **Lazio** is the only region where family firms are above the national average for all indicators. The performance of large regions such as **Lombardy** and **Piedmont** are good. Instead, the level of diversity for Tuscany, Sicily, Sardinia and Liguria is lower.

Other services and Diversified Holding are the sectors with the highest degree of diversity. Among the manufacturing sectors, **Pharmaceutics, Chemical, Electronics and Rubber and Plastic** are well positioned on various indicators, while Paper and Printing, Fashion and Food and Beverage are below the national average for several indicators.

3. Diversity in the top 1,000 family groups by size in four European countries

The XIV edition of the AUB Observatory presents for the first time a comparative analysis of the **top 1,000 family groups in France, Germany, Italy and Spain**. Following the same approach as before, the analysis is focused on the level of diversity in governance bodies.

It should be noted that I**talian family groups are arrived to have a distribution by size similar to that of France**, even if a greater number of very large firms is present in France: while in Italy 2.7% of firms have revenues over 2.5 billion euro, in France this percentage rises to 5.2%. On the other side, in the following lower class (from 1 to 2.5 billion euro) Italian firms are 6.6% of the total, while French companies are 4.8%. **The German system is still far away**: groups with revenues in excess of 2.5 billion euro are 7.9%, and other 13.4% of firms have revenues between 1 and 2.5 billion euro. The Spanish system is characterized by smaller family firms.

On the issue of diversity in governance, the first result to be pointed out is **the still widespread presence in Italy of the Sole Director, equal to 12%,** while in France and Germany no family firms adopt this leadership model (also due to a different legislative system).

Then, if we focus only on family groups with Executive Boards and BoD, the Italian system shows many similarities to the French and German countries. In particular, looking at the percentage of firms with:

[1] About 28% of Italian family firms are managed by a Sole Director without the presence of a Board of Directors.

- **at least one director under the age of 40**: Italy reaches 28.4% compared to 26.6% in France and 15% in Germany;
- **at least 33% of female board members**: Italy reaches 34.9%, a percentage lower than that of France (40.9%), but well above that of Germany (15.7%);
- **at least one non-family member**: Italy reaches 78.3%, more o less the same as France (77.6%) and Germany (78.9%);
- **no more than one board member over 75**: Italy reaches 84.6%, while France is just above (90.1%). In Germany, however, almost all companies (99.7%) comply with this good governance requirement.

When all groups are considered, including those where there is a Sole Director, the governance standards of Italian companies are less comparable with those of France and Germany.

On the leadership side, the top 1,000 Italian groups are characterized by a **greater presence of family leaders (60.8%)** than France (54.8%) and Germany (46.0%). **The gender gap remains very high for all countries**: Italy has 21.7% of female leaders, a percentage higher than that of France (20.0%) and Germany (15.8%). As regards the age of the directors, **in Italy the presence of leaders over 70 remains very high (29% of the total),** while in Germany it is 19% and in France 10%. These differences are attenuated when the youngest member of joint leadership is considered, a widespread leadership model in Italy and, even more, in Germany.

Finally, if we consider the **leaders under the age of 40,** they are very few in Italy, France and Germany (a percentage between 8 and 9%). If we raise the threshold to less than **50** years, the young leaders become 33% in Italy, just below France (37%) and Germany (39%).

4. Companies listed on EURONEXT markets

IPOs and ownership structures

Since 2017, the number of firms – especially family firms - that went public throught the IPO listing procedure increased in Italy, and **2021 was the year with the highest number of IPOs in the past decade (50).**

From January 1, 2020, to the first half of 2022[2], family firms represented **90.8% of the total IPOs that took place on the Milan Stock Exchange** (equal to 77). This percentage is by far the highest one in the European markets controlled by Euronext.

It is due to family firms if the number of listed firms is increased in the last years. Indeed, family confirm a certain dynamism in the process of opening the share capital, even if they took place on the AIM market in most cases, mobilizing limited financial resources.

Extending the analysis to all 1,992 companies listed on the European markets controlled by Euronext, it can be seen that the Milan Stock Exchange is the second largest Euronext market in terms of number of listed companies (422), and it is **the highest one for incidence of family-controlled companies** (74.9%)[3]. In addition, Italy is the stock market (together with France) where **family owners hold the highest controlling share in the ownership** (about 60%).

Economic and financial performance

Family firms listed on the Milan Stock Exchange performed better, especially in 2021, than other family firms listed on Euronext markets. In terms of growth, they recorded **in 2021 a "rebound" in revenues of 27.3%**, higher than both family firms on other Euronext markets (+21.1%) and Italian non-family firms (+23.5%). In terms of **net profitability, family firms on the Milan Stock Exchange**

[2] IPO registration from 1 January 2020 to 30 June 2022.

[3] Family-controlled companies were defined as companies controlled by one (or two) owning families with a share of more than 25%.

performed better than 2019 (ROE 2021 of 9.1% vs 7.3% in 2019), exceeding the profitability of both Italian non-family firms (6.9%) and other Euronext family firms (4.5%).

Family firms listed on the Milan Stock Exchange are also proving to be more solid than in 2019. The leverage ratio decreased further in 2021 (down to 3.7 from 3.9 in 2019), in line with what happened in the other family firms listed on the Euronext markets (down from 3.0 in 2019 to 2.8 in 2021). The improvement in capital strength is also confirmed by the analysis of the NFP/EBITDA ratio. After the peak reached in 2020 (mainly due to the decline in profitability), **the NFP/EBITDA ratio returned to lower levels in 2021 than pre-covid ones** for Italian family firms (down from 3.1 in 2019 to 2.9 in 2021). The NFP/EBITDA of European family firms decreased by more than 20% compared to 2020 (from 5.7 to 4.4).

<u>The governance structures of listed family firms</u>

The XIV edition of the AUB Observatory presents also for the first time a comparative analysis of some governance indicators for family firms listed on Euronext markets (in order, Amsterdam, Brussels, Dublin, Lisbon, Milan, Oslo and Paris). The analysis focused on the following indicators:

- **Family leadership:** family firms in Milan have about 44% of CEOs belonging to the controlling family. Only French country shows a greater presence of family leaders (55.6%). All other markets record greater openness towards non-family leadership;
- **a family Chairman:** in more than 3 out of 4 Italian companies (77.4%), the Chairman is a family member; this percentage is higher of at least 10-20 points than those of family firms listed on other Euronext markets;
- **the presence of family in the board:** family firms listed on the Milan Stock Exchange have, on average, 22% of family directors on the board. It is a lower value if compared to that of listed firms in Portugal (27.8%) and France (29.6%). The greater openness to non-family members of Italian family firms is confirmed by observing the percentage of companies with the majority of non-family members (93.3%, compared to 75.8% in Portugal and 78.8% in France);
- **the presence of women directors on the board:** Italian family firms with at least 33% of women directors are 52.5%. Only French family firms show a higher percentage (58.1%);
- **the presence of "young" directors on the board:** 35.0% of companies listed on the Milan Stock Exchange show at least one director under 40 in BoD, a percentage in line with that of France (33.3%).

An overall reading of these indicators shows that the governance standards of Italian family firms are comparable with those of other Euronext markets. **Compared to France** (the first market by number of listed firms), **the Milan Stock Exchange is characterized by a lower level of "familiness" in both BoD and leadership.** Compared to other listed markets, Italian family firms show a good openness of the BoD towards both the female gender and "young" people.

5. Governance structures of Italian listed companies

The XIV edition of the AUB Observatory also devotes a specific in-depth study on the governance structures of listed companies in Italy. We analyzed the "corporate governance report" of 445 companies listed in at least one of the years from 2014 to 2021, monitoring the evolution of some corporate governance indicators. The main evidences that emerged are reported below.

<u>Biographical data of the Board of Directors, President and CEO</u>:

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- **Family control reduces board size:** in 2021 family firms have about 20% fewer board members than non-family firms;
- **Family firms have a Board of Directors that remain in office for a greater number of years** (in 35% of cases for more than 6 years, against 11% in non-family firms);
- **The seniority of the Chairman and CEO in family firms is higher,** respectively, than 64% and 29% in comparison to non-family firms (10.7 years vs. 6.5 in the case of Chairman, and 8.9 vs. 6.9 for the CEO);
- **Family control does not influence the average age of the Chairman (which is particularly high):** 1 Chairman out of 4 is over 70, with no particular differences between family and non-family firms;
- **Family firms have younger leaders:** CEOs of family firms under 50 are 27% (5 points higher than that of non-family firms);
- **Family firms show a more pronounced gender gap to be filled:** 56.9% meet the 33% threshold of female board members, a data significantly lower than that of non-family firms (75.7%).

Data on executive, family and independent directors:

- **Family firms have a higher incidence of executive directors** (29% vs 20% in 2021), and nearly twice the percentage of firms with an executive Chairman (71.0% vs 38.0%), although the data shows a decline in recent years (-11% in eight years);
- **The LID (Lead Independent Director) is more prevalent in family firms** (34.0% vs 15.0%), partly due to the large number of family Chairman (about two-thirds);
- Family firms have a **higher incidence of board members with 2 or more (other) job positions** (48% vs 41%) and 3 or more (34% vs 28%) than non-family firms;
- **The percentage of independent directors is about 18 points lower** in family firms (37.4% vs 55.9%);
- **Lower representation of minority directors:** the incidence of firms with at least one director appointed by minority shareholders increased from 40% in 2014 to 45% in 2021, but a huge gap remains compared to non-family firms (58.9%);
- Both the **incidence of family leaders** (equal to 43%) **and family directors** (equal to 24 %) **is stable over the period 2014-2021.**

The last insight was devoted to the profile of CEOs. Two main features were analyzed:

- **Education:** CEOs of family firms have, on average, a lower level of education: 82.2% show a bachelor's degree vs 94.5% of non-family firms' CEOs;
- **International experience:** CEOs with work and/or study abroad experience are fewer in family firms (15.9% vs 24.6% in non-family firms), and with a shorter experience (2.6 vs 6.7 years).

From the summary picture outlined above, three main areas of improvement seem to emerge (and the family firms should work on them to improve their governance structures): i) openness to independent directors; ii) board representation of minority shareholders; iii) board representation of the female gender.

6. The share buyback in Italian family firms

The XIV edition of the AUB Observatory devotes an in-depth study to ownership structures, analyzing **the diffusion of share buyback transactions.** Starting from the whole Italian population

of companies with turnover over 20 million euro[4], we analyzed the shareholdings of 9,871 groups in the years from 2013 to 2021. The results indicate that share buyback transactions have grown over the period under consideration, especially in family firms: **in less than 10 years, the percentage of family firms that have purchased treasury shares has almost doubled, from 8.7% in 2013 to 15.8% in 2021.** And the amount of treasury shares has also grown by about 3 points (from 8.1% to 11.0%). An increase of similar proportions also occurred in non-family firms, even if their diffusion is lower (the percentage of non-family firms with treasury shares increased from 5.2% to 10.3% in the same period).
The AUB Observatory also tried to investigate some possible drivers behind share buybacks, and the results show that the phenomenon is greater in:

- **Companies with more concentrated ownership,** whereas the first shareholder (not necessarily a family member) holds more than 50% of shares;
- **Large companies:** the incidence of firms with treasury shares grows with the company size;
- **Longest-running companies**, probably due to a more fragmented ownership structure over the generations.

By contrast, no differences emerged between the incidence of firms that purchased their own shares and: i) the firms' NFP; ii) the business sector and the CAGR of the sector's revenues; iii) the geographical area of the firm. Therefore, it can be concluded that the use of the "buyback" instrument does not seem to be related to either cash availability (measured in terms of negative NFP) or lower growth perspectives of the industry (measured in terms of revenue CAGR).

The results allow us to conclude one of the goals of such an instrument (perhaps the main one) is **to allow (and enhance) the exit of one or more shareholders from the company shareholding,** facilitating phenomena of ownership reconfiguration.

[4] Subsidiaries in the case of monobusiness groups and parent companies (often financial holding companies) in the case of multibusiness groups, as well as branches of foreign companies (with a non-Italian head office) were eliminated. As a result, the number of companies analysed fell from 17,901 to 9,871.