Re-Awaken Your Inner Capitalist

The sale of a family business marks a time of celebration, the beginning of an exciting new chapter. Finally, after years, if not decades, of diligent focus, hard work, and delayed gratification, the entrepreneur enjoys a well-earned liquidity event.

For many families, this moment also marks the transition from '*Operating Family*' to '*Financial Family*' as they shed their operating assets and shift their focus from building businesses and satisfying customers to constructing and managing investment portfolios. At this point, a new universe opens, featuring the capital markets, risk analysis, behavioral finance, family office structure, advisor and manager selection, and other compelling topics. This is often the time when capital preservation and stewardship become conscious priorities.

Who could possibly argue with the concepts of capital preservation and stewardship? And why would anyone assert that a family shouldn't simply relax and enjoy a well-deserved break from the rigors of business building?

Well, that's precisely the purpose of this brief article…

The Trouble with Stewardship:

Capital preservation and stewardship are laudable objectives. *Of course* you want to protect the hard-earned proceeds from the sale of your business. Why should you be any less thoughtful about your portfolios than you were with your business? You must invest well, seek solid advice, diversify with prudence, make more good decisions than bad, and generally do your best to ensure there is plenty left over for future generations, right?

Well… yes, but some folks take this too far. Just as chronic over-exposure to essential vitamins can lead to increased risk of cancer, excessive focus on capital preservation can incubate serious problems down the road, problems that accentuate conflict and accelerate the decline that eventually fulfills the '*shirtsleeves to shirtsleeves*' prophesy.

In the context of this article, the term '*Stewardship*' refers to a particular feeling of obligation that family members often experience, an obligation to protect the family's wealth, losing and spending as little as possible, in order to preserve purchasing power for future generations. At some level, '*Stewards*' do not consider themselves *owners* of the wealth; rather they believe they are simply *responsible* for it during their time on the planet. They'll take a sip off the top now and then, but their main objective is to pass along the balance to future generations.

This is a fine sentiment, one with which I enthusiastically resonate. For years, I advocated the notion of stewardship with my clients and staff without reservation. However, after witnessing surprising negative consequences with some families, I have become convinced that unchecked stewardship can inflict unintended damage.

Some family members take the commitment to stewardship so seriously that their worldview begins to shrink inward. They become '*professional clients*', behaving as if their primary mission in life is to protect the principal. This leads them eventually to look at the world through a lens of *scarcity*.

I have actually encountered parents with tens, even hundreds of millions of dollars in the bank, who express fear that their children won't have enough money. And I have known adult children of equally wealthy parents who are vaguely anxious that there will be nothing left for them in the end. Left unchecked, this often-unconscious concern can permeate the family, injecting bitter and acrimonious dynamics into all aspects of life, imposing a prison with velvet bars that poisons each subsequent generation.

The effects of '*Hyper-Stewardship*' may not become apparent for some time; Mr. and Ms. G1, first-generation founders the business, will likely never display the symptoms. And depending upon their involvement with the family's business, the members of G2 might not either. But once a family's operating assets become a distant memory, these negative dynamics can quietly creep into the picture and erode the family's ability to enjoy and sustain their wealth.

The trouble is… over the long term, it is nearly impossible for investment portfolio returns to overcome the corrosive effects of family population growth, increased individual consumption, investment mistakes, and taxes.

Without periodic injections of '*New Capital*', long-term dissolution is inevitable. It's a slow glide path down, and it may take several generations, but family members feel and begin reacting to the threat long before the reality settles in.

Inoculate Your Family with Entrepreneurship.

In sharp contrast to the stewards described above, entrepreneurs, assuming their ventures are moving even remotely in the right direction, tend to view the world through a lens of *abundance*.

We've all encountered people who are flat broke, even in debt, who feel rich as can be. Why is that? How can a person whose only asset is a dream feel wealthier than a family member with ten or even hundreds of millions of dollars in the bank? More important, perhaps, how can *your* family recapture some of that feeling of abundance?

The entrepreneur's perspective focuses outward. He or she thinks about growth, satisfying customers, developing talent, planting seeds for the future. Somehow, in pursuit of external priorities and dreams, their worlds expand, and entrepreneurs find a way to move forward, secure in the unconscious certainty that growth *will* come.

Of course, we're painting a rosy picture here. It would be irresponsible to assert that the act of entrepreneurship can solve a family's problems or by itself snap their worldview into a positive perspective. However, over time, appropriate and well-placed injections of business building *can* help the family combat the negative spiral of a scarcity mindset by bringing fresh assets into the portfolio, shifting the family's focus outward, and illuminating a possible path to long-term sustainability.

In my opinion, every generation should have at least one entrepreneurial experience. This means someone in each generation should launch, run, or at least rigorously participate in operating businesses that can create *new* wealth for the family, wealth that goes beyond portfolio returns.

What Does it Mean to be a Capitalist?

The title of this article refers to '*Reawakening Your Inner Capitalist*'. What does that mean? Aren't stewards capitalists too?

Well, technically speaking, I suppose *every* investor is a capitalist. Any person who risks capital with the expectation of positive returns probably qualifies at some level, but not in my book.

In contrast to a '*Steward'* who adopts a defensive and largely passive approach based upon diversified investment portfolio returns, our '*Capitalist'* concentrates the power of his or her assets – *money, time, sweat, and/or relationships* – to create *new* assets, to expand their family's portfolio with value that simply didn't exist before.

Our definition also draws a distinction between '*Capitalist*' and '*Entrepreneur*'. Entrepreneurs risk time, talent, and relationships – *and often other people's money* – to build businesses. Capitalists risk these assets too, of course*, but they commit their own money as well*. Thus, according to our definition, all capitalists are entrepreneurs, but not all entrepreneurs are capitalists.

This may feel like splitting hairs, but these distinctions are important because they contribute to a distinct worldview that leads to specific behavior over time. Families of wealth are uniquely qualified to act as capitalists, and I assert that over the long term, many would be better off if they did.

Carefully Nurture Your Inner Capitalist…

Let's get something straight. I am not suggesting that you should abandon the philosophy of stewardship; quite the contrary, in fact. Stewardship and capital preservation are essential, the stars of the show. You owe it to yourself and to your family to maintain a prudent, well managed and diversified approach that will preserve spending power for future generations. However, this doesn't mean your approach should be purely defensive.

You can and should be a steward and a capitalist at the same time.

In fact, if you have multigenerational aspirations, that is the only prudent approach.

The key is to carefully inject a small element of entrepreneurship into your affairs and then develop it carefully over time. *Don't fall into the Financial Family Trap*. Gingerly bring operating assets back into the fold, and keep the spark of business alive in order to avoid the poison of hyper-stewardship.

Despite its numerous long-term benefits, capitalism is a most dangerous game, so I recommend that you follow a few defensive guidelines:

1. ***Start Small*** – *Do not leap back into a scenario where major, illiquid operating assets dominate your asset base*. Carve out a tiny initial allocation to direct investments in operating business and real estate. Over time, you may decide to make a more major commitment, but it would be absurd to take big risks early on.

2. ***Take Your Time*** – *Do not rush this process*. You have multiple generations to get this right, so do your homework thoughtfully and make sure you have the resources required to tilt the probability of success in your favor. It would not be unreasonable for the initial search/incubation period to take years.

3. ***Seek Solid Advice*** – *Do not try to do this on your own*. Expert advisors exist along all dimensions of the entrepreneurial challenge. Make prudent use of them, but don't let their fees get out of control.

4. ***Be Extremely Selective*** – *Do not buy into the first business or business plan that comes your way.* It is far better to miss out on a few good opportunities than it is to invest in a stinker. Sourcing operating assets requires careful planning, hard work, disciplined focus, and a ruthless ability to say no. You will likely make thousands of phone calls and kiss dozens of frogs, but in the end, it's worth the extra effort.

5. ***Establish a Culture of Capitalism*** – *Do not encourage a passive mindset in your family*. At the very least, make sure everybody works. No one should depend entirely upon portfolio returns over the long term. Family members should support themselves and contribute to the pool whenever possible. Help your children and future generations recognize that they have the power to expand their portfolios, to live their lives from a perspective of *abundance* not *scarcity*.

6. ***Teach Them to Fish From an Early Age*** – *Do not expect your children to learn how to become entrepreneurs on their own*. Over time, your family's '*Human Capital*' will prove more valuable than its '*Financial Capital*'; invest yourself accordingly. As with stewardship, a capitalist mindset requires extensive training and is best nurtured from an early age.

7. ***Never Give Up the Ghost*** – *Do not fall into the seductive trap of the Financial Family*.

The sale of a family's operating business marks the beginning of an exciting and well-deserved new chapter. But it need not mark the end of an era. Capitalism and concerted entrepreneurship likely built the foundation upon which your family's success stands today. By all means, preserve your capital for future generations, but keep your inner capitalist alive and well. Your children, their children, and generations yet unborn will thank you for the gift of abundance.