Family Values

As we edge past the ten-year mark into the current bull market, some investors are understandably asking questions about how their equity investments might fare whenever the next downturn hits. At Guardian, we spend plenty of time thinking about the same thing. One factor working in our favour is the prevalence of family-owned businesses populating our client portfolios, both within Canada and internationally. There is a robust, intuitive rationale for tilting towards these owner-operator businesses. When led by teams with a strong sense of attachment, and a greater purpose that comes with being part of a founding family, the odds improve that executives will steer the business in a prudent, thoughtful method. With a sense of genuinely long-term vision, these companies are more likely to make the investments required today that will allow the company to thrive years into the future, as well as conservatively fund them that avoids placing the business at undue risk. These are companies well positioned to withstand economic slowdowns and thrive as conditions improve afterward.

To be sure, there is a counter-argument that these family-run businesses are at higher corporate governance risk: neglecting minority shareholders, running the business purely for current cash flow, or failing to recognize competitive threats. However, in a collective sense, the evidence is to the contrary. Recent research out of Credit Suisse highlights that family-owned companies have outperformed the broader global universe of stocks by 3.4% annually since 2006. As a group, these companies are of higher quality, with greater profitability, better balance sheets and superior growth, by virtue of investing greater amounts into asset growth and new product development.

Versus Global Universe	Profit Margins	Financial Leverage	Return On Capital	R&D As % Of Revenues	Annual Stock Returns
Family Owned Companies	+1.5%	-22.0%	+1.7%	+1.3%	+3.4%

Source: Credit Suisse, "The CS Family 1000", September 2018

Delving deeper, in North America, the top 25 family-owned companies beat the broader market by an even more impressive 9.0% annually over the past decade, reflective of a 1.0% annual revenue growth advantage and a 0.9% lead in return on capital. Within this select group are some longstanding holdings within Guardian client accounts, such as Saputo, NIKE and Rogers Communications, all businesses with highly invested family oversight that affords a long-term perspective in corporate planning. Lino Saputo Jr. might be the current CEO of the company his grandfather started, but he has a hands-on experience that began with mopping the shop floor and working on the production line in his youth. Over the years, his rapport with dairy farmers has been a folksy touch, helping secure several acquisitions in the United Kingdom, the United States and Australia that have propelled Saputo to quietly become a global dairy leader with the majority of profits coming from international markets. Conditions in the dairy industry are tough, with oversupply pushing prices lower across North America, but we sleep better at night knowing that great managers like Lino Jr. are working overtime to ensure Saputo prospers regardless of the environment.

This view extends to other family-led businesses common to Guardian clients, such as Larry Ellison positioning Oracle for long-term growth in software, or Johann Rupert taking action to protect and grow Cartier's prestigious reputation as "The Jeweller of Kings" at Compagnie Financiere Richemont. Owner-operators like this are more likely to enact significant changes when required to ensure sustainable growth in the long term, ultimately supporting profit growth and dividend gains for investors. As the post-Financial Crisis period enters its eleventh year in duration, our bias towards owner-operator companies should add comfort to clients wondering about the timing and impact of the next slowdown. When looking for attributes of high-quality, sustainable long-term growth, and superior stock market performance, it's hard to beat family values.