EMERGING MARKET SUPERCLANS.

MODELS AND OPPORTUNITIES IN CRISIS FOR ROMANIA'S TOP BUSINESS FAMILIES

THIS REPORT IS SUPPORTED BY BANCA TRANSILVANIA

This project was completed with the kind support of Banca Transilvania.

CONTENTS

TRENDS IN GLOBAL WEALTH

A look at global trends in wealth both at the level of the population in general as well as high-net worth individuals, followed by a regional breakdown of current trends

- OVERVIEW
- GROWTH
- REGIONAL PERSPECTIVE

OVERVIEW

The past 3 years have been dominated by the impact of SARS-CoV-2, whether at the level of the global economy or the level of households' accumulated wealth. Nevertheless, for all of its human cost, the pandemic has hardly put a dent in macro trends evidenced over the past few decades in terms of what may be called the upper tenth of wealth holders and income earners.

Instead, if anything, the events of the previous few years have accelerated those long-running trends to paint an ever clearer picture of the future. North America's total wealth actually increased by over USD 12 trillion while Europe saw an increase of over USD 9 trillion. The same pattern holds for most of the world, with the exception of India and Latin America. This could be hardly regarded as exceptional, despite the exceptional circumstances, as the pattern has held for most of the past 30 years.

12.4

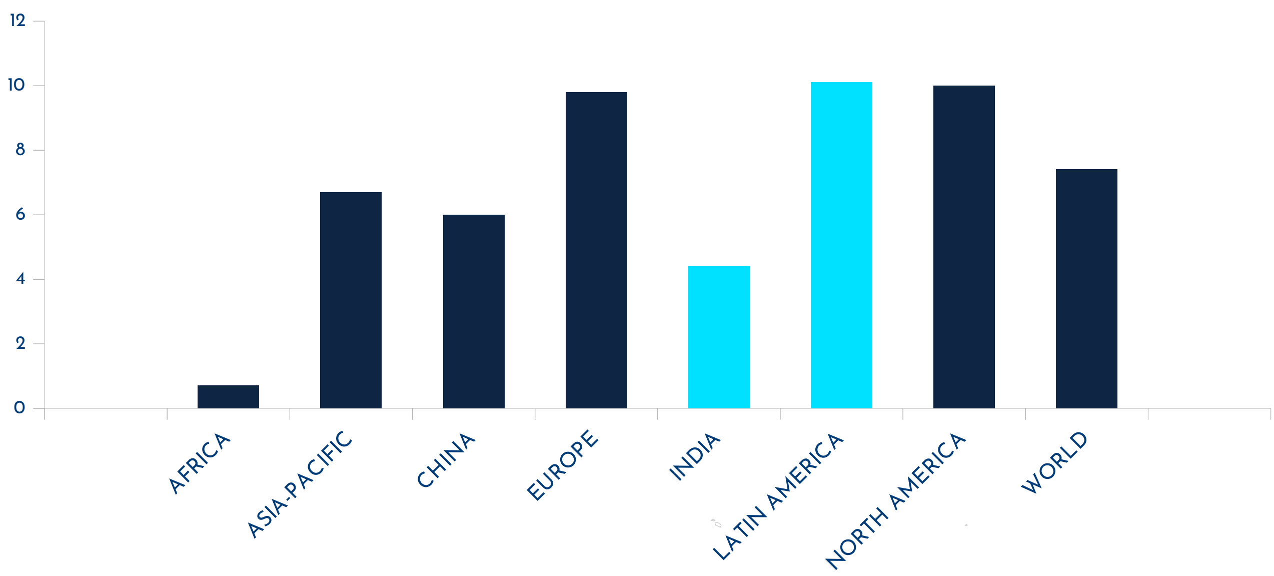
TRILLION USD INCREASE IN TOTAL WEALTH IN 2020 IN NORTH AMERICA

WORLD BANK

9.2

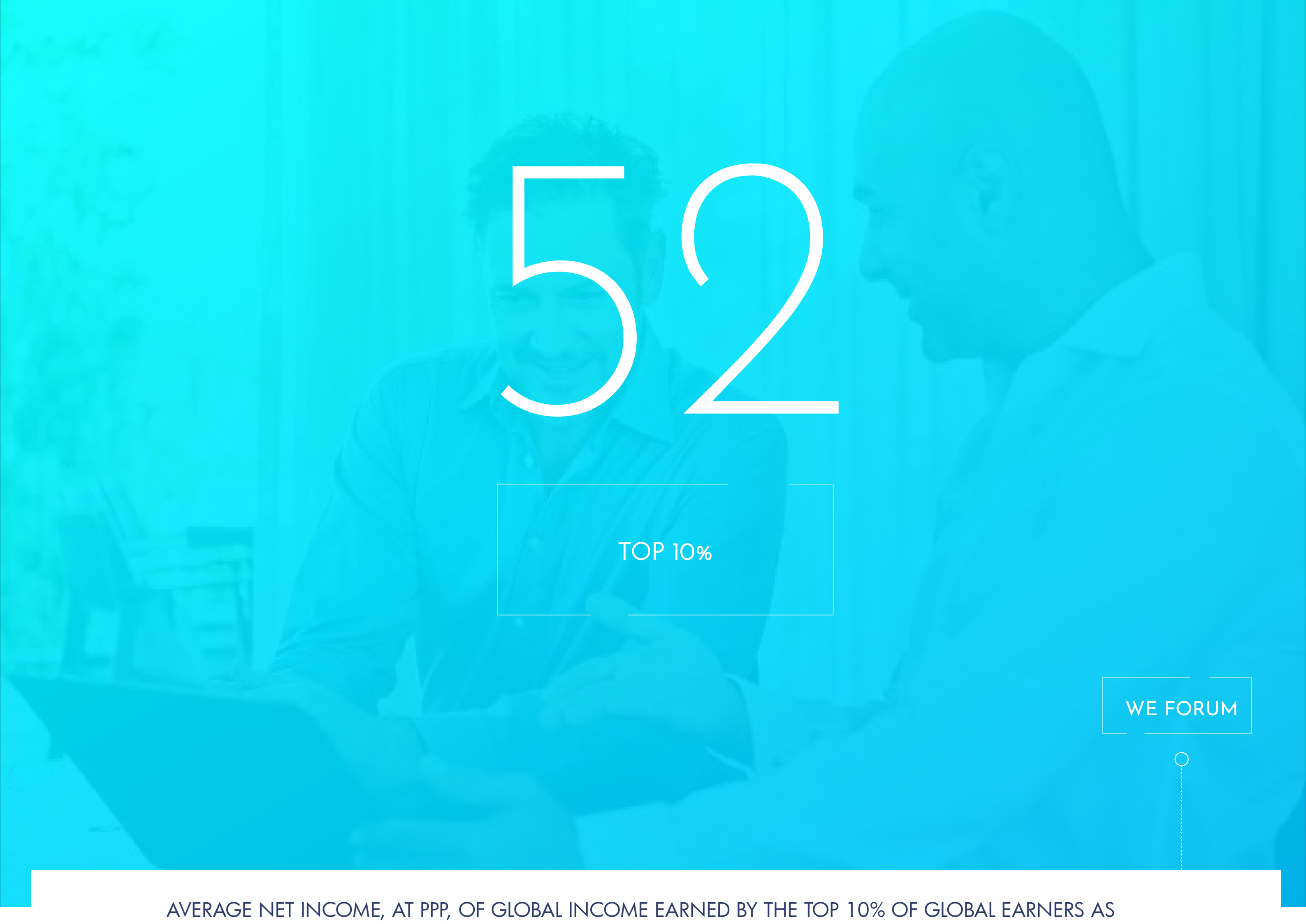
TRILLION USD INCREASE IN TOTAL WEALTH IN 2020 IN EUROPE

WORLD BANK



CHANGE IN HOUSEHOLD WEALTH IN 2020. BLUE INDICATES GROWTH, LIGHT BLUE INDICATES A DECREASE. ALL FIGURES GIVES ARE PERCENTAGES.

WORLD BANK



52

TOP 10%

WE FORUM

AVERAGE NET INCOME, AT PPP, OF GLOBAL INCOME EARNED BY THE TOP 10% OF GLOBAL EARNERS AS OPPOSED TO THE BOTTOM 50%

8

BOTTOM 50%

That pattern is four-fold.

First, we have seen a general increase in wealth globally. While this has accumulated to the top, it has nevertheless been general in scope and it may be summarised by the fact that just since 1990, during what is called the Third Wave of Globalization, global GDP has increased by over 100%. Second, wealth based on income has increased. This does not match wealth derived from capital ownership, nor is it likely to ever do so, but it represents a significant shift whereby the top 10% may be regarded, or at least regards itself, as far more meritorious than in the past. Third, wealth has become far more globalised than ever before in modern human history, with wealth having become a truly global phenomenon. Fourth, wealth in relative terms is increasingly the preserve of a specific strata of society, a pattern which is surprisingly uniform across different economies.

71

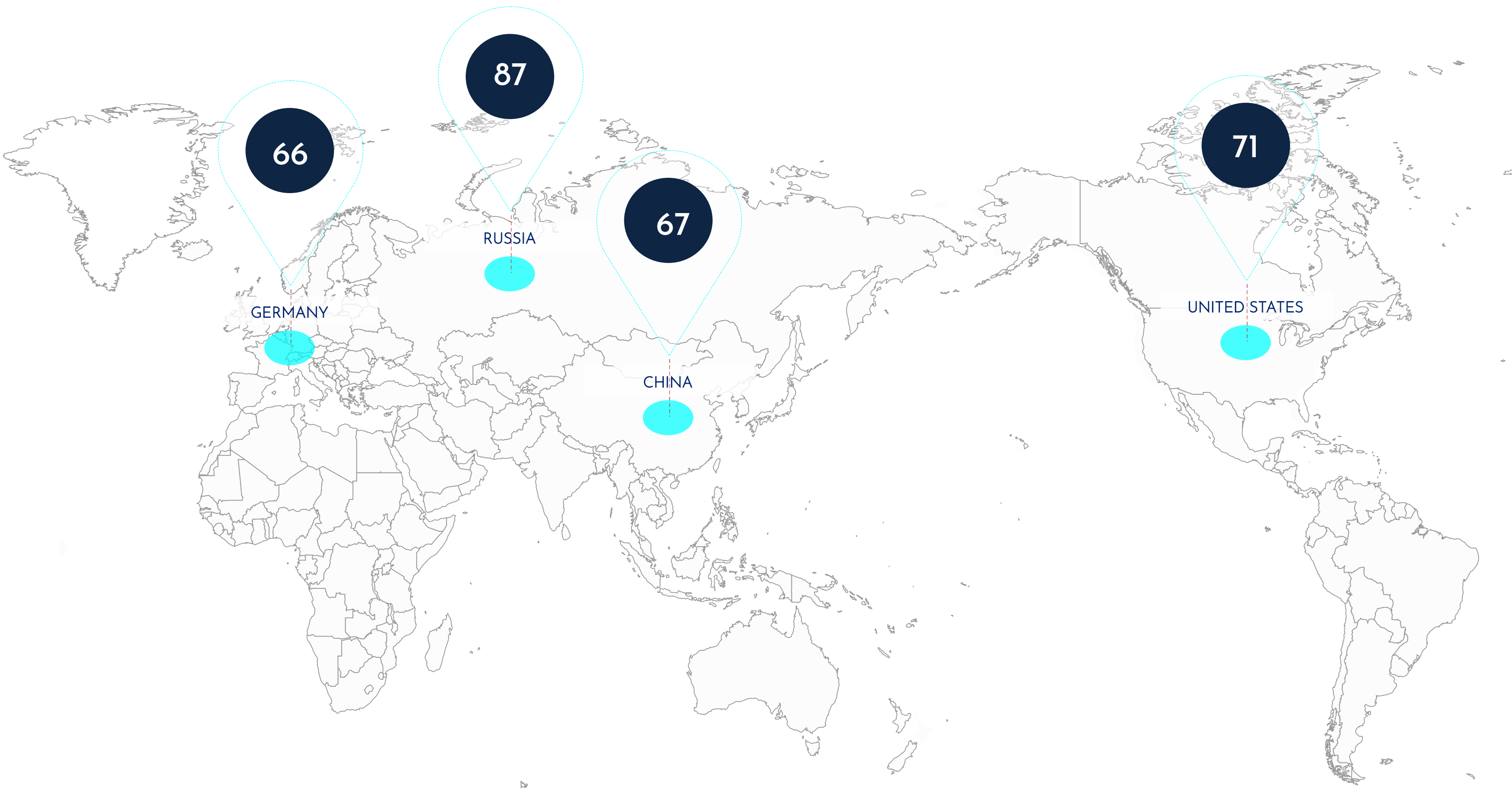
PERCENTAGE OF NATIONAL NET WEALTH HELD BY THE TOP10% OF HOUSEHOLDS, IN 2019, IN THE US

MCKINSEY

67

PERCENTAGE OF NATIONAL NET WEALTH HELD BY THE TOP10% OF HOUSEHOLDS, IN 2019, IN CHINA

MCKINSEY



PERCENTAGE OF NET NATIONAL WEALTH HELD BY THE TOP 10%

WORLD BANK

GROWTH

Perhaps the most important, and often overlooked, trend in global wealth is the simple increase in wealth. This is not necessarily a matter which actually makes headlines as often as negatives but sometimes the good news needs to be mentioned.

The majority of people are, on average, a lot richer than before. This genuine boom in GDP per capita may be seen as the result of the internationalization of the Second and Third Industrial Revolutions, better governance and, not least, the Second and Third Waves of Globalization. It has determined wealth both on the top as well as more generally across society.

This has had two overall effects : it has made a lot of households significantly better off, and a few tremendously rich such that we may now speak of emerging markets as dominating the leagues of the world's most well-heeled.

21

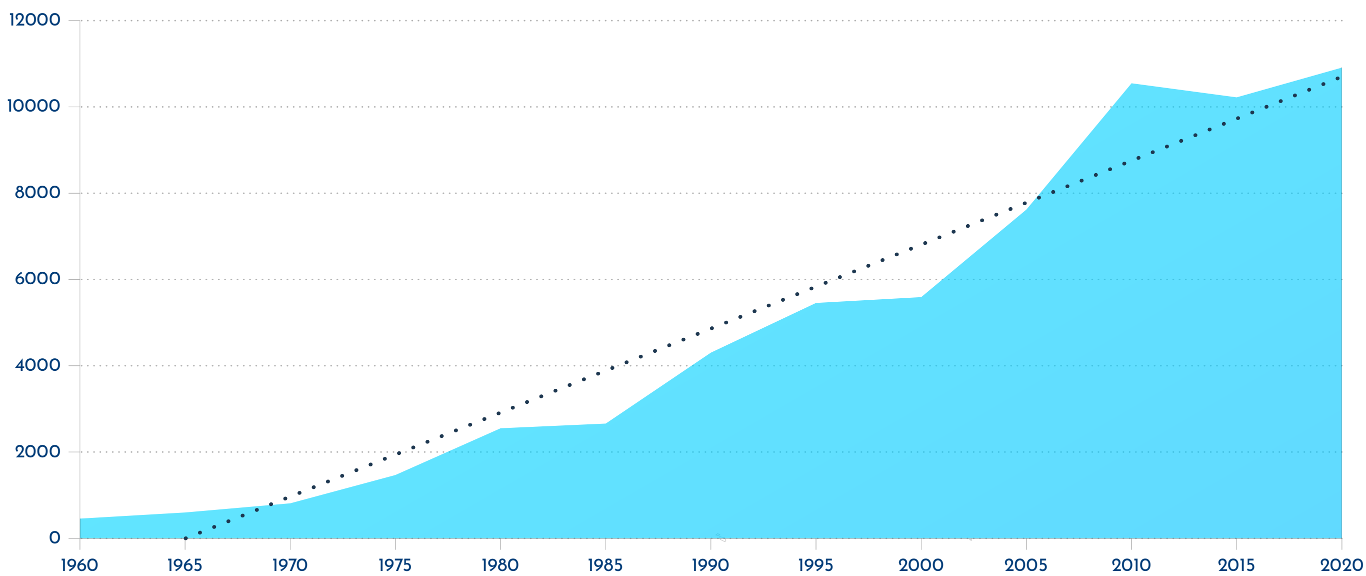
TIMES GDP PER CAPITA INCREASED IN CHINA SINCE 1978

WORLD BANK

232

TIMES RETAIL SALES HAVE INCREASED IN CHINA SINCE 1978

IMF



AVERAGE GDP PER CAPITA ACROSS THE WORLD, IN CONSTANT 2015 USD

WORLD BANK


100
PERCENTAGE INCREASE IN GLOBAL GDP SINCE 1990
WORLD TRADE ORGANIZATION

The first of these effects has the most important humanitarian effect and there is every reason to celebrate it.

However, the second is equally, if not more so, important by what it indicates about the future. It announced the arrival of a new class of businesspeople, entrepreneurs and humanitarians as well as new approaches to business that may be seen as distinct. Social and cultural differences aside, the wave of growth which the past 30 years alone have generated has not only given rise to a new global middle class but also a vast redistribution of relative wealth towards emerging markets. That needs to be understood in its statistical context, beyond headlines. While the underlying theme has been of emerging markets generally, the primary trend has been the convergence of China with the rest of North East Asia, and the tidal wave of commodities demand that it generated.

10

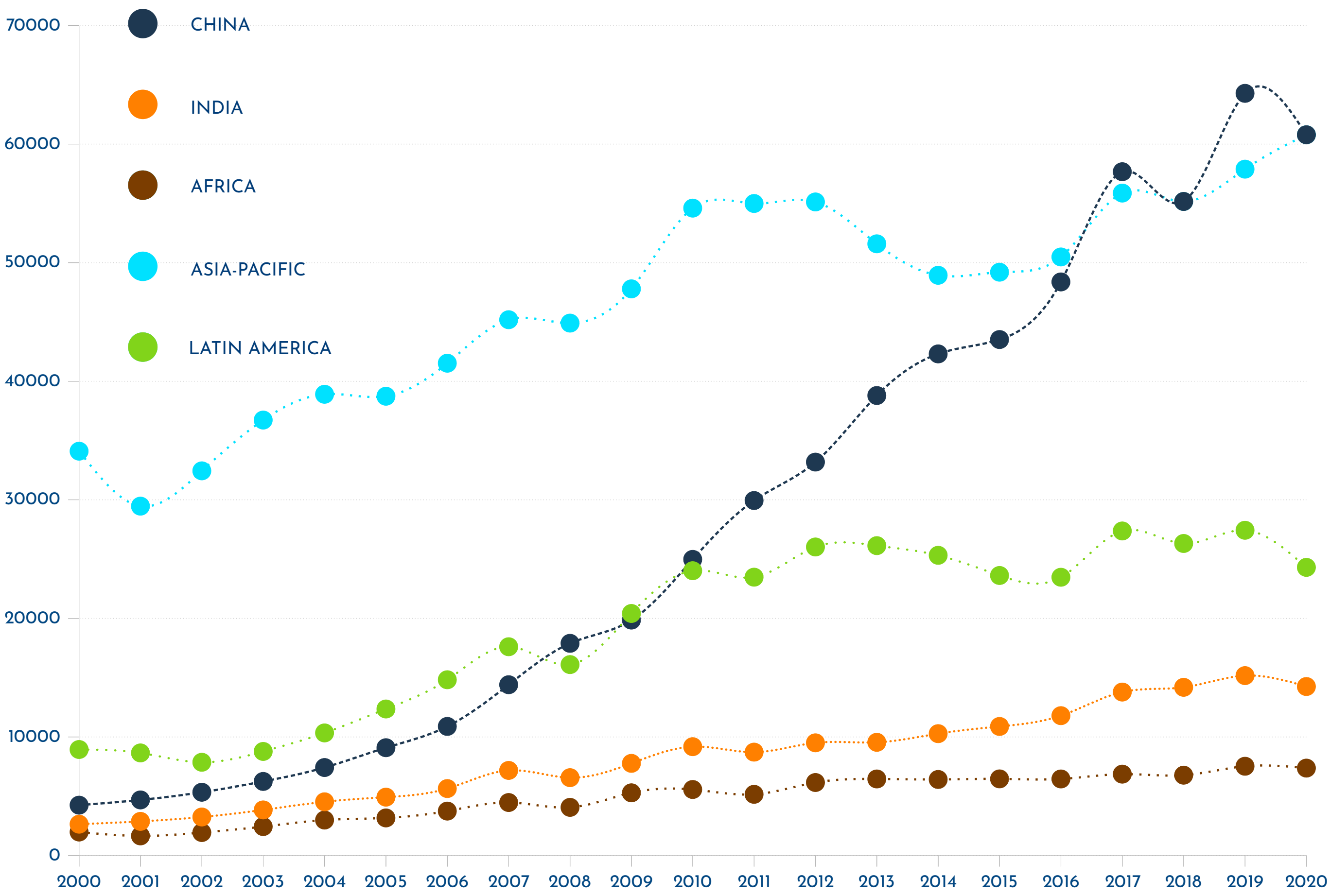
PERCENTAGE OF THE WORLD POPULATION WHICH LIVED ON LESS THAN USD 1.9 PER DAY IN 2015

WORLD BANK

36

PERCENTAGE OF THE WORLD POPULATION WHICH LIVED ON LESS THAN USD 1.9 PER DAY IN 1990

WORLD BANK



AVERAGE WEALTH PER ADULT, SELECTED CONTINENTS, USD 2016 CONSTANT

CREDIT SUISSE

3.35

CHINA

IEA

ELECTRIC VEHICLES REGISTERED IN TOTAL UP UNTIL 2019, INCLUDING HYBRID VEHICLES. FIGURES FOR EUROPE INCLUDE ALL EU-27 COUNTRIES. FIGURES ARE IN HUNDRED THOUSANDS.

1.75

EU-27

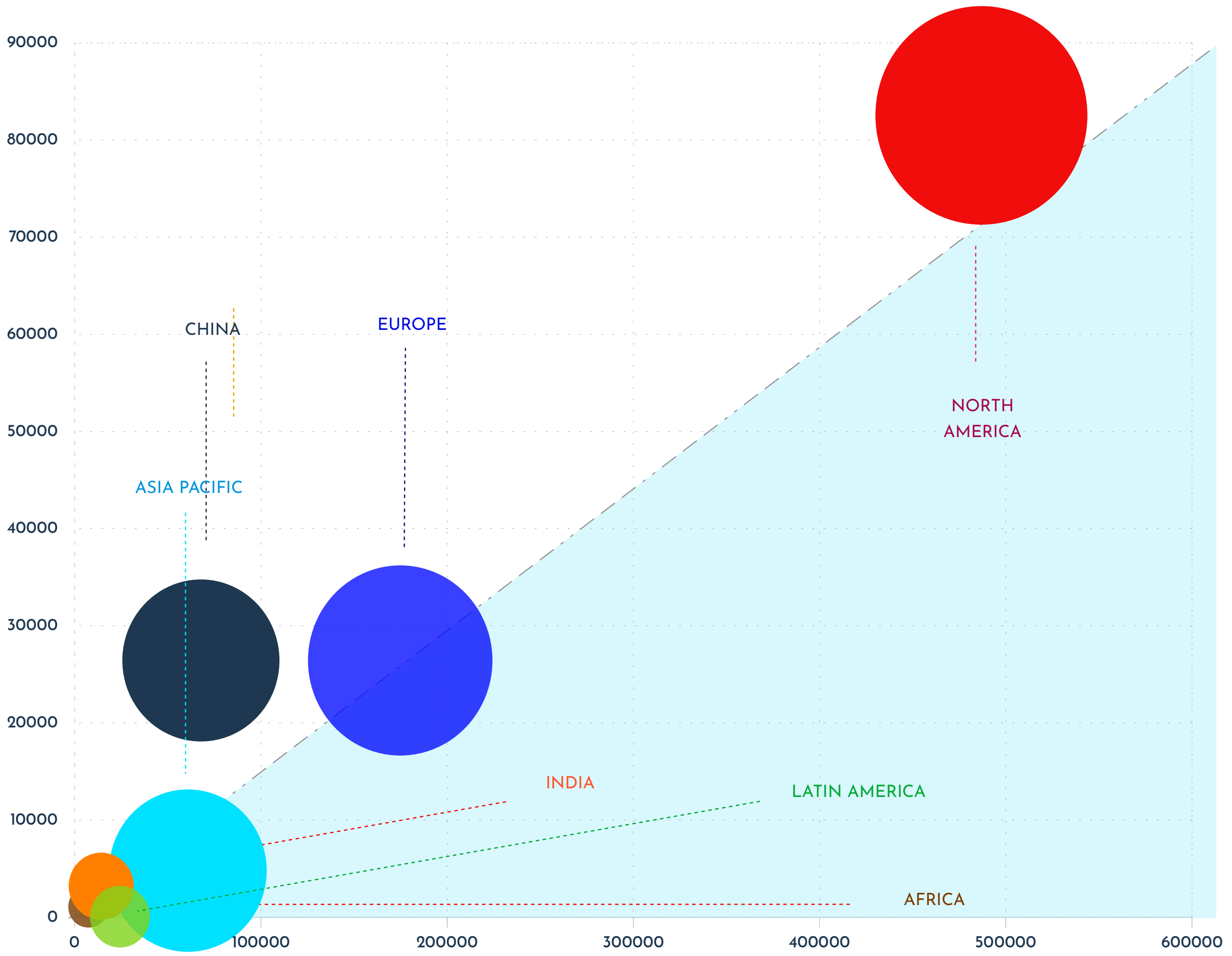
In absolute terms, a significant part of the wealth generated over the past 30 years, while unprecedented in human history, can be attributed to East Asia. Secondly, while it has done a world of good to a significant number of people, the absolute numbers still point to a vast lead in the case of North America and Europe.

This is partially explainable by the fact that while they account for a declining relative global GDP, America and Europe still account for a high proportion of equity market capitalization globally. Consequently, wealth, as a statistical entity distinct from income, has positive exposure to the very growth seen in emerging markets, even if incomes do not. The net effect is that while wealth has increased tremendously, it has in particular benefited Europe and North America – with the latter very much remaining in a league of its own and starkly so.

19

PERCENTAGE OF CHINESE GLOBAL FORTUNE 500 REVENUE EARNED OUTSIDE CHINA IN 2017

MCKINSEY



HORIZONTAL : WEALTH PER ADULT. VERTICAL MEDIAN WEALTH PER ADULT. RELATIVE SIZE : SHARE OF GLOBAL WEALTH. ALL FIGURES USD 2017 CONSTANT

CREDIT SUISSE

The variable with the greatest explanatory power is quite simply trade. The leitmotiv over the past 30 years has been the expansion of trade during what has come to be known as the Third Age of Globalization.

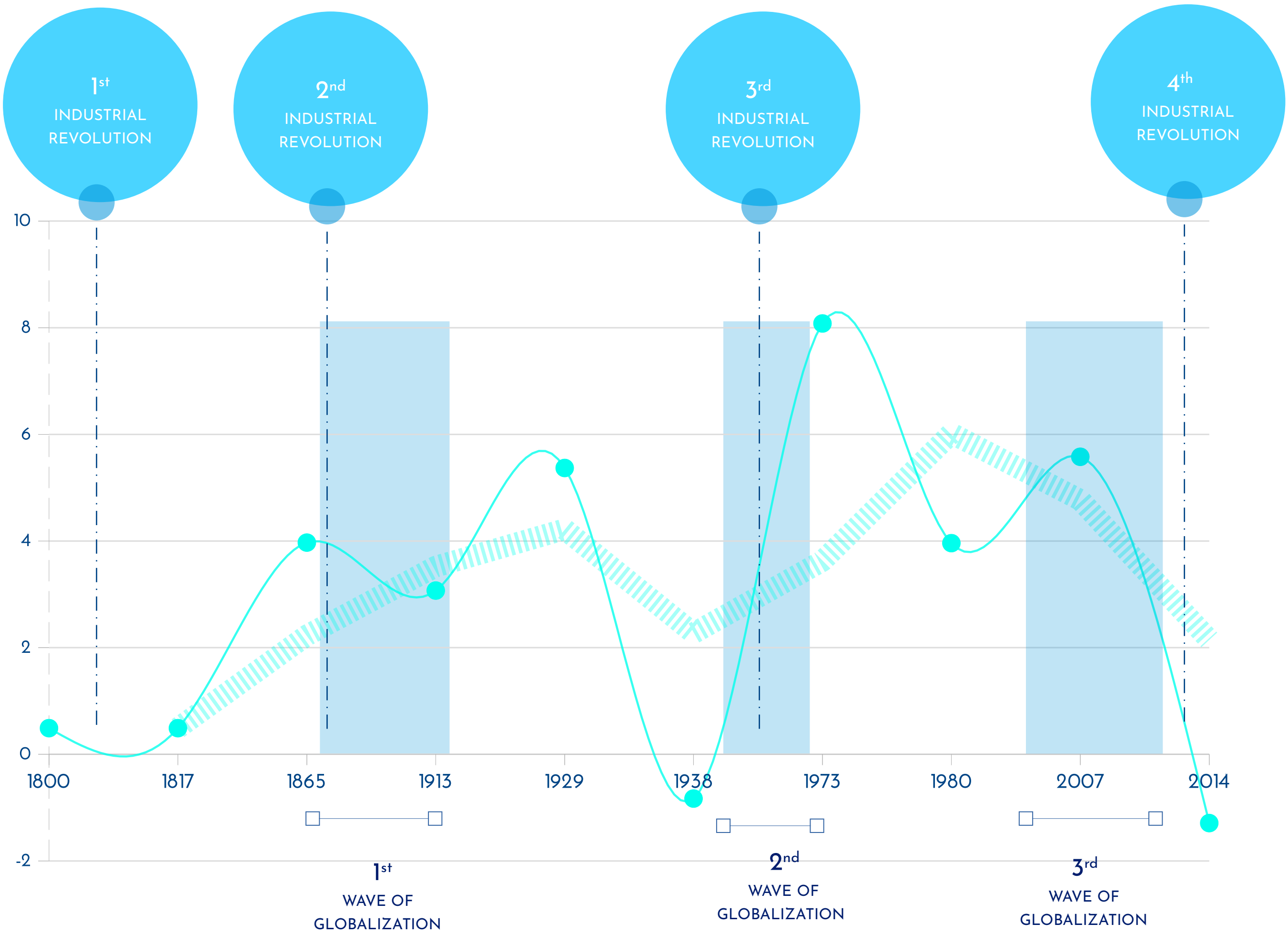
While the First and Second were significant for a whole host of reasons, it has been the Third which, in absolute terms, actually shifted the economic balance. That is reflected both in terms of the plain correlation of trade with relative distribution. This is a key point for it explains the patterns of growth observed generally and runs contrary to the general BRICs narrative.

Quite simply, the data would indicate that the relative redistribution has been dominated by trade, which has been dominated by China, which in turn has fuelled a commodity supercycle in Latin America, Asia Pacific and Africa.

40

TIMES WORLD TRADE IS LARGER, IN ABSOLUTE TERMS, IN CONSTANT 2017 USD, IN 2018 THAN IN 1913

WTO



CHANGE IN THE RATE OF TRADE GROWTH

FREDERICO - TENA WORLD TRADE HISTORICAL DATABASE

70

PERCENTAGE OF GLOBAL GROWTH ACCOUNTED FOR BY EMERGING MARKETS TO 2030

HSBC

In turn, this provides an explanation of why despite the significant rise in wealth observed across the latter – Latin America, Africa and Asia Pacific – the discrepancy between average wealth and median wealth has actually increased. Median wealth in some places, such as Africa, has risen only modestly, with demographics partially accounted for by the inclusion of only adults in the population observed.

That trend, in turn, does not run contrary to rising wealth in North America or Europe, despite the relatively stagnant average real incomes, as much of this trade has been intermediated within Western supply chains, led by Western companies and financed by Western banks, investment funds and pension funds. The effect has been to let financial wealth held in North America and Europe enjoy exposure to growth in emerging markets while still remaining primarily held in what may be called 'risk off' assets in the world's reserve currency – a very much enviable position by most standards.

166

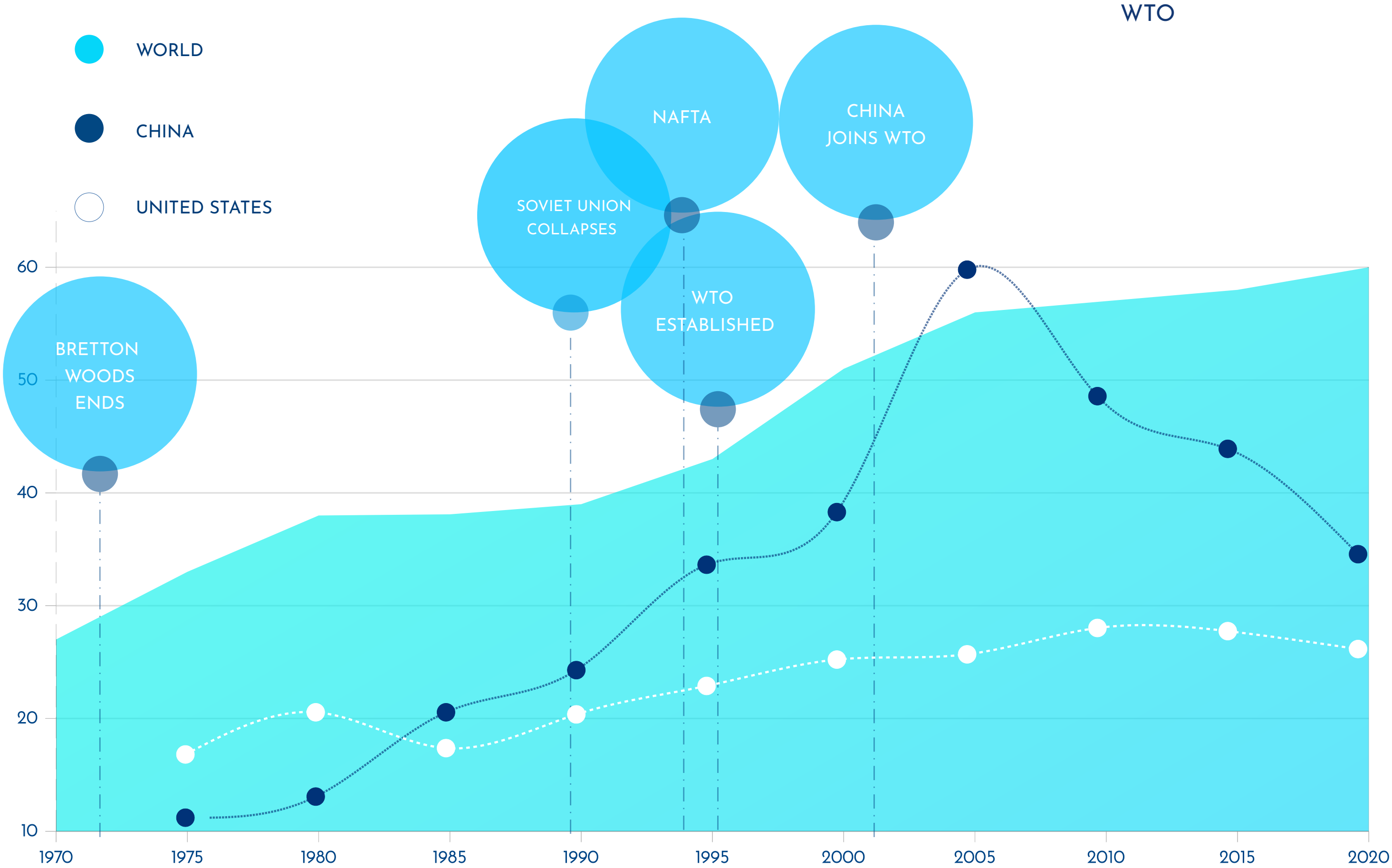
PERCENTAGE INCREASE IN MARKET CAPITALIZATION OF DOMESTIC COMPANIES SINCE 2000, UNITED STATES

WORLD BANK

10.1

TRADE AS PERCENTAGE OF GDP FOR THE UNITED STATES, IN 1970

WTO



PERCENTAGES OF GDP ACCOUNTED FOR BY TRADE, IMPORTS AS WELL AS EXPORTS, FOR CHINA, THE UNITED STATES AND THE GLOBAL AVERAGE

WORLD TRADE ORGANIZATION

That particularity of the 'rise of the rest' is reflected in the manner in which North American and European companies very much continue to dominate the upper echelons of international companies – the exception being China and the Asia Pacific region.

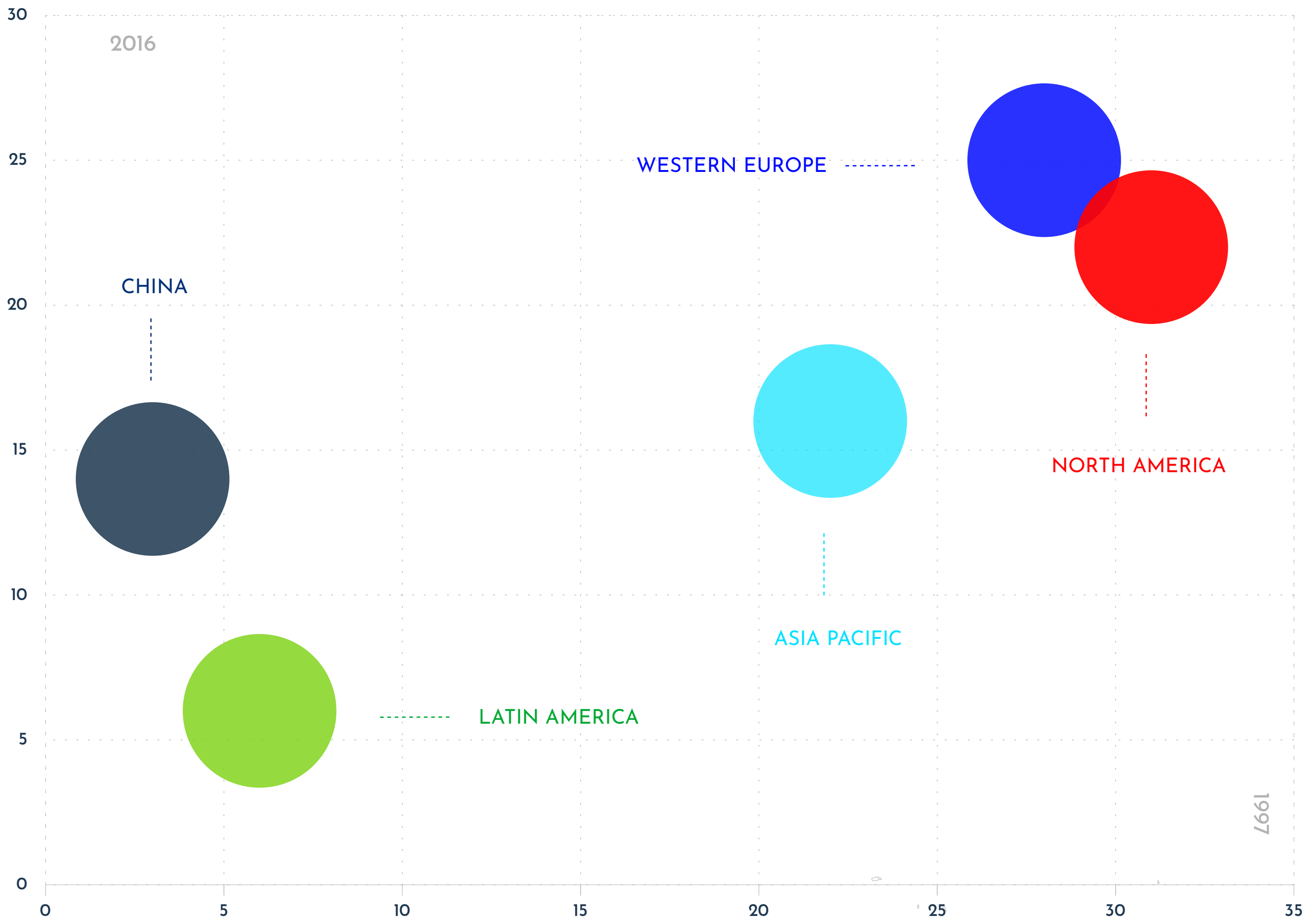
In other words, the previous three decades successfully created unprecedented wealth across the world, most of the new corporate titans have been in the Asian area while much of the rest of the world experiencing not a steady sequence of growth but a commodity supercycle.

This was laid-out in no uncertain terms during the SARS-CoV-2 pandemic : in 2020 more than 80 developing countries had to seek financial help from the IMF. Of the largest 18 crude exporting countries, 17 are no richer in relative terms today than when they discovered oil to begin with.

1

NUMBER OF THE 18 HIGHEST EXPORTERS OF CRUDE OIL WHO ARE RICHER IN RELATIVE TERMS THAN WHEN CRUDE OIL RESERVES WERE DISCOVERED

FOREIGN AFFAIRS



PERCENTAGE OF CORPORATE AT REGIONAL REPRESENTATION IN GROSS INCOME AT THE 1% LEVEL. HORIZONTAL AXIS REPRESENTS FIGURES FOR 1997 AND THE VERTICAL AXIS FIGURES FOR 2016.

MCKINSEY

14

CHINA

MCKINSEY

PERCENTAGES OF CORPORATE REPRESENTATION AT THE 1% INCOME LEVEL, IN 2018

16

EUROPE

CHINA

China has been noted for its tremendous growth over the past 30 years, its swift response to the pandemic as well as by the fact that it took the route of industrialization towards middle income status. This seems at least partially reflected in its particularities : while it shows the same discrepancies between median wealth and average wealth, the patterns observed are closer to Europe or the United States than other emerging market economies. This may be observed by the gradient of the trend-lines between median wealth and average wealth, showing a marked difference with, for example, Latin America. By numbers alone, the wealth picture in China is in many respects closer to the West than, for example, Russia, which shows discrepancies similar to other commodity exporting economies. This is important in understanding Chinese businesses, and the enterprising families that rose during the previous thirty years. While political patronage is its own commodity in many respects, the majority has risen in the context of arduous work of industrialization and global competitiveness. It has also been significantly more normally distributed, being the only of the emerging markets studied where, in percentage terms, median wealth has increased almost as much as average wealth.

14.9

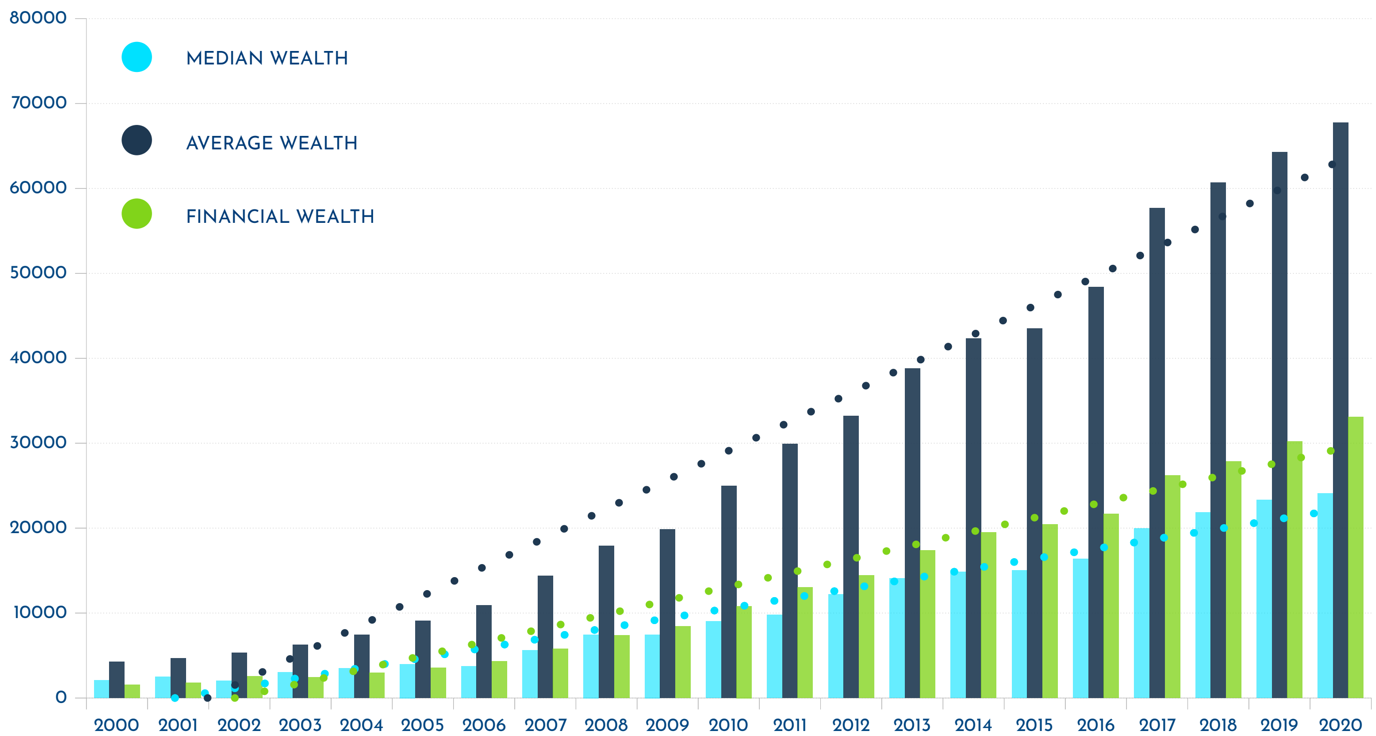
TIMES AVERAGE WEALTH HAS INCREASED OVER THE BASE IN CHINA SINCE 2000

CREDIT SUISSE

11.7

TIMES MEDIAN WEALTH HAS INCREASED OVER THE BASE IN CHINA SINCE 2000

CREDIT SUISSE



AVERAGE WEALTH PER ADULT AND MEDIAN WEALTH PER ADULT OVER THE SELECTED PERIOD OF TIME, 2000 TO 2020. ALL FIGURES IN USD.

CREDIT SUISSE

NORTH AMERICA

Wealth in North America has not only increased considerably but at levels actually surpassing many emerging market countries. Likewise, the SARS-CoV-2 pandemic has hardly impacted wealth, as opposed to general incomes, as much as in some places like Latin America or Asia Pacific.

Needless to say, this stands in clear contrast with the picture of stagnant real incomes observed in countries such as America since the late 1970s and the discrepancy between average wealth and median wealth continues to increase, particularly in the context after the housing boom. Nevertheless, rising wealth remains a fact and overall figures are still well above global averages despite 'the rise of the rest'. This is partially a reflection of the degree to which wealth is financial, often tied to companies and assets which themselves enjoy the fortunate position of being 'risk-off' assets during downturns while remaining exposed to emerging market growth during upturns. Quite simply, North American wealth has well documented habit of landing on its feet regardless of the situation, even if the picture at the lower rungs of social class remains fairly stagnant.

137

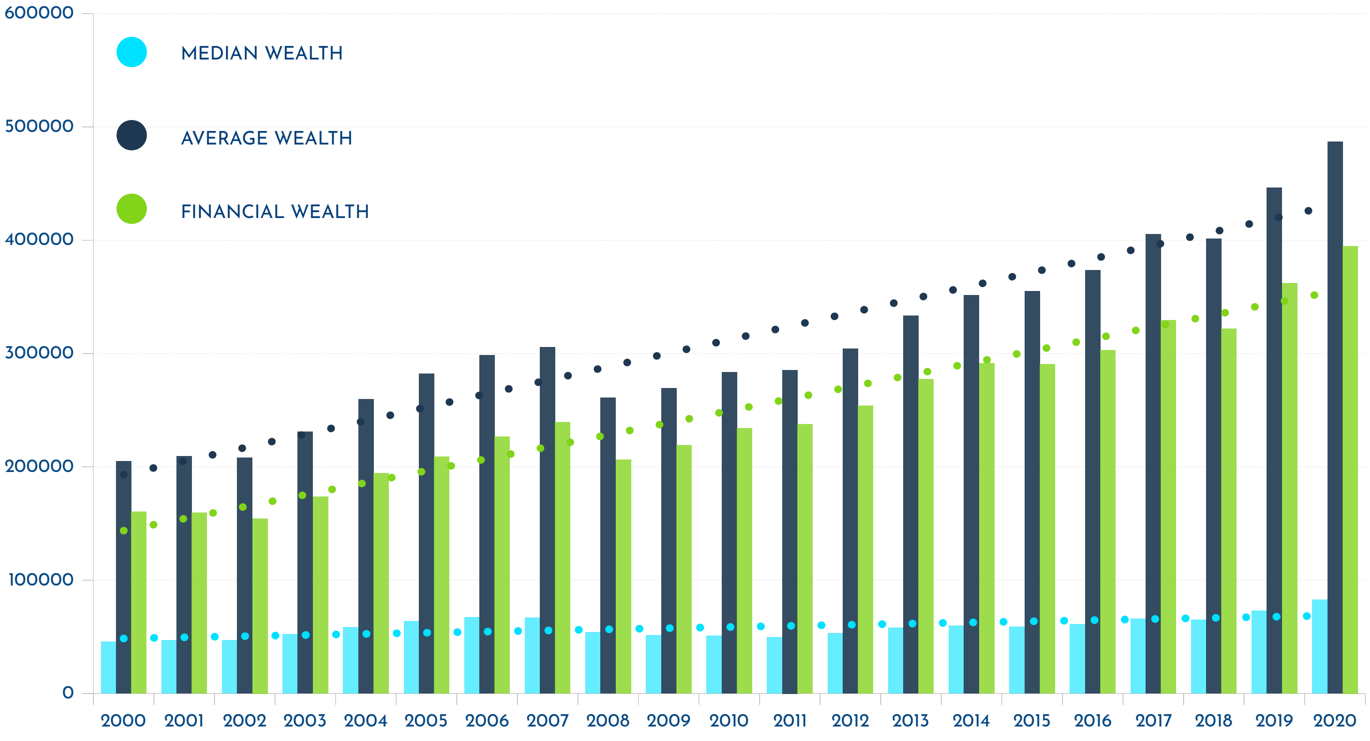
PERCENTAGE INCREASE OVER THE BASE IN AVERAGE WEALTH FOR THE NORTH AMERICAN REGION SINCE 2000

CREDIT SUISSE

81

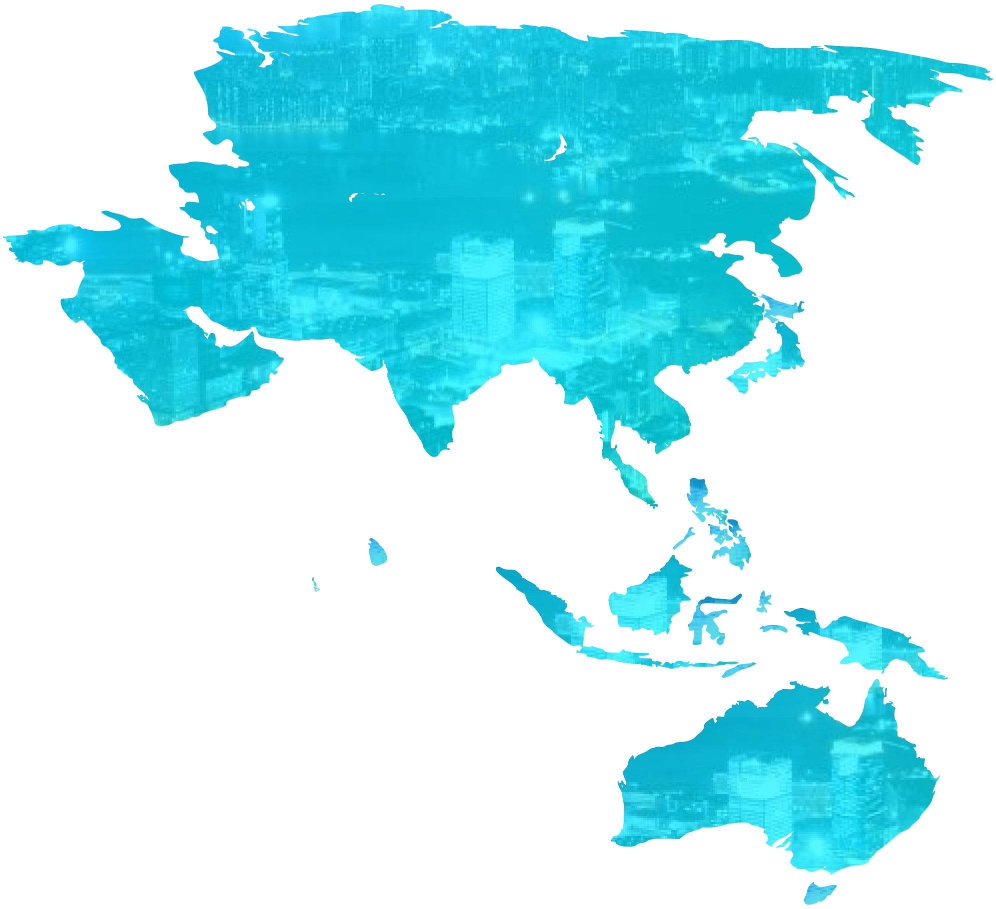
PERCENTAGE INCREASE OVER THE BASE IN MEDIAN WEALTH FOR THE NORTH AMERICA REGION SINCE 2000.

CREDIT SUISSE



AVERAGE WEALTH PER ADULT AND MEDIAN WEALTH PER ADULT OVER THE SELECTED PERIOD OF TIME, 2000 TO 2020. ALL FIGURES IN USD.

CREDIT SUISSE



ASIA - PACIFIC

Wealth in Asia-Pacific has a distinct, highly particular profile which reflects the stark heterogeneity of the area – from the slums of India to the Korean and Japanese metropolises. That is in turn reflected in the vast discrepancy seen between median wealth and average wealth, with Australia and North East Asia essentially acting as outliers in average terms.

Compounding the statistical effect are two fairly straightforward facts. First, that the most populous countries in the population sample have some of the highest rates of inequality in the world, such that great wealth often resides next to abject poverty. Secondly, the increase in population makes the median wealth of most households remain well below global averages, such that while most families are significantly better off than before, the emerging markets boom over the past 30 years has left many people's lives almost untouched. Not least, this is reflected in the profile of families which have risen to the top in this environment, with many export-based industrialists and real estate tycoons dominating the charts in East Asia, while commodity exporters and sprawling conglomerates dominate in India, the Philippines and Australia.

78

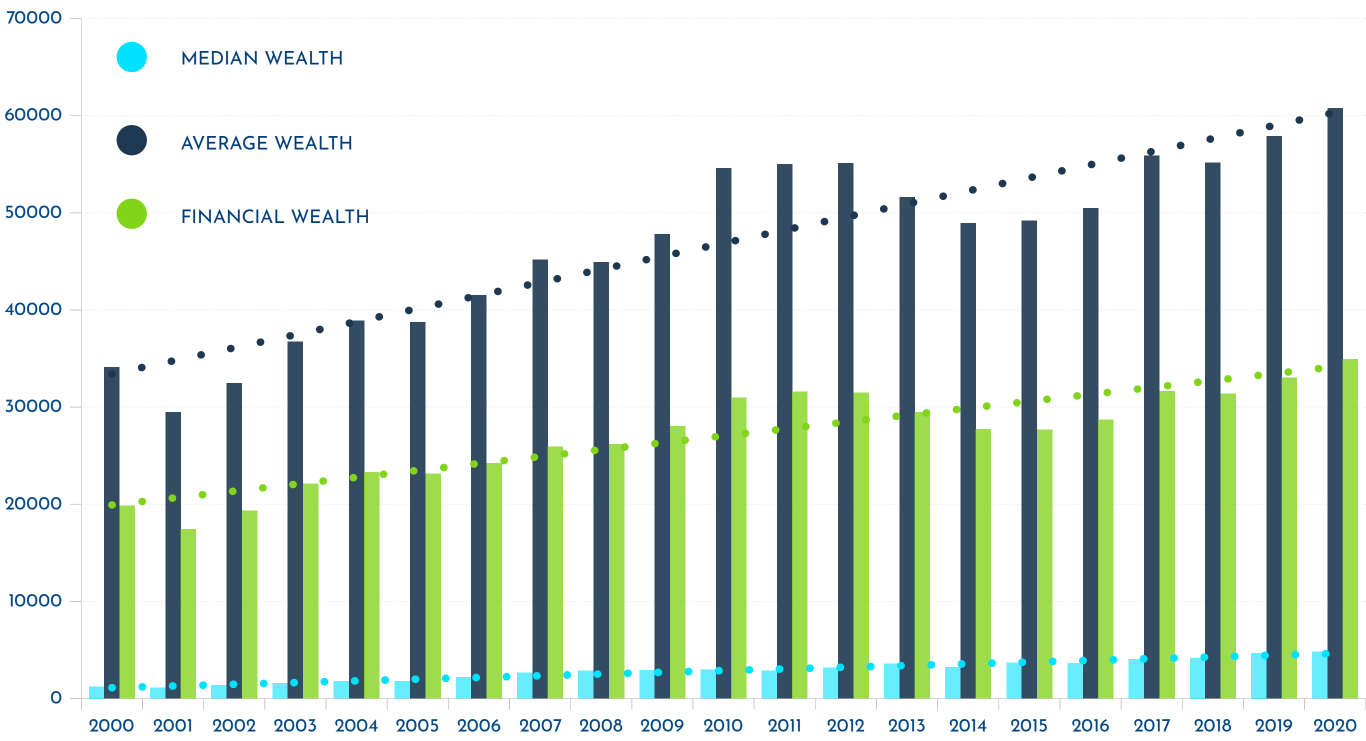
PERCENTAGE INCREASE OVER THE BASE IN AVERAGE WEALTH FOR THE ASIA - PACIFIC REGION SINCE 2000

CREDIT SUISSE

289

PERCENTAGE INCREASE OVER THE BASE IN MEDIAN WEALTH FOR THE ASIA - PACIFIC REGION SINCE 2000.

CREDIT SUISSE



AVERAGE WEALTH PER ADULT AND MEDIAN WEALTH PER ADULT OVER THE SELECTED PERIOD OF TIME, 2000 TO 2020. ALL FIGURES IN USD.

CREDIT SUISSE

SOUTH AMERICA

Wealth in Latin America is often characterised by inequality and this remains statistically true but it may also be taken into account to what degree that wealth also displays above average variance. This seems to be a reflection of the degree to which commodities remain a critical part of both government revenues, and thus poverty alleviation programmes, as well as the wealth of the top families and business in Latin America.

Even to a greater degree than in Africa, wealth seems tied to commodity exports and is financial to a lesser extent than average. To an extent, this simply reflects relatively poorly developed equity markets and a higher degree of inequality but Latin America stands out in this respect in that, in contrast to Africa, government revenue often translates into a plethora of programmes. This has the effect of creating covariance between both wealth at the top and at the bottom with commodity demand – at times figures almost mirroring Chinese GDP growth. Nevertheless, the overall picture remains one of growth, even if initial projections of emerging markets did not materialise.

171

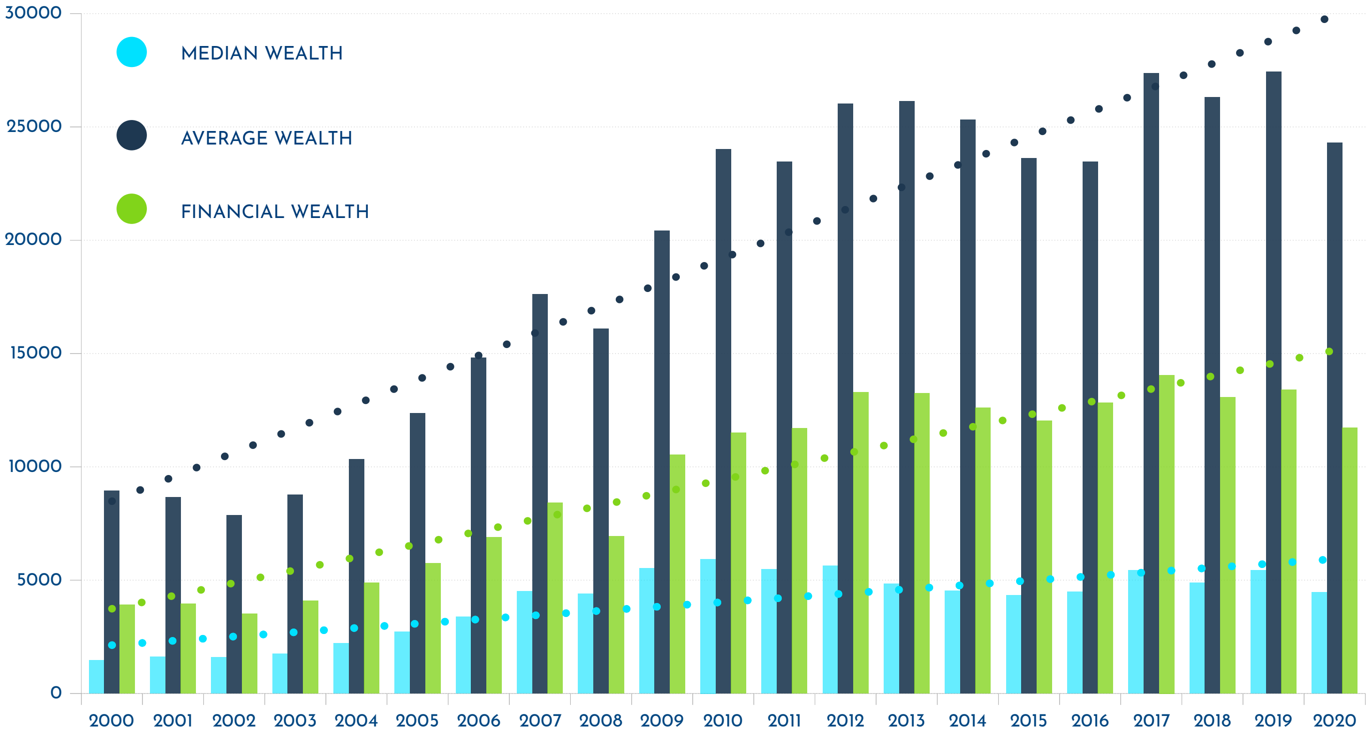
PERCENTAGE INCREASE OVER THE BASE IN AVERAGE WEALTH FOR THE LATIN AMERICAN REGION SINCE 2000

CREDIT SUISSE

205

PERCENTAGE INCREASE OVER THE BASE IN MEDIAN WEALTH FOR THE LATIN AMERICAN REGION SINCE 2000.

CREDIT SUISSE



AVERAGE WEALTH PER ADULT AND MEDIAN WEALTH PER ADULT OVER THE SELECTED PERIOD OF TIME, 2000- TO 2020. ALL FIGURES IN USD.

CREDIT SUISSE

EUROPE

While stagnation tends to make headlines and, in relative terms, it cannot be said that Europe holds the same position it once did, statistics would indicate at least some of this is somewhat exaggerated. Median wealth alongside average wealth have increased considerably over the previous two decades, and a significant number of people seem better off.

Like in North America's case, wealth in Europe is financial to a greater degree than the global average, such that some of the increase in wealth stems from rises in equity markets and investments which tend to accumulate at the top, are at least partially a reflection on emerging markets growth, and may not necessarily reflect in the lower classes of society as much. This polarization of wealth creation has some explanatory power in elucidating Europe landscape of often stagnant real average incomes and rising wealth – a highly divergent return on capital to domestic economic growth. However, the overall picture is not as bleak as suggested by that dynamic, with the vast majority still enjoying a median level of wealth still well above global averages and at least growth in wealth, including that held in real estate and pension savings.

178

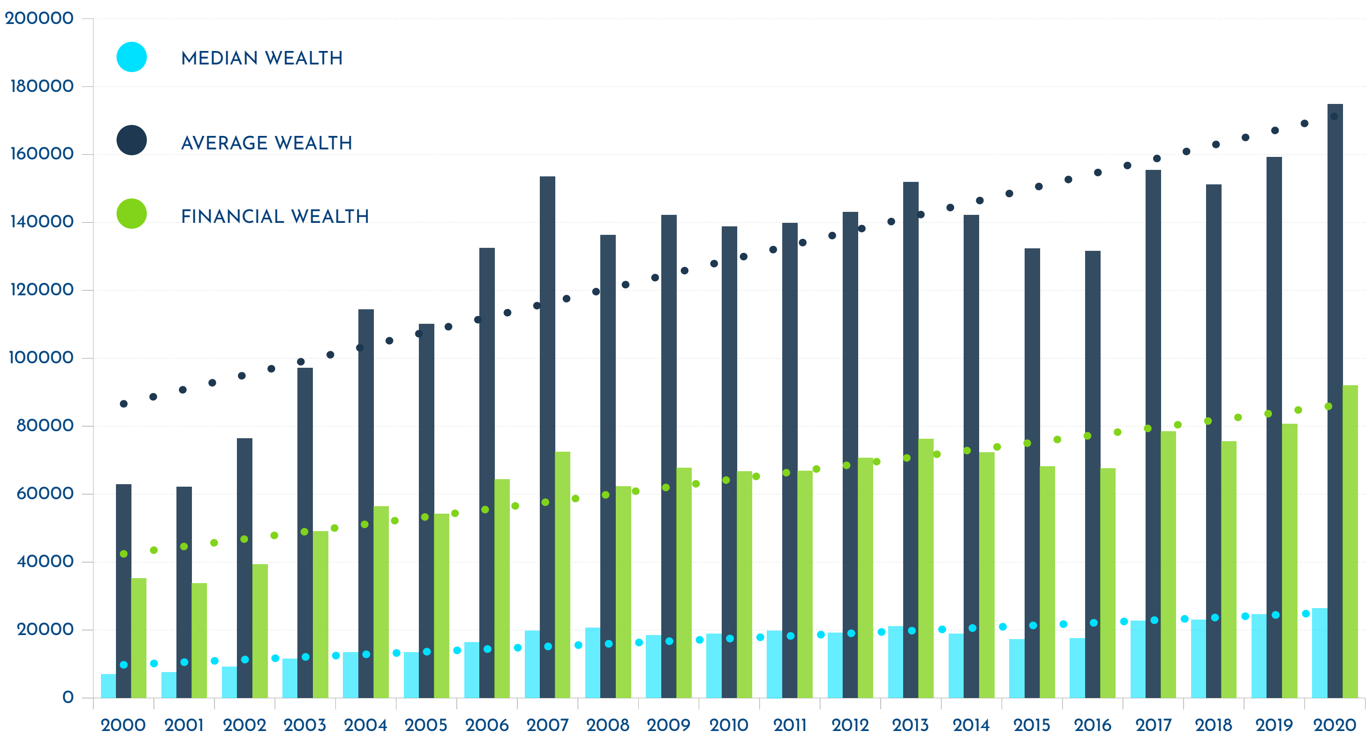
PERCENTAGE INCREASE OVER THE BASE IN AVERAGE WEALTH FOR THE EUROPEAN REGION SINCE 2000

CREDIT SUISSE

276

PERCENTAGE INCREASE OVER THE BASE IN MEDIAN WEALTH FOR THE EUROPEAN REGION SINCE 2000.

CREDIT SUISSE



AVERAGE WEALTH PER ADULT AND MEDIAN WEALTH PER ADULT OVER THE SELECTED PERIOD OF TIME, 2000 TO 2020. ALL FIGURES IN USD.

CREDIT SUISSE

AFRICA

Over the past decades Africa, and by extension African wealth, has seen a tremendous boom – so much so as to generate speculation about an new emerging addition to the world's middle class. Part of that is true, as average wealth has indeed risen in line with most other regions while median wealth, in percentage terms, has actually outperformed the global average, even if only slightly.

However, this bears qualification. The low base from which that growth is calculated still means the otherwise much vaunted African middle class is still thin on the ground. Likewise, the correlation between growth and commodity exports, points to the phenomenon of premature de-industrialisation, which makes it difficult to create the basis of that broad middle class and state development alongside responsive, if not strictly democratic, lines. Predictably given parameters, most of the 'superclans' which arose during this time are either involved in commodity exports or are focused on consumer goods for the domestic market, a dynamic which bodes ill for long-term development and income equality.

278

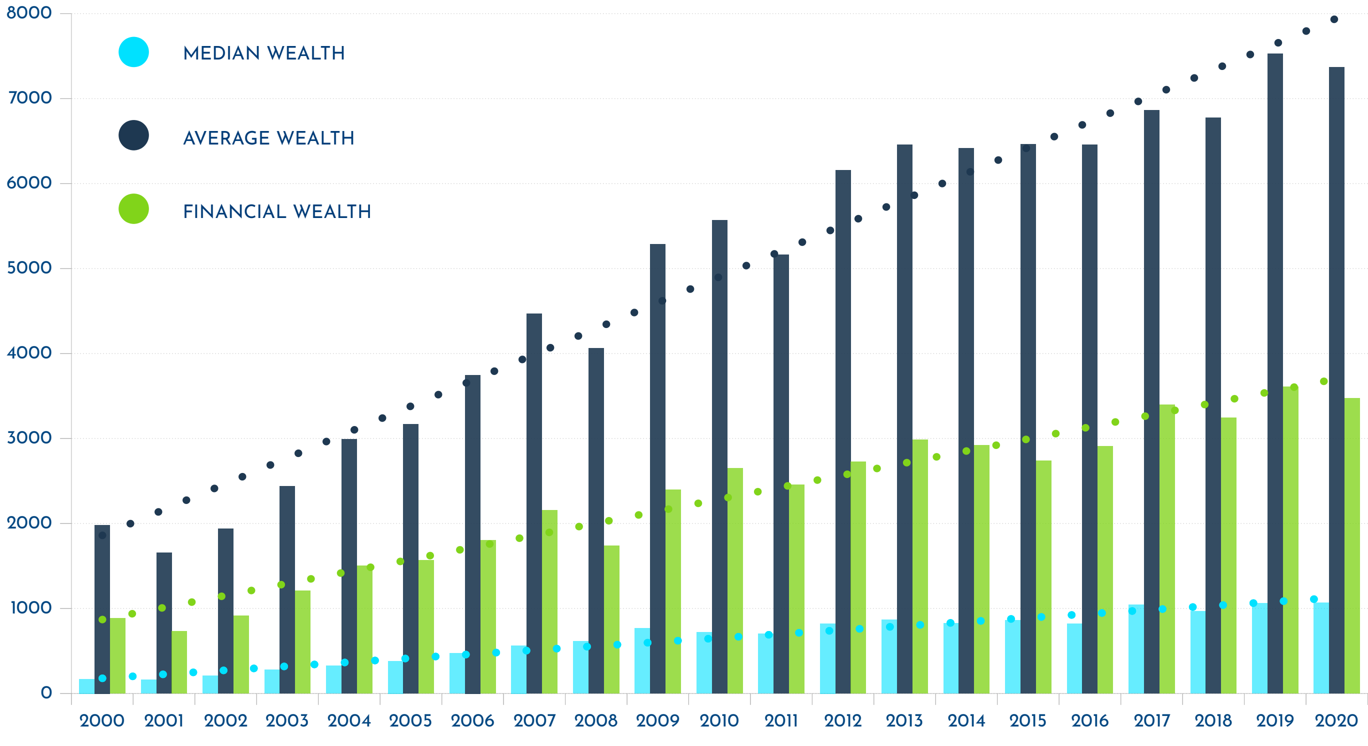
PERCENTAGE INCREASE OVER THE BASE IN AVERAGE WEALTH FOR THE AFRICAN REGION SINCE 2000

CREDIT SUISSE

500

PERCENTAGE INCREASE OVER THE BASE IN MEDIAN WEALTH FOR THE AFRICAN REGION SINCE 2000.

CREDIT SUISSE



AVERAGE WEALTH PER ADULT AND MEDIAN WEALTH PER ADULT OVER THE SELECTED PERIOD OF TIME, 2000 TO 2020. ALL FIGURES IN USD.

CREDIT SUISSE

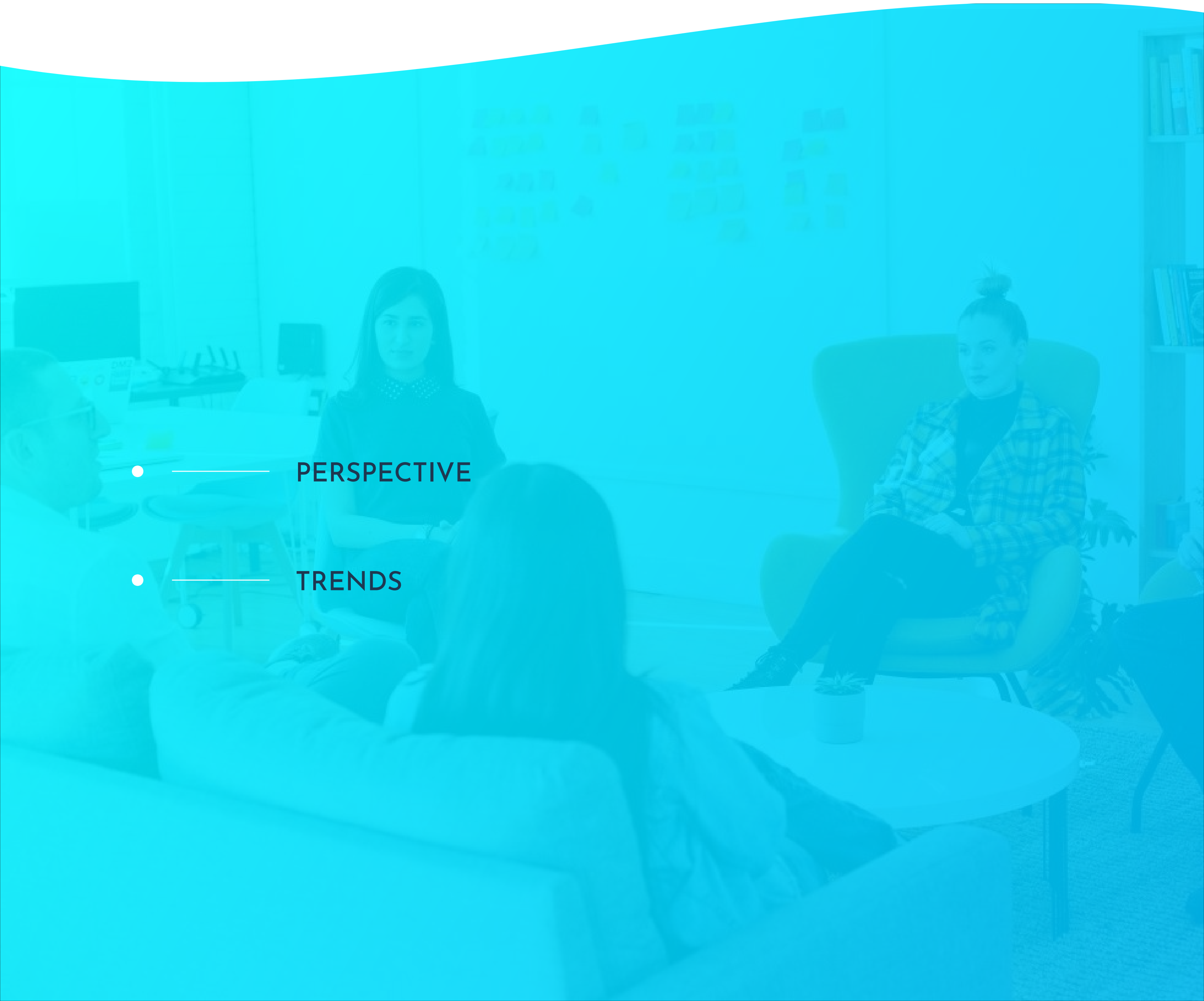
26.8

TRILLION USD CURRENTLY ESTIMATED TO BE OWNED BY HIGH NET WORTH INDIVIDUALS, GLOBAL FIGURES

BARRONS

TRENDS IN FAMILY BUSINESS

An overview of trends in family business, in particular large family businesses, from both a historical perspective which explains the concept of the 'superclan' as well as current trends which make it highly relevant.



- PERSPECTIVE
- TRENDS

PERSPECTIVE

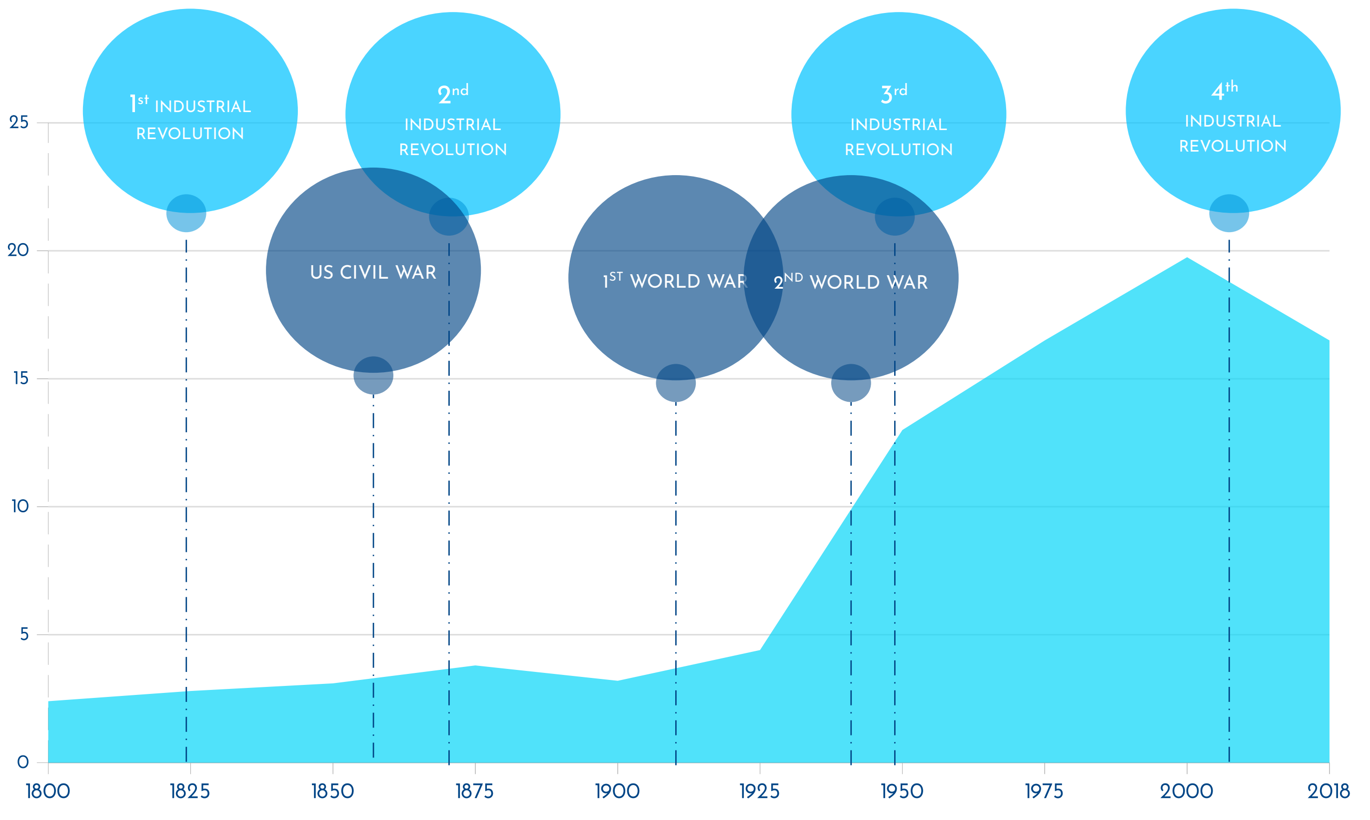
The clan as an organisational unit is often associated with a perceived distant past, almost medieval in nature and regarded as both anachronistic as well as ineffective. Likewise, the concept of a family business is seen as limited in scope, in the vein of small businesses and limited partnerships which have neither the financial means nor the ambition to expand.

Statistically, that is simply not the case, and the reasons are two-fold. First, the transition from patrimonial structures often based on direct family links and traditional leadership, in Weberian terms, to the formal bureaucratic structures from which the limited liability corporation evolved is a very much recent affair, correlated with the Second Industrial Revolution and the World Wars.

60

PERCENTAGE OF EMPLOYMENT IN THE UNITED STATES ACCOUNTED FOR BY FAMILY BUSINESSES

DELOITTE



TAX REVENUE AS A PERCENTAGE OF GDP IN THE UNITED STATES

ST. LOUIS FEDERAL RESERVE


7.28
TRILLION USD IN REVENUE OF THE TOP 500 FAMILY BUSINESSES, GLOBAL FIGURES
ERNST & YOUNG

Its expansion, and eventual global spread, has been associated with the vast expansion of the state in Western countries following the World Wars and the eventual development of the Keynesian Welfare state in their aftermath. That state of affairs is a century old and may not necessarily be regarded as a constant in economic history. Quite the contrary, it may be seen as the result of a particular set of economic, social and political circumstances, which precipitated its rise in the Western world.

14.9

TIMES AVERAGE WEALTH HAS INCREASED IN CHINA SINCE 2000

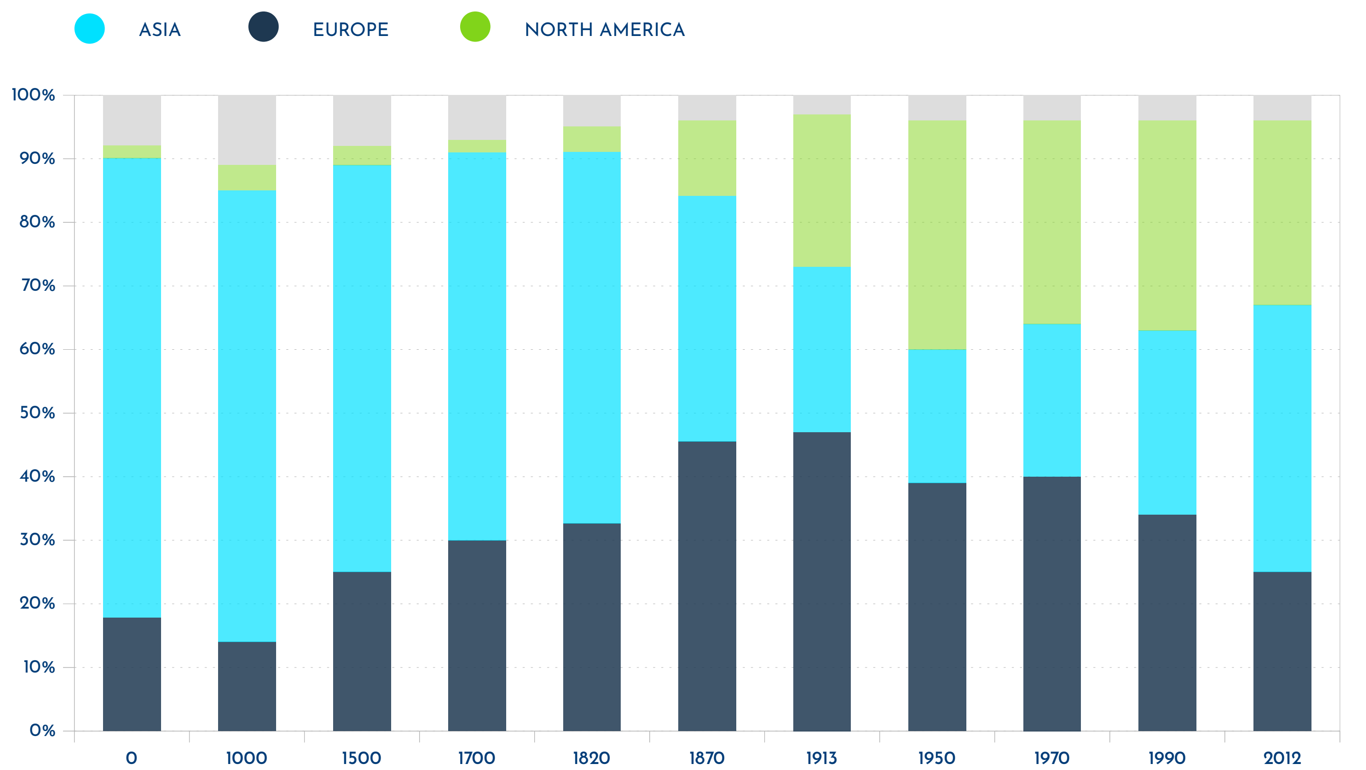
CREDIT SUISSE

In the context in which the First Industrial Revolution and Second Industrial Revolution primarily started in Western countries and the First Wave of Globalization and Second Wave of Globalization were also led by Western countries, the norms and structures observed in that context became universalised to an extent – in particular in terms of expectations and what development may look like. Elsewhere, with the exception of the East Asian states in Fukuyama's taxonomy of state development, it has been the clan as an organisational unit which showed the highest degree of endurance – from monarchical families of various sorts to the business conglomerates of today.

11.7

TIMES MEDIAN WEALTH HAS INCREASED IN CHINA SINCE 2000

CREDIT SUISSE



PERCENTAGE OF WORLD GDP BY CONTINENT

MADDISON

67

SOVEREIGN

HSBC

PREDICTED PROPORTION OF GLOBAL GDP IN ACCORDANCE TO ECONOMIC PROFILE, SPLIT BETWEEN SOVEREIGN AND LIBERAL, ROUGHLY DEFINED BY HSBC AS EITHER PRIMARILY DOMINATED BY PRIVATE MARKETS OR STATE AUTHORITIES

33

LIBERAL

The late period of the Third Industrial revolution and the Third Wave of Globalization was concurrent with the phenomenon otherwise referred to as 'the revolt of the elites' in Western countries and the outsourcing of significant parts of the industrial capacity of the aforementioned.

With economic growth and, to a degree, development in emerging markets the structures which dominate these naturally rose to prominence, approximating but not necessarily matching Western standards. Specifically, this may be noted in the phenomenon of tremendous family-owned conglomerates alongside more traditional SOEs (State-Owned Enterprises) common to the the East Asian development model.

In turn, these changed the composition of the global business landscape away from what came to be known as the Western standard of equity-financed public limited companies to a more historically-oriented patchwork of debt-financed, often state-led or family-owned companies. As such, far from being anachronistic, the rise of family businesses to the upper echelons of business is a natural consequence of the 'rise of the rest', in particular China and East Asia, to relative prominence.

50

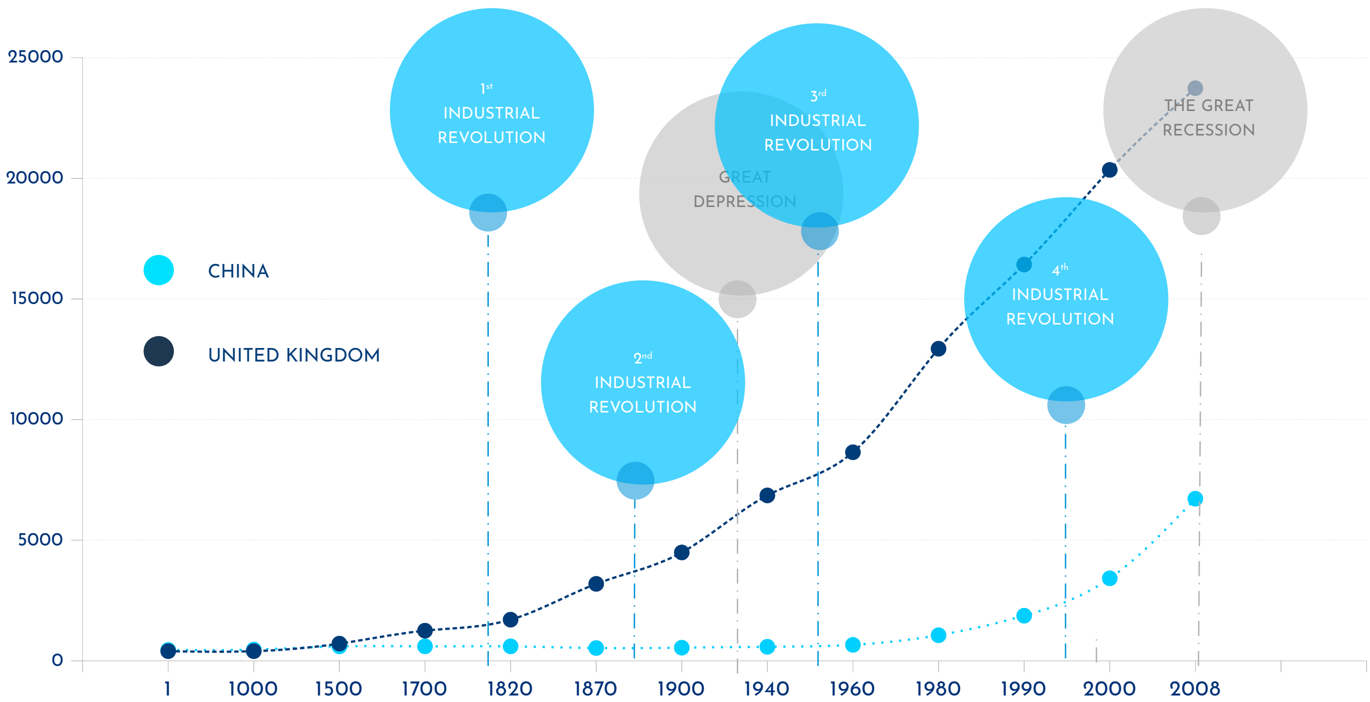
PERCENTAGE THAT CHINA REPRESENTS OF THE GLOBAL INCREASE IN NET WEALTH SINCE 2000

MCKINSEY

21

NUMBER OF TIMES GDP PER CAPITA IN CHINA HAS INCREASED SINCE DENG XIAOPING'S REFORMS

WORLD BANK



HISTORIC GDP PER CAPITA IN CHINA AND THE UNITED KINGDOM, FIGURES QUOTED IN PPP USD SPECIFIC TO THE MADDISON SET

MADDISON

Specific to the rise of emerging markets and the resurgence in family business has been the return of the phenomenon here referred to as the 'superclans'. This may be loosely defined as a family unit which has amassed significant wealth and, more often than not, political power while primarily keeping in line with what may regarded as, roughly speaking, a family business. Historically, such 'superclans' have in fact dominated economies, finance, trade and politics alike for most of human history, in most places.

As with some emerging markets, their return is not so much a new phenomenon but mean-reversion. In this case it implies reverting to the historical norm of, arguably, the high inequality of tri-part societies to use Piketty's Hegelian terminology, an otherwise natural and expected phenomenon in the context in which the post-war Keynesian welfare state along national lines is duly receding as the Second Industrial Era in which it arose give way to the Third and Fourth.

Quite simply, the world is returning to normal, in terms of the distribution of global GDP between states and in terms in wealth distribution along class lines. Family business, and the 'superclans' which dominate it, are far from anachronistic. This is what the future looks like.

40

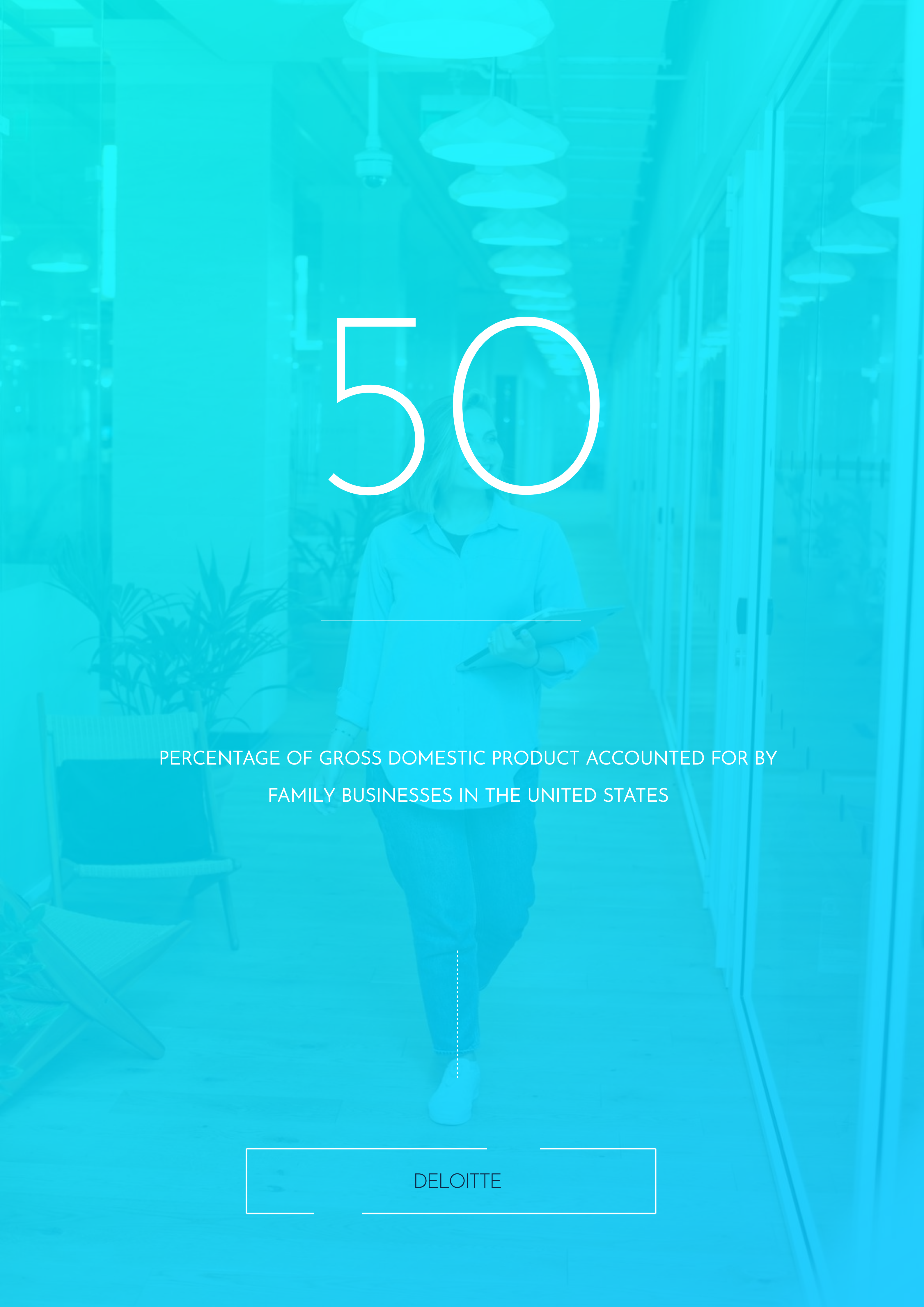
YOUTH
UNEMPLOYMENT RATE
IN SPAIN, IN 2018

MCKINSEY

3.9

TRILLION USD BY
WHICH WEALTH HELD
BY BILLIONAIRES
INCREASED IN 2020

OXFAM



50

PERCENTAGE OF GROSS DOMESTIC PRODUCT ACCOUNTED FOR BY FAMILY BUSINESSES IN THE UNITED STATES

DELOITTE

TRENDS

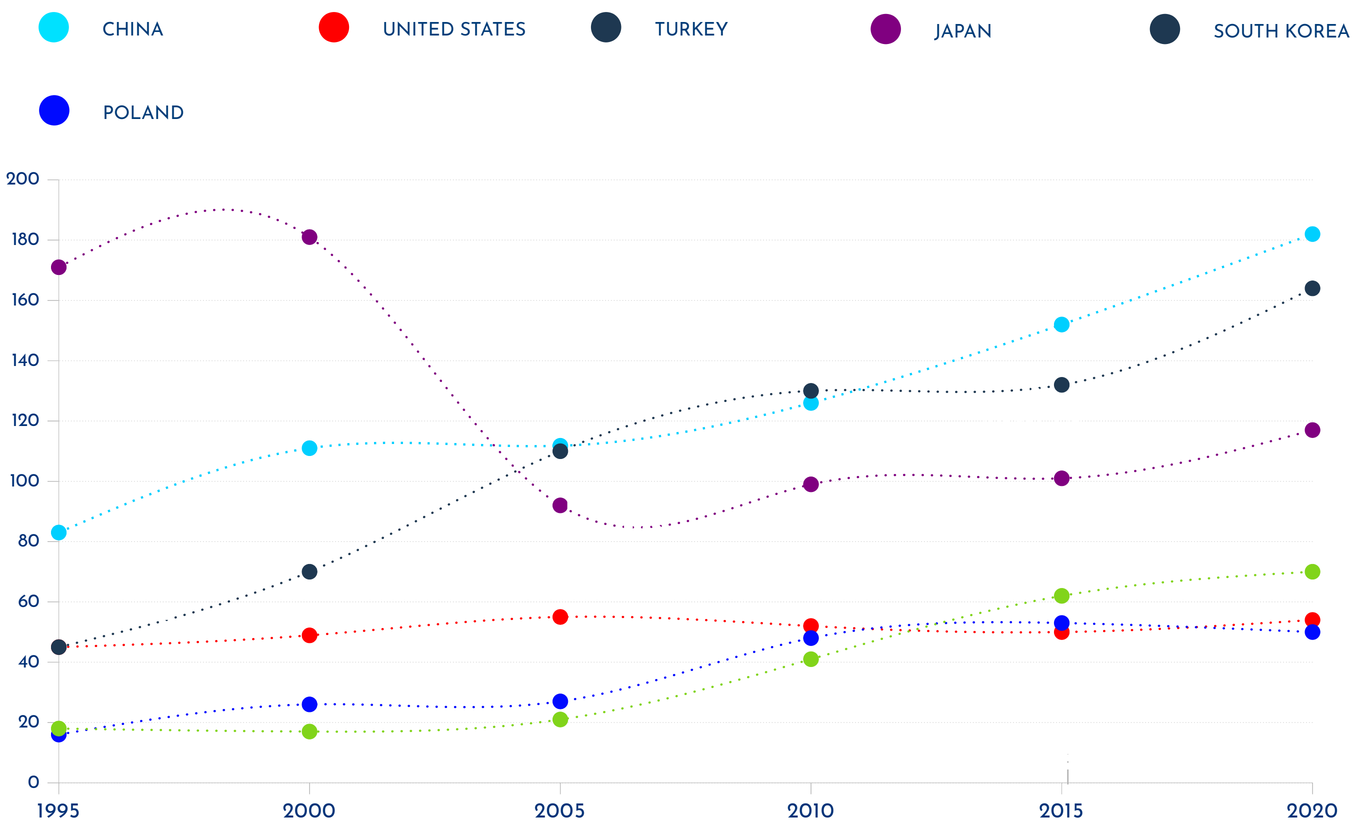
Family business has enjoyed some of the best decades in modern recorded history. Part of the that is historical as a reflection of the rise of this model alongside emerging markets generally, and may be referred to in the first section. However, there have been other general trends which impacted family businesses in a positive manner, and by extension, what is being termed as 'superclans'.

First, the previous three decades have seen a significant shift from equity capital to debt capital, for three core reasons. In absolute terms, most important has been the rise in the relative prevalence of companies in 'bank-led' countries where a majority of large companies are financed through debt, be it Germany or China.

90

PERCENTAGE OF BUSINESSES IN GERMANY WHICH ARE FAMILY CONTROLLED

ERNST & YOUNG



DOMESTIC CREDIT PROVIDED BY BANKS AS A PERCENTAGE OF GDP

WORLD BANK

Secondly, debt has been given a new lease on life due to regulatory changes. The issue itself is complex but it suffices to say that in America, Britain, Germany and Japan, debt-based finance is taxed at rates that are 3.8% to 6% lower than those on equity investments.

In the context where many of these investments are from pension funds, the effect can be considerable. Third, quantitative easing has meant that central bank interest rates have been kept at historic lows to perhaps the longest period in history. Despite the natural spillover effect into equity markets this has made debt financing cheaper relative to equity capital and companies have reacted naturally by adjusting their ratio of debt to capital to achieve lower weighted average costs, at relatively higher levels of risk and control.

This shift towards debt may be regarded as highly beneficial to family businesses, and privately held businesses generally, as it helped negate of the core drawbacks of privately held companies, as opposed to publicly listed companies, namely access to capital.

30

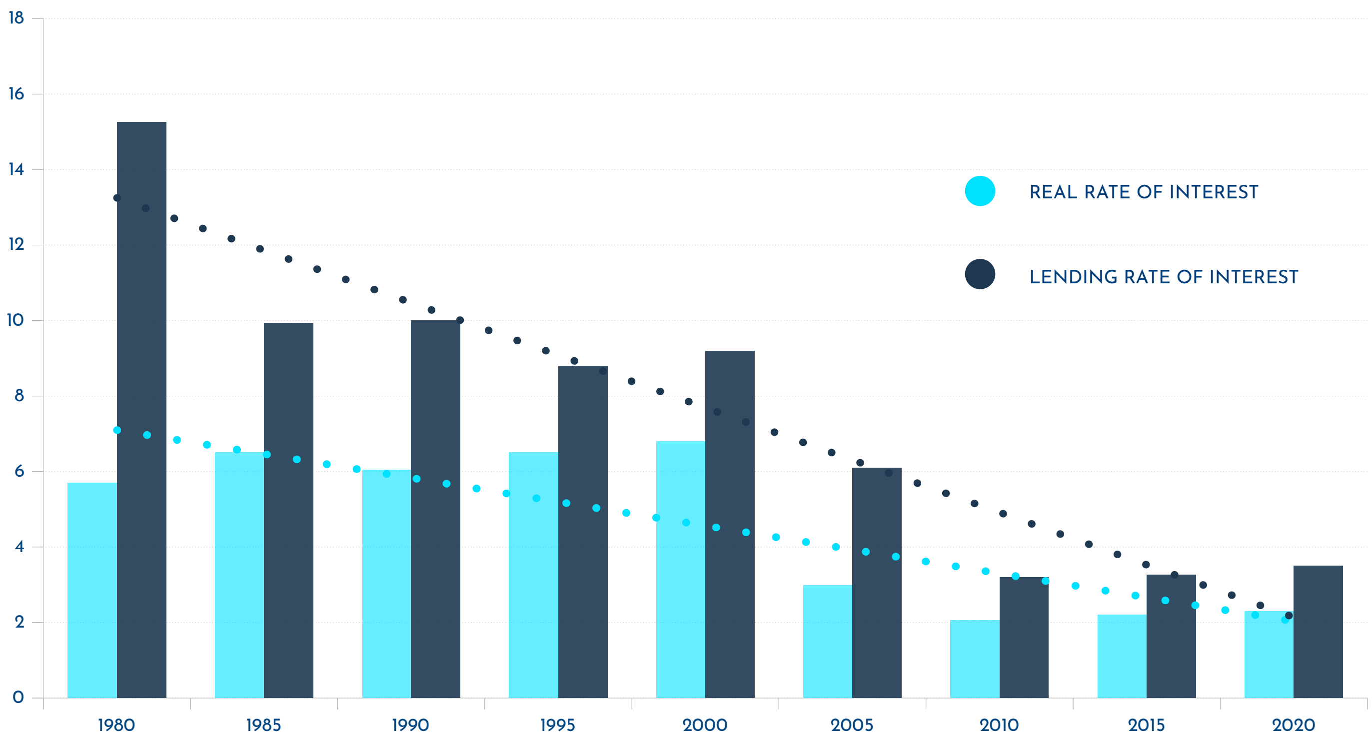
PERCENTAGE OF FAMILY BUSINESSES WHICH REPORT USING ONLY INTERNAL RESOURCES FOR FINANCING, IN 2020

DELOITTE

50

OF FAMILY BUSINESSES SURVEYED REPORTING THAT THEY ARE WILLING TO OFFER EQUITY IN EXCHANGE FOR FINANCING IF LONG TERM

KMPG



REAL RATE OF INTEREST AND THE LENDING INTEREST RATE, FOR THE UNITED STATES

WORLD BANK

Not least, debt has gained on equities due to the level of quantitative easing seen over the past few years. For example, about 20% of USD currency in circulation has been created in the past three years, according to Ruchir Sharma of Morgan Stanley.

Some of the 'cheap money' thus created found its way into equity markets, alternative investments and commodities as asset classes. But much reflected into improved access to capital for family businesses, particularly those family businesses with established collaterals, and who could quite straightforwardly borrow at relatively low rates while being able to invest into higher yielding activities. Quite simply, the intent of quantitative easing has been to ensure the supply of credit, to corporate clients foremost. However, in the context in which the differentiation factor to risk remains often non-normal, it may be said that it led to slightly better access to companies in general – and a lot better to a few companies who would have had access anyway.

The effect has not only been to help what is colloquially termed 'mom and pop' stores, but also to essentially guarantee the upper echelons of society, particularly those from the background of well-established family businesses, ample capital at close to bottom rates. By most indications, that capital was often used successfully and the period of low interest rates accelerated what Tomas Piketty explained thorough the divergence of r > g, namely the return on capital and economic growth.

That, in turn, accelerated the phenomenon here called 'superclans', namely family businesses which could benefit from this conjecture of having access both to low rates of interest as well as ample opportunities for yielding activities beyond the scope of main market indexes and thus fully take advantage of the many opportunities a developing economy presents.

20

PERCENTAGE OF USD CURRENCY IN CIRCULATION WHICH HAS BEEN CREATED IN THE PAST 3 YEARS

MORGAN STANLEY

42

OF FAMILY BUSINESSES SURVEYED WHICH REPORT ACCEPTING FINANCIAL CAPITAL FROM HNWI

KMPG

44

OF HIGH NET WORTH INDIVIDUALS SURVEYED WHO REPORT HAVING PREVIOUSLY INVESTED IN A FAMILY BUSINESS

KMPG

CRISIS ADAPTATION

An overview of the impact of the SARS-CoV-2 pandemic and the supply-side shocks of 2022 on family businesses, followed by an overview of the responses family businesses undertook.

- SARS - COV - 2
- RESPONSE
- SUPPLY - SIDE SHOCKS

SARS-COV-2

Overall, we may categorise the impact of the SARS-CoV-2 pandemic into three analytical categories of impact :

- Economic
- Financial
- Managerial

The first is primarily environmental while the second are primarily a matter of reaction and adaptation to that environment and may be further categorised as such. In economic terms, as far as exogenous shocks as concerned, SARS-CoV-2 provided both a statistically raw initial shock but also a tremendous amount of uncertainty for most businesses. A few months after its initial detection, by April 2020 most of the globe was experienced protracted lock-downs, and significant restrictions on most activities. The effect has been very much heterogeneous, with some businesses enjoying a boom in demand in the context of accelerated digitalisation while others effectively closed doors. Despite the scale of the impact itself, the S&P500 as well as emerging market

46

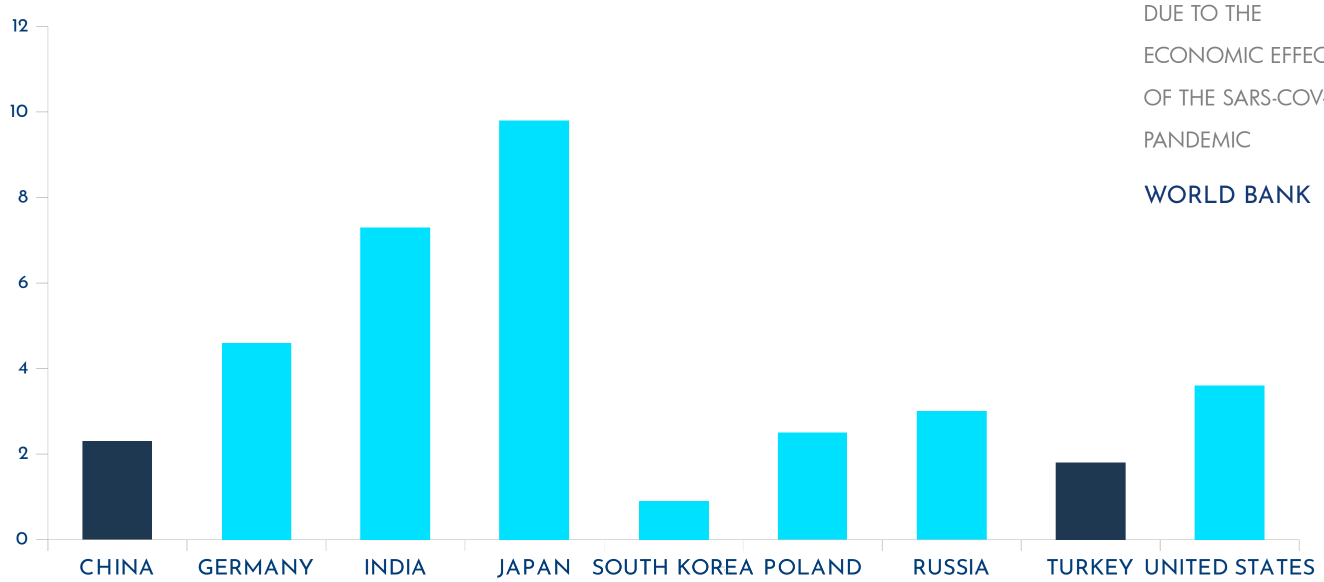
PERCENTAGE OF FAMILY BUSINESSES SURVEYED WHICH REPORTED A DECREASE IN SALES DUE TO THE SARS-COV-2 PANDEMIC, IN 2021

PWC

100

MILLION PEOPLE WHO HAVE FALLEN BELOW THE POVERTY LINE, GLOBALLY, IN 2021, DUE TO THE ECONOMIC EFFECTS OF THE SARS-COV-2 PANDEMIC

WORLD BANK



GROSS GDP GROWTH IN 2020. BLUE INDICATES GROWTH, LIGHT BLUE INDICATES A DECREASE. ALL FIGURES GIVES ARE PERCENTAGES.

WORLD BANK

indexes may be said to have done well – in January 2022, the S&P500 for the United States stood at 40% above its 2018 level.

That does not hold universally, however. When looking at emerging markets, the degree to which growth actually equalled development as well as the degree to which that growth was based on broad growth in Total Factor Productivity or fuelled by commodity exports proved a source of concern. As China went into a national lock-down, some emerging markets experienced a nosedive due to lower commodity demand. Likewise, some developing countries proved relatively ineffective in their responses in enforcing quarantine measures or state effectiveness in times of crisis, with a significant economic impact on many businesses, particularly smaller business which benefited from neither cash reserves nor government guarantees on loans. Needless to say, that does not necessarily apply to those who could afford to 'weather the storm', such that some better-heeled family businesses may in fact find fewer competition as recoveries take hold.

75

PERCENTAGE OF EMERGING MARKET FIRMS SURVEYED SAYING THEY HAVE BEEN NEGATIVELY IMPACTED BY THE SARS-COV-2 PANDEMIC

VOXEU

"

Without COVID-19, GDP growth in the past decade would have been about 3.6 percent—just below the 3.7 percent experienced in 2000–09. Not bad given all the challenges, and contrary to the mood of pre-pandemic times. Indeed, each decade has witnessed stronger economic growth than the 1980s and 1990s, each about 3.3 percent. Hundreds of millions of people have been taken out of absolute poverty as a result, in part because of the growth miracle led by the so-called emerging markets, of which my beloved BRICs were front and center. [.] While India has notably disappointed in recent years, it is broadly developing along the path we envisioned. For both Brazil and Russia, however, 2010–20 economic performance was very disappointing, which has occasionally led me to joke that perhaps I should have called the "BRICs" the "ICs." Brazil and Russia have both suffered from the well-known commodity curse and, as evidence suggests, are far too dependent on the world commodity cycle for their own sustainable development.

JIM O'NEILL

FINANCE & DEVELOPMENT

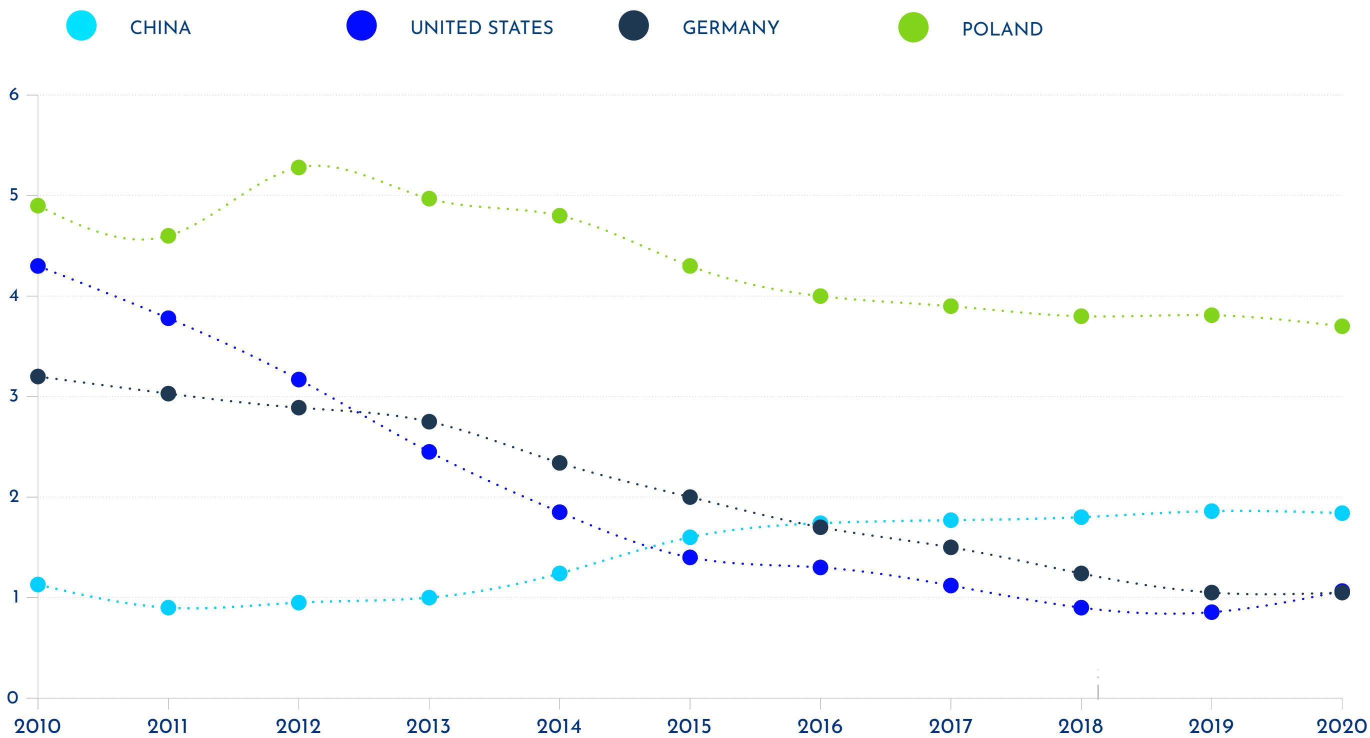
RESPONSE

In terms of finance and management, it may said that most family business proved far more resilient than initial worries raised during the start of the SARS-CoV-2 pandemic. Part of that is due to government responses, which collectivity undertook one of the greatest fiscal and monetary expansions seen outside of wartime, inclusive of direct payments, interest rate cuts, loan guarantees and in some cases freezes on interest payments. Part of that is due the context in which many banks and larger companies found themselves, having already de-leveraged significantly following the 2008 'Great Recession'. This may be seen as reflected in the fact that there has been no large scale bank failure or financial contagion. Furthermore, as reflective of the overall response, the number of non-performing loans has barely budged in 2020, with the note of caution that full data for 2021 is not yet available.

25

PERCENTAGE OF FAMILY BUSINESSES SURVEYED WHICH REPORTED AN INCREASE IN SALES DUE TO THE SARS-COV-2 PANDEMIC, IN 2021, GLOBALLY

PWC



BANK NON-PERFORMING LOANS AS A PERCENTAGE OF TOTAL GROSS ASSETS

WORLD BANK

In managerial terms, it may be said that family businesses responded the best way they could, given the above economic context and financial situation – with government help playing a key role in the degree to which management could weather cash flow and sales problems.

This has meant some degree of heterogeneity based on countries. In Europe and North America, greater help from governments seems to have translated into business confidence and, by extension, adaptations such as working from home and rapid digitalization which proved successful. While problems abound, such as with employee on-boarding, it has meant business continuity at the very least.

Meanwhile, in countries where support has been more conservative, management often had to respond with a somewhat shorter timeline in mind and perhaps darker expectations. Notably, in cases such as India and its low-margin garments industry in particular, this meant mass layoffs and sometimes business closures, at least for the time being. This tended to ripple across companies and show-up in GDP figures but the extent to scarring effects which may be long term remains to be seen.

80

PERCENTAGE OF FAMILY BUSINESSES SURVEY WHICH REPORT TO HAVE BEEN ABLE TO ALLOW STAFF TO WORK FROM HOME

PWC

31

FALL IN URBAN EMPLOYMENT IN INDIA, IN THE FIRST 4 MONTHS OF 2020

VOXEU

"

Only one-third (34%) of surveyed businesses have had to cut dividends, and 31% of family members have taken salary cuts. Overall, only one in five businesses (21%) needed to access extra capital; 15% of the owners are putting in more of their own cash, and a further 23% say they are prepared to do so if necessary. Family businesses have proven robust and adaptable—and as we have come to expect, they are taking a people-first approach, prioritising the well-being of their employees and supporting their local communities throughout the crisis. Eighty percent are enabling staff to work from home, and 25% are repurposing their production to meet pandemic-related demand.

PWC

SUPPLY SHOCKS

Following the pandemic, businesses faced further supply-side shocks. These have commonly been referred to a single shock associated with the Ukrainian conflict but the situation for businesses is more heterogeneous and merits decomposition into :

- The Trade Shock
- Demand Pull Inflation
- Supply Push Inflation
- Debt Pressure

The trade shock was very much in place even before the SARS-CoV-2 pandemic and political instability associated with the Ukrainian conflict, in the context of trade disputes between the United States and China. However, as modern supply chains could not re-polarise in time and there is indication that most companies both in the West as well as emerging markets chose to let profit margins absorb most cost increases, this shock took a significant amount of time to actually be felt by the general public, becoming partially co-incidental with other shocks. Furthermore, it was initially localised in a number of key sectors and while it deeply affected certain large businesses – including large family businesses – it did not initially translate into widespread, potentially dangerous, cost increases for the business community as a whole.

Afterwards, in the second half of 2021, came the realisation that the fiscal expansion initiated by governments in response the SARS-CoV-2 pandemic was partially overestimating the capacity of economies, primarily in the Western world, to immediately transition out the context of the SARS-CoV-2 pandemic to full capacity. This may have led to a situation o fiscally-induced

8

ANNUALISED U.S. INFLATION RATE IN THE FIRST QUARTER OF 2022

PEW RESEARCH

82

PERCENTAGE INCREASE IN THE PRICE OF BRENT CRUDE SINCE JANUARY 2020

WORLD BANK

11

TIMES THE PRICE OF LNG DELIVERIES TO EUROPE IS HIGHER IN MARCH 2022 COMPARED TO JANUARY 2020.

WORLD BANK

demand-pull inflation. Partially, this was not necessarily negative, as it was focused on the consumer market and that allowed retail business to begin passing on the previously absorbed costs to consumers, increasing the financial sustainability of their respective supply chains. However, it also raised inflation expectations for the general economy, which in turn raised the prospects of significant interest rate increases, primarily from the United States' Federal Reserve. In the context of a potential 'risk off' moment, this raised the risk of potential appreciations in exchange rates and investor re-calibrations away from emerging markets, which had not been observed with the feared intensity during the SARS-CoV-2 pandemic. While there was little indication of a repeat of the late 1990s emerging market crises, it is safe to say that most business were acutely cognizant of the tail risk for such a phase shift occurring, potentially lowering investment and any overly-aggressive pushes for market share in the post-pandemic market.

As these twin shocks – the trade shock and the risk associated with a rise in interest rates – were being felt by businesses worldwide, the Ukrainian conflict began in earnest.

48

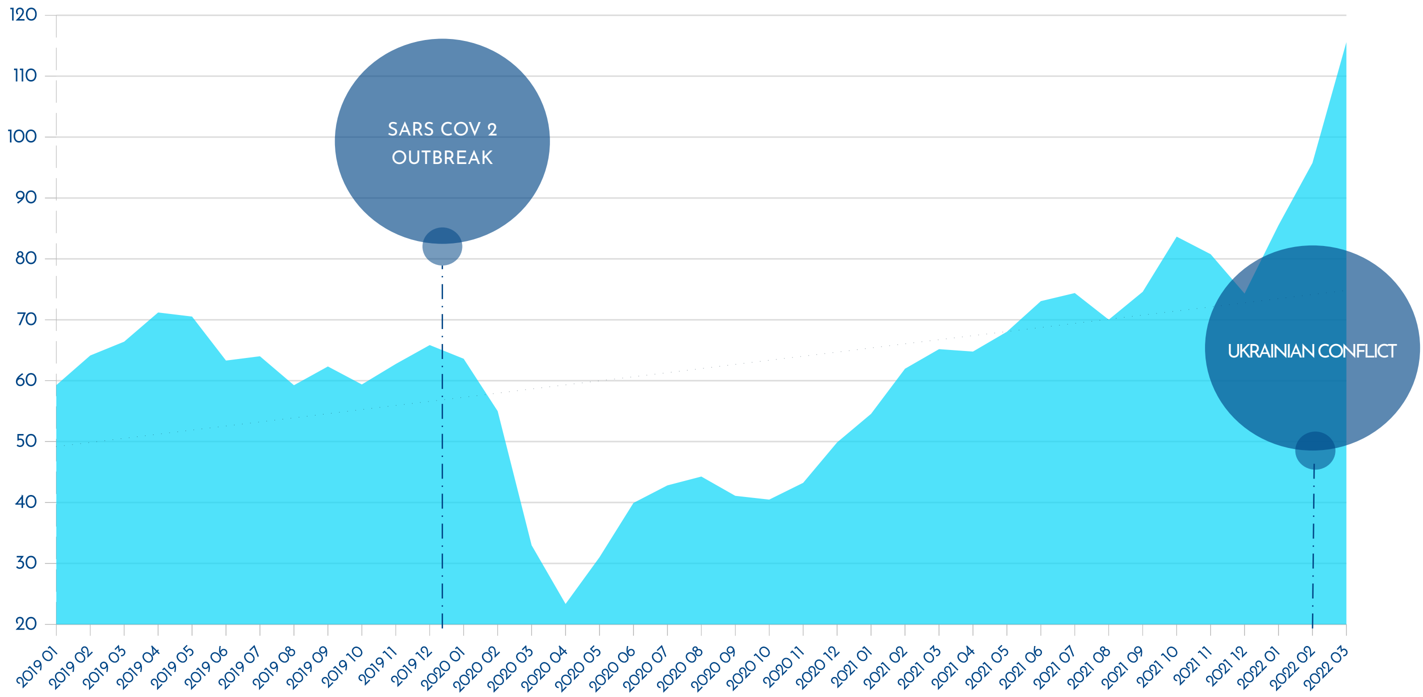
PERCENTAGE OF U.K. BUSINESSES SURVEYED WHICH REPORT THE UKRAINIAN CONFLICT AS A 'TOP THREE' SOURCE OF BUSINESS UNCERTAINLY

VOX EU

97

PERCENTAGE OF U.K. BUSINESSES SURVEYED WHICH REPORTED THE SARS COV 2 OUTBREAK AS A 'TOP THREE' SOURCE OF BUSINESS UNCERTAINLY, IN APRIL 2020.

VOXEU



MONTHLY AVERAGES FOR BRENT CRUDE PRICES FROM JANUARY 2019 TO MARCH 2022

WORLD BANK

This sent commodity prices surging and gave way for supply-push inflation. As a qualification, it needs to be mentioned that this situation primarily affected the Western world, in the context of sanctions – for example the price of LNG for Europe rose from USD 3.6 to USD 42 between January 2020 and March 2022, while for Japan it rose from USD 9.89 to USD 18 over the same time period. Nevertheless, since the focus has been on energy prices and basic foodstuffs, the impact was felt throughout, hitting both businesses as well as the lowest quantiles income of the consumer market the hardest. This, in turn, precipitated the scenario most businesses the world over were most weary of, namely a significant rise in interest rates from Western central banks, most importantly the United States' Federal Reserve. This is expected to put significant strain on corporate finances, albeit with qualification and cognizant of the historic context.

On one hand, the period of low interest rates led many companies to systematically move from equity capital to debt capital and do so over a significant period of time. This leaves many business with a wider exposure to those rate increases while leaving many emerging market businesses with increased risks of financially detrimental exchange rate fluctuations.

On the other hand, the aforementioned period of low interest rates was also a period where many business could issue debt on very favourable terms both in terms of the cost of capital but also its structure. A historically above average size of the debt has the form of bonds, has long maturity and often is in the form of fixed rate coupon bonds.

For example, of the approximately USD 5 trillion worth of corporate bonds issued since the start of 2020 on the U.S. market, 87% are fixed rate coupons bonds. Furthermore, the average rate of those coupons for investment-grade bond is just 3.6%, according to the Economist Intelligence Unit, meaning that the inflation shock gets passed on disproportionately to bond investors, as opposed to the issuers.

3.5

TIMES THE PRICE OF SOUTH AFRICAN COAL HAS INCREASED SINCE JANUARY 2020 TO MARCH 2022

WORLD BANK

87

PERCENTAGE OF THE CORPORATE BONDS ISSUED ON THE U.S. MARKET IN 2022 WHICH ARE FIXED COUPON BONDS

EUI

2029

YEAR ESTIMATED TO HOLD THE MAJORITY OF THE DEFAULT RISK FOR U.S. CORPORATE BONDS

EUI

Also benefiting for longer average maturities, this leaves many of the largest businesses in a relatively enviable position of being able to pass on the price increases to the consumer market while having the debt market at least temporarily maintained at fixed rates.

Needless to say, this does not fully insulate businesses, either on the supply side or the demand side. McKinsey estimates that for companies in most sectors a prolonged supply side shock could wipe out from between 30% to 50% of the company's earnings before interest and tax. Furthermore, as expected inflation increases, the risk of a price spiral remains a source of concern for businesses and governments alike, in particular in the Western world.

However, while U.S. businesses have so far been helped by longer dated debt at low rates, other businesses such as East Asian business by relatively lower inflation rates and while some business will not survive the supply-side shocks, the past few years' crises have shown businesses the world over to be adaptable and resilient beyond common expectations.

30

LOWER ESTIMATE OF THE AVERAGE COMPANY'S EBITA THAT WOULD BE ELIMINATED BY A PROLONGED SUPPLY SIDE SHOCK

MCKINSEY

CENTRAL & EASTERN EUROPE

A look at family business from the economic and social context of Central and Eastern Europe (CEE) countries as well as a look at the case of the Polish economy, which represents one of the paths on which CEE countries began diverging.

- CONTEXT
- POLAND'S PATH
- TAXONOMY

CONTEXT

The landscape across Central and Eastern Europe in terms of family businesses tends towards a few points of homogeneity and significant heterogeneity overall.

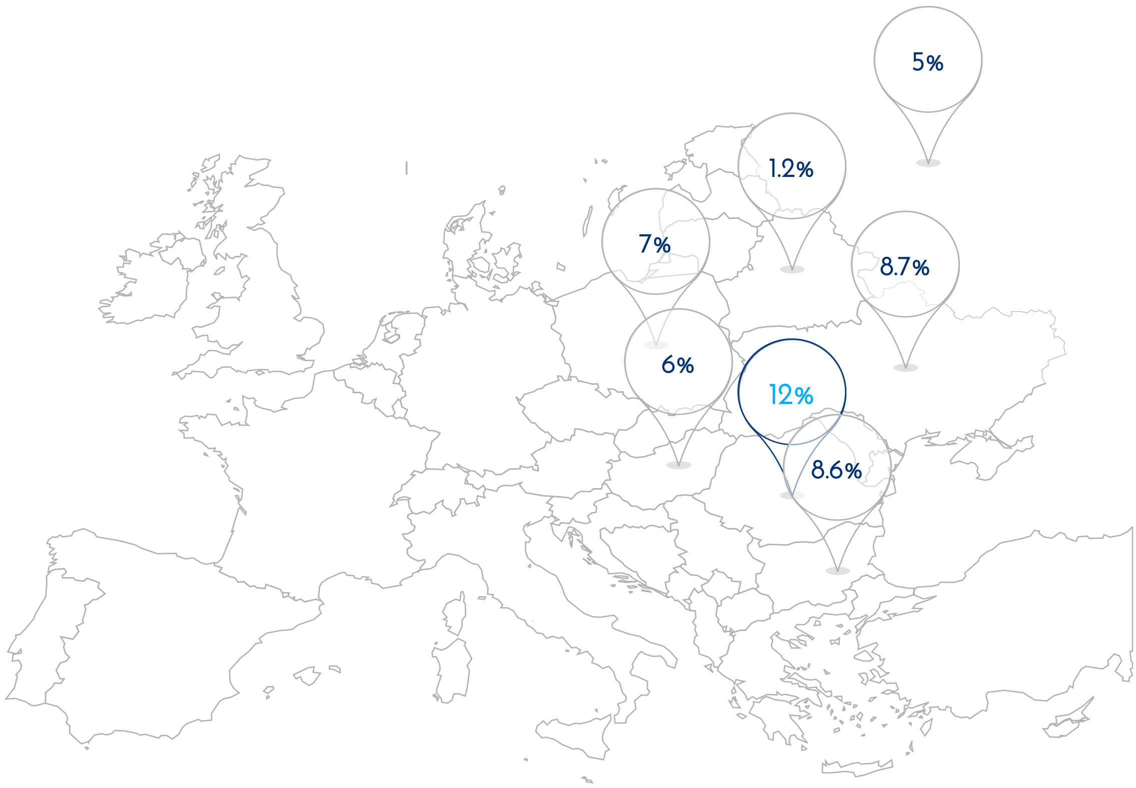
The first may be due to the shared political history, which to a degree created the geographic definition to begin with, as post-Communist states. The second may be due to different paths taken after the fall of communism as well as sometimes significantly different cultural backgrounds.

What the region shares in terms of family businesses tends to trace its roots in the fairly high-risk environment of the 1990s, where family connections and access to credit or business opportunities counted for at least as much as any particular business ideas or innovation.

12

FALL IN GDP EXPERIENCED IN ROMANIA IN 1991 ALONE

WORLD BANK



FALL IN GDP EXPERIENCED IN THE YEAR 1991 ALONE, SELECT COUNTRIES

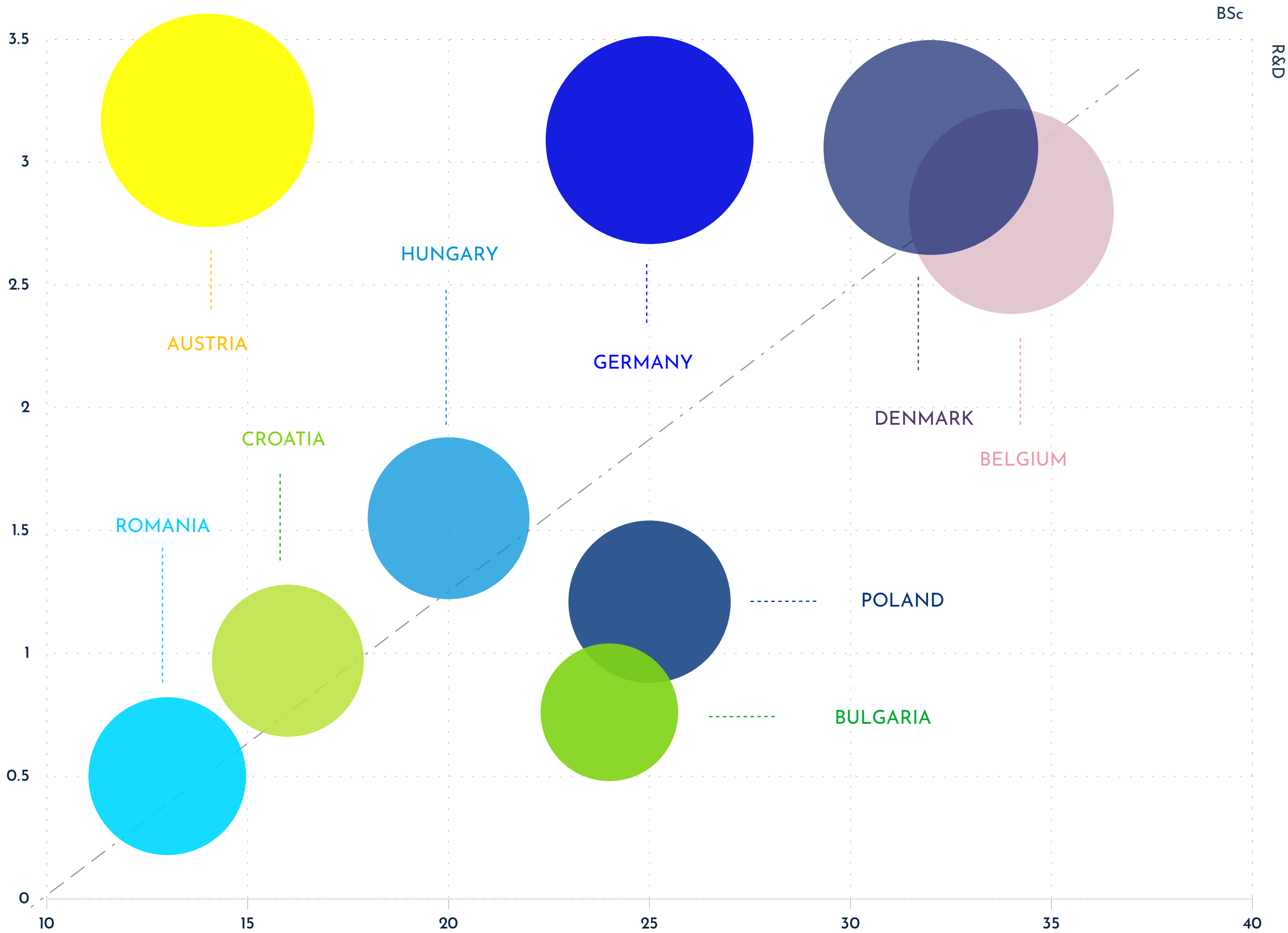
WORLD BANK

That particular environment tended to favour those who had a first-mover advantage : with the market open and unmet demand at every corner, whoever could supply good and services in a particular market could often claim near monopolies in the short term. That, in turn, translated into high profit margins and thus revenue to expand in other markets where competition was still limited. The effect across the economy is to create a lot of domestically-focused companies often spanning multiple industries and markets but not necessarily being truly competitive in any of them. In other words, a lot of big fish in a small pond. In turn, that dynamic translated into lower export competitiveness, relatively low research and development as well as a degree of de-skilling, in particular due to emigration. This is partially reflected in the profile of R&D as well the educational level of the working age population.

37

PERCENTAGE OF THE EU-27 POPULATION CONSIDERED TO HAVE NO DIGITAL SKILLS

EU COMMISSION



A COMBINATION CHART WHERE ON THE VERTICAL AXIS IS THE THE PERCENTAGE OF GDP THAT IS SPENT ON R & D IN A COUNTRY, ON THE HORIZONTAL AXIS PERCENTAGE OF THAT COUNTRY'S WORKING AGE POPULATION THAT HAS A BSc OR ABOVE AND THE SIZE OF EACH THE GDP PER CAPITA OF THAT COUNTRY IN PPP TERMS.

WORLD BANK

That, in turn, aided the continuation of a bank-led model of corporate financing, leaving most of Central and Eastern Europe with relatively underdeveloped equity markets. The net effect, still very much present after many years, has been to produce a set of bank-financed, family-owned, domestically-oriented companies which tend towards uncompetitiveness – at least when compared with those who arose from the export-led, East Asian model at similar levels of development. Those environmental conditions were shared between most former Soviet countries, but as they developed further most began taking their own routes, which is where the heterogeneity in Central and Eastern Europe may be said to have arisen from.

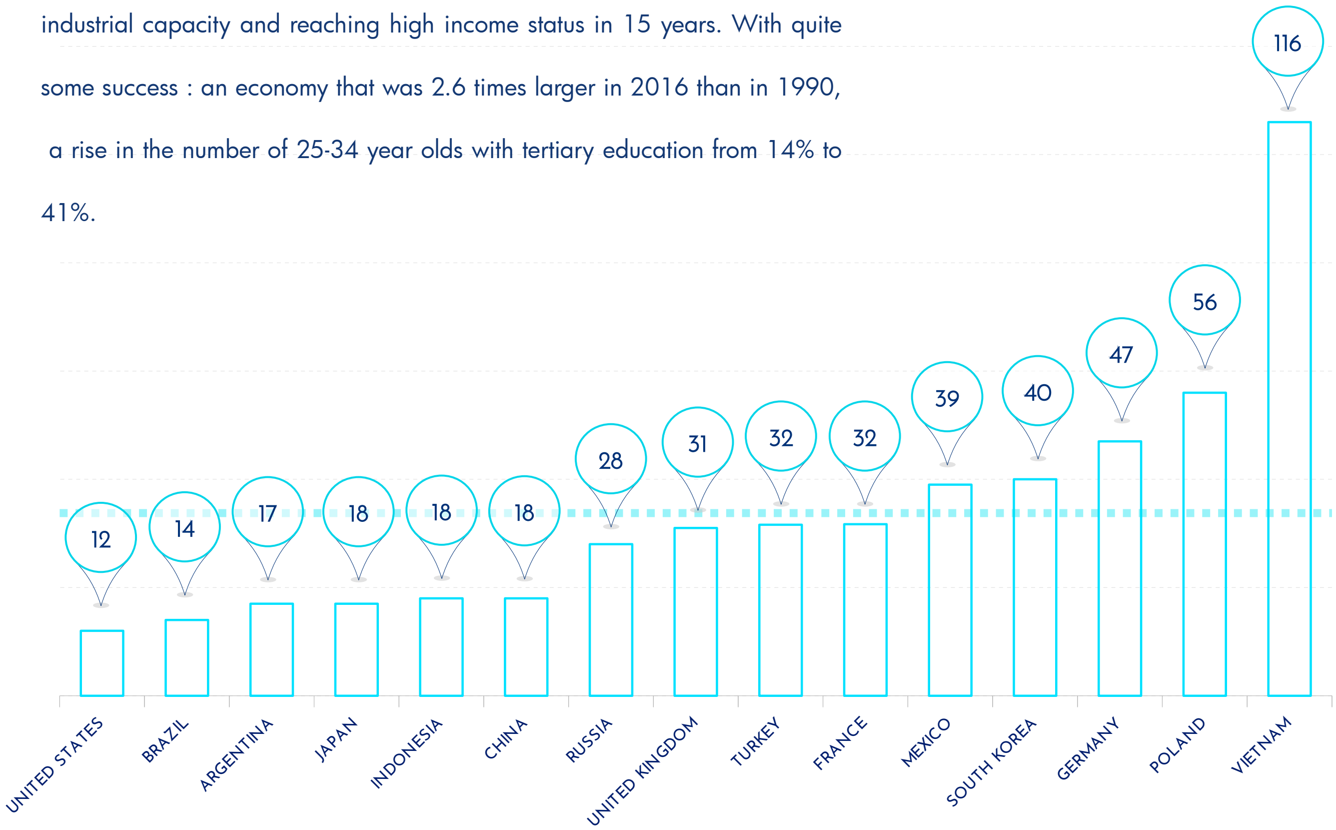
2.6

TIMES THE POLISH ECONOMY WAS LARGER, IN GDP TERMS, IN 2016 WHEN COMPARED TO 1990 LEVELS

WORLD BANK

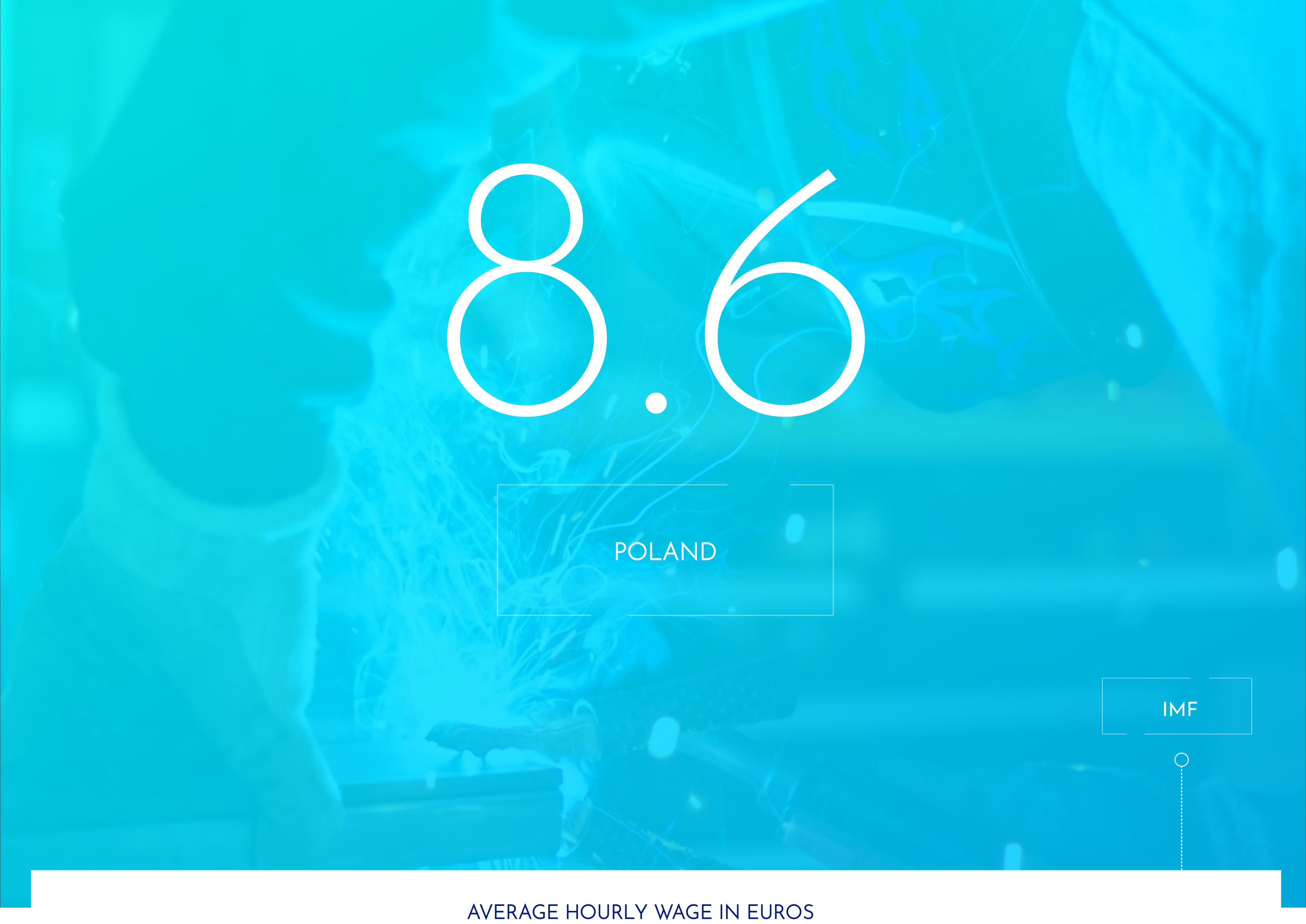
POLAND'S PATH

For example, while Poland can be said to have been in the same situation during the late 1990s, a degree of national strategy, integration into global supply chains meant it took the route of export competitiveness, retaining industrial capacity and reaching high income status in 15 years. With quite some success : an economy that was 2.6 times larger in 2016 than in 1990, a rise in the number of 25-34 year olds with tertiary education from 14% to 41%.



PERCENTAGES OF GDP REPRESENTED BY EXPORTS. EACH BAR'S LEVEL OF FILL REFLECT THE PROPORTION TO WHICH THAT IS BALANCED BY THE LEVEL OF IMPORTS AS A PERCENTAGE OF GDP.. FIGURES ARE FOR 2019.

WORLD BANK



8.6

POLAND

IMF

AVERAGE HOURLY WAGE IN EUROS

25.6

EU-27

Somewhat naturally, when the transition towards export-competitiveness began, those exports were dominated by the same companies which previously thrived in the domestic market. However, other companies soon began to rise, such that the proportion of exports attributed to large companies fell from 80% in 2006 to 52% in 2013.

This success story may be compared to others, such as Romania, Ukraine or Bulgaria, which continued on the path set by the initial parameters. Still focused on the domestic market, the family businesses which rose to prominence in the 1990s often remained around or simply sold to foreign companies looking for local distributors.

The result has been that neither developed in the direction of export competitiveness, becoming quite locked in a still growing but ultimately limited market. In this set, most of the top business families follow the same pattern, of having become great at serving domestic needs but having little foothold outside their respective economies.

That carries a stark reminder to country and business alike, one that East Asian 'superclans' can serve as an positive example. What has been observed in other developing economies of their time – namely Spain, Italy and Portugal in the 1960s to the 1980s – was that success in convergence with the rest of Western Europe can prove illusory. Likewise focused primarily on the domestic market, rapid growth was achieved and gains in productivity observed on the basis of inter-sectoral flows – primarily moving labour from low-productivity agriculture to higher productivity manufacturing and services. But, being focused only on the domestic market and not becoming export competitive also meant that once this shift was completed in an equilibrium with the demand of the domestic market, growth in Total Factory Productivity almost stopped to give way to decades of malaise for country and business.

1.5

PERCENTAGE OF EMPLOYEES IN ROMANIA WHO REPORT THAT THEY ARE ENGAGED IN A PROFESSIONAL COURSE PRIVATELY

WORLD BANK

15

PERCENTAGE OF MANUFACTURING EXPORTS WHICH ARE REGARDED AS HIGH-TECHNOLOGY ACROSS THE EU-27

WORLD BANK

18

PROPORTION OF THE INCREASE IN CHINA'S GDP BETWEEN 1978 AND 2007 WHICH IS ATTRIBUTABLE TO INCREASES IN LABOUR SUPPLY

WORLD BANK


3
PERCENTAGE OF ITALIAN CITIZENS WHO EXPERIENCED INCOME GROWTH BETWEEN 2004 AND 2014
MCKINSEY

The East Asian family businesses which rose through exports had a more difficult time, having to produce at higher standards and absorb technology faster. But it also meant a faster technological catch-up, investment in R&D, and a productivity boom that continued beyond the comforts of middle income. Quite simply, the East Asian export oriented model generated and depended on research and development as much as cheap labour for export competitiveness and, in retrospect, it made all the difference. That proved more sustainable an engine of growth than the domestically-oriented European model, at least to some extent. Therein a cautionary tale for Central and East European economies and domestically oriented family businesses alike, namely that as the transition ends, productivity and average real incomes stagnate – and do so quite fast, and quite constantly afterwards. Over-adaptation to that domestic market may look unwise down the line as growth begins slowly while financing for foreign expansions becomes scarcer.

33

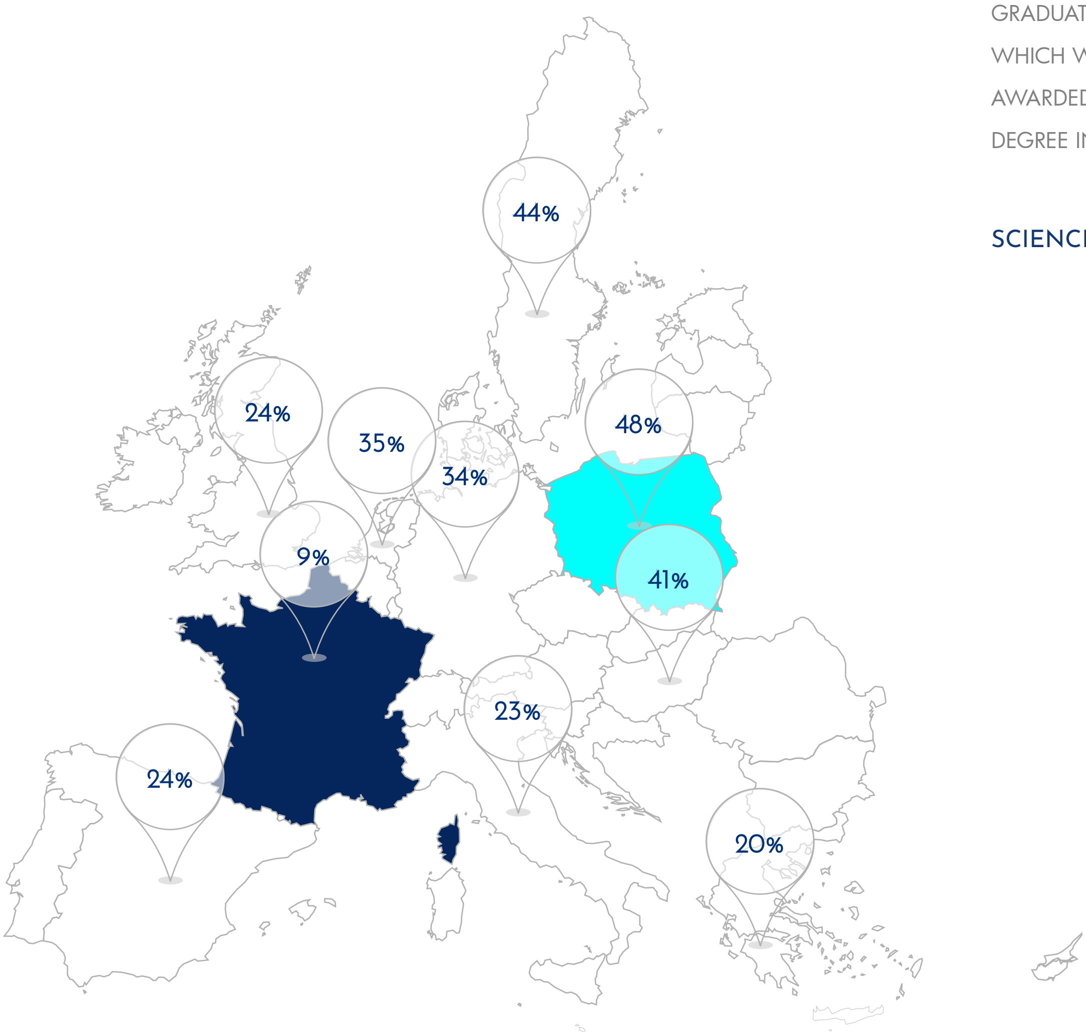
NUMBER OF TIMES R&D SPENDING HAS INCREASED IN CHINA SINCE 1990

CSIS

23

PROPORTION OF STEM GRADUATES GLOBALLY WHICH WERE AWARDED THEIR DEGREE IN CHINA

SCIENCE BOARD



PERCENTAGE OF PEOPLE WHO AGREE WITH THE STATEMENT THE THEIR CHILDREN'S FUTURE WILL BE BETTER THAN THE PAST

PEW RESEARCH

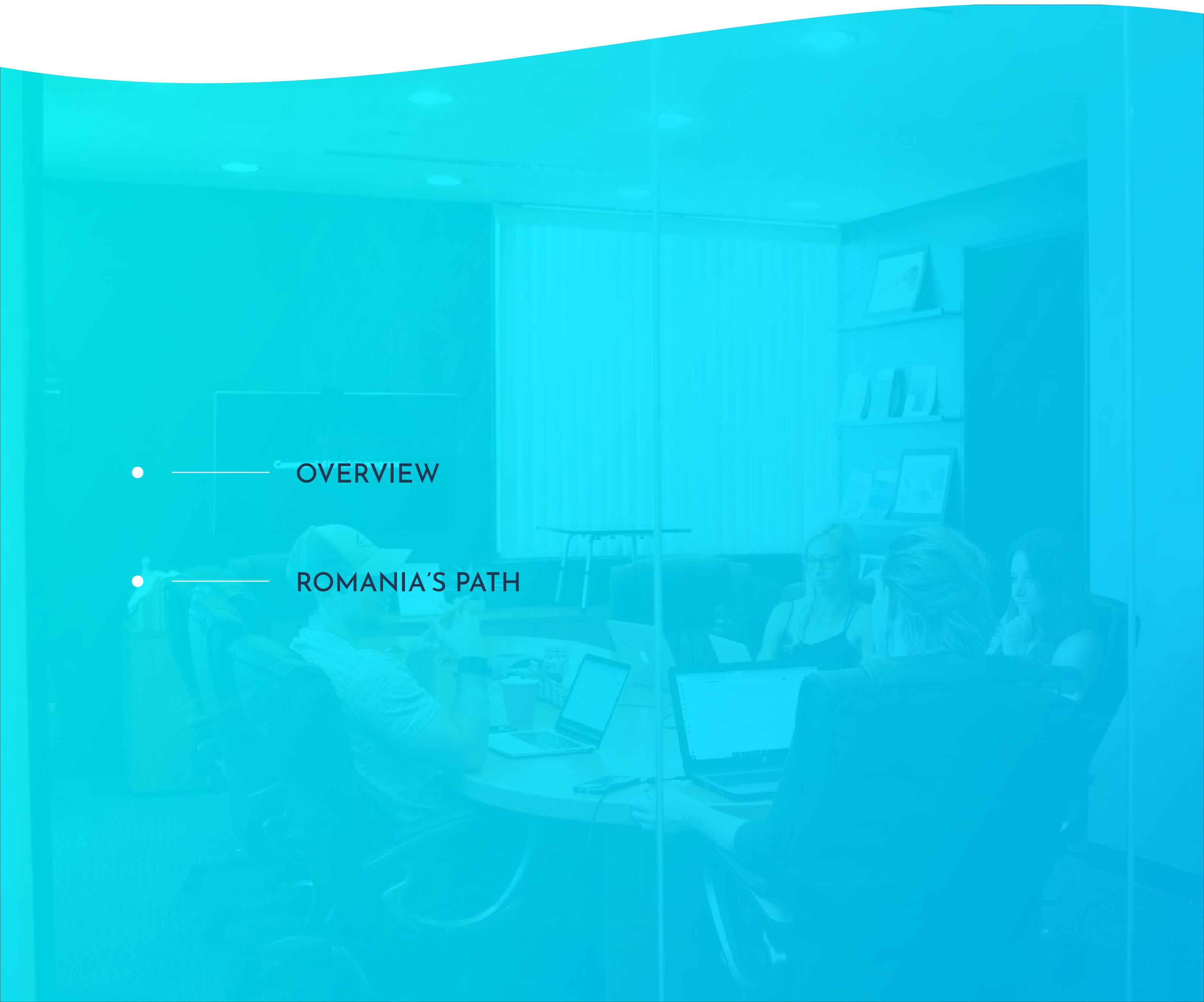
9

PERCENTAGE OF GLOBAL GDP OF COMBINED GDP PROJECTED TO 2050 OF THE EU-27 COUNTRIES, PPP TERMS

PWC

ROMANIA'S SITUATION

A look at the Romanian context in terms of business development and wealth generation.



- OVERVIEW
- ROMANIA'S PATH

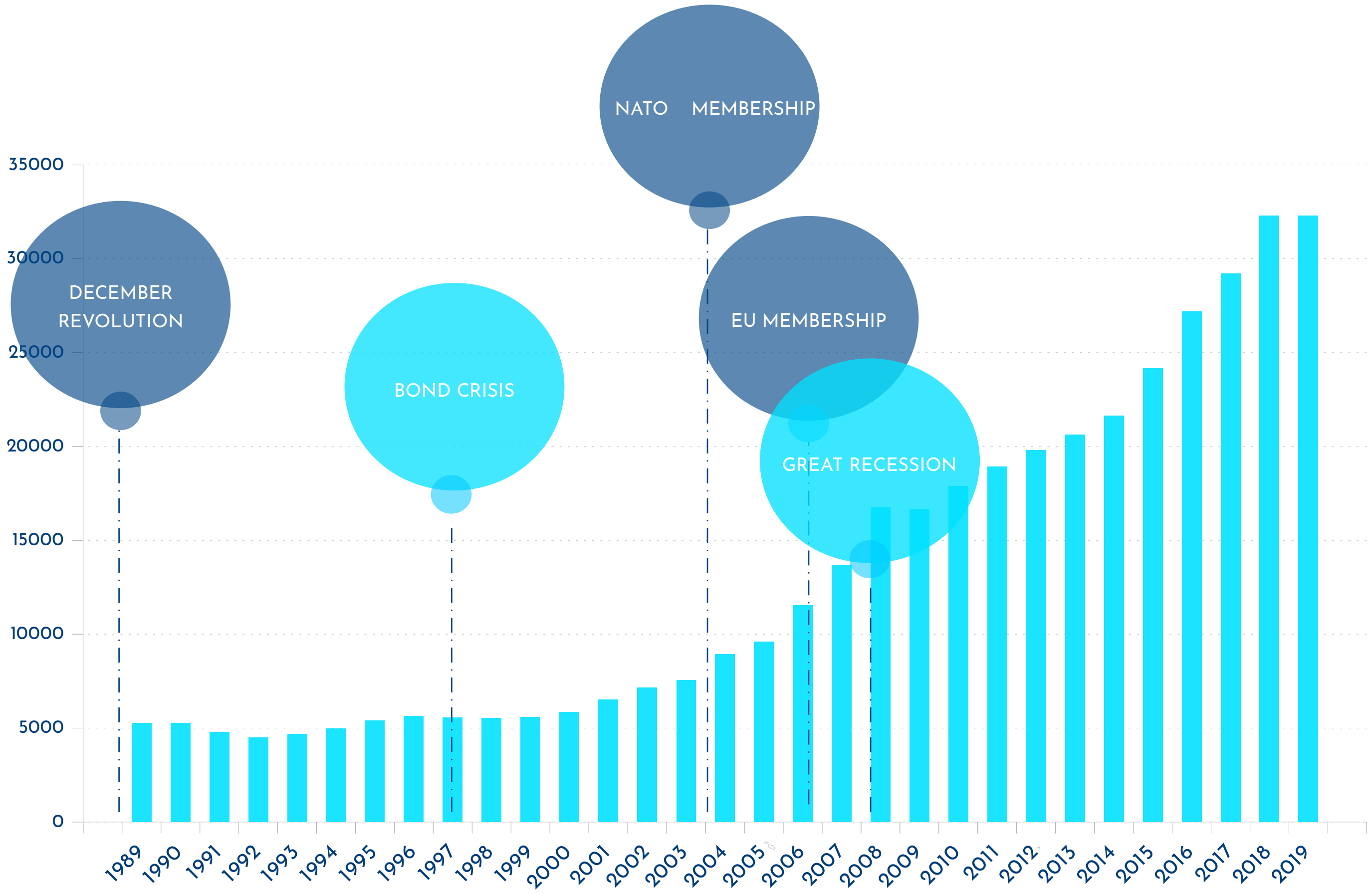
OVERVIEW

Romania, and by extension Romanian family business, may be seen as a main example of those who took the second post-Soviet path. The country faced one of the worse, in quantitative economic terms, transitions from communism in the early 1990s, with double digits falls in GDP and significant disruption. While the situation ameliorated somewhat in the course of the decade despite significant social unrest, GDP per capita remained both almost stagnant as well as well below European averages. During this time, the most important fortunes were also made, often quickly and based less on expertise and more on access to scarce capital, political connections to provide it and, in the second half, expansive marketing practices into what remained a 'terra incognita' of consumer products. Later, as NATO and EU membership became discussed, GDP per capita did begin to rise and the economy became significantly more formalised.

46

PERCENTAGE OF THE ROMANIAN POPULATION WHICH IS CLASSED AS RURAL, 2021

WORLD BANK



ROMANIAN GDP PER CAPITA IN PPP TERMS

WORLD BANK

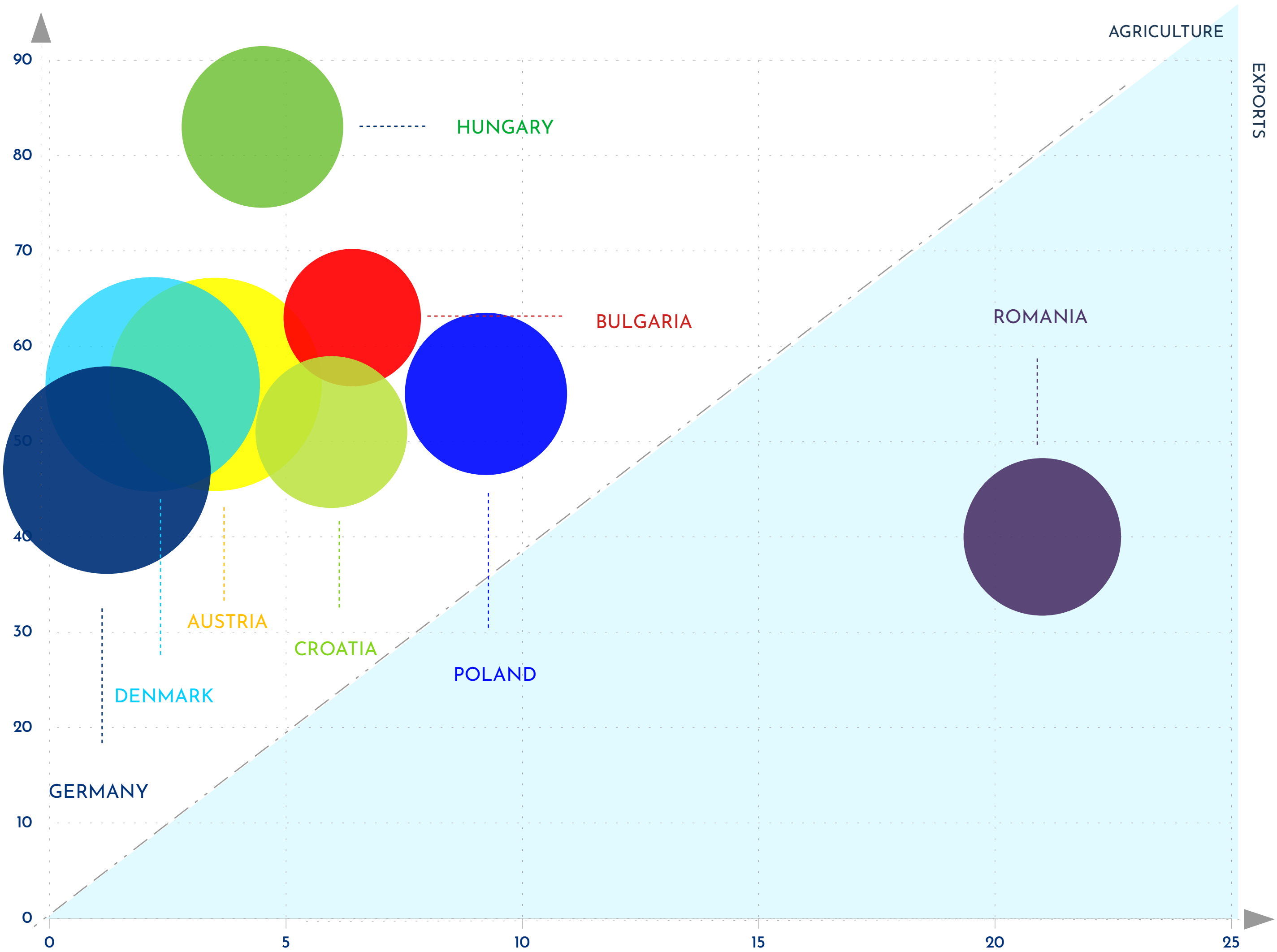
Since, growth has remained both steady and, at least in purely quantitative terms if not in terms of quality, well above European averages. During this time, some the initial crop of magnates and family businesses either sold to foreign buyers or at times dwindled in the face of foreign competitors.

Nevertheless, a dichotomy with Poland, while strictly-speaking false, may nevertheless prove illustrative. While find themselves with similar parameters towards the end of the 1990s, Poland quite began integrating into Western supply chains as well as courting allies both West and East. Despite the issue that entry into formal legal structures such as the European Union effectively limit technological convergence through weak patent laws and thus would permit higher levels industrialisation, as was seen in East Asia, Poland nevertheless succeeded in retaining its industrial capability through exports.

7.1

PERCENTAGE OF ROMANIAN FIRMS SURVEYED WHICH REPORT SPENDING ON RESEARCH AND DEVELOPMENT, 2020

WORLD BANK



WORLD BANK

A COMBINATION CHART WHERE ON THE VERTICAL AXIS IS THE THE PERCENTAGE OF GDP THAT ACCOUNTED FOR BY THE EXPORT OF GOODS AND SERVICES IN A COUNTRY, ON THE HORIZONTAL AXIS THE PERCENTAGE OF THAT COUNTRY WHICH IS EMPLOYED IN AGRICULTURE AND THE SIZE OF EACH THE GDP PER CAPITA OF THAT COUNTRY IN PPP TERMS.

This in turn allowed Poland to maintain and develop its manufacturing base at above Soviet levels, which in turn allowed the highest productivity raising shift to occur in the Polish economy, namely moving labour from low productivity agriculture to high productivity manufacturing, as in the East Asian model.

36

PERCENTAGE OF THE POPULATION WHICH IS CONSIDERED BELOW THE POVERTY LINE OR AT RISK OF POVERTY, IN 2018

WORLD BANK

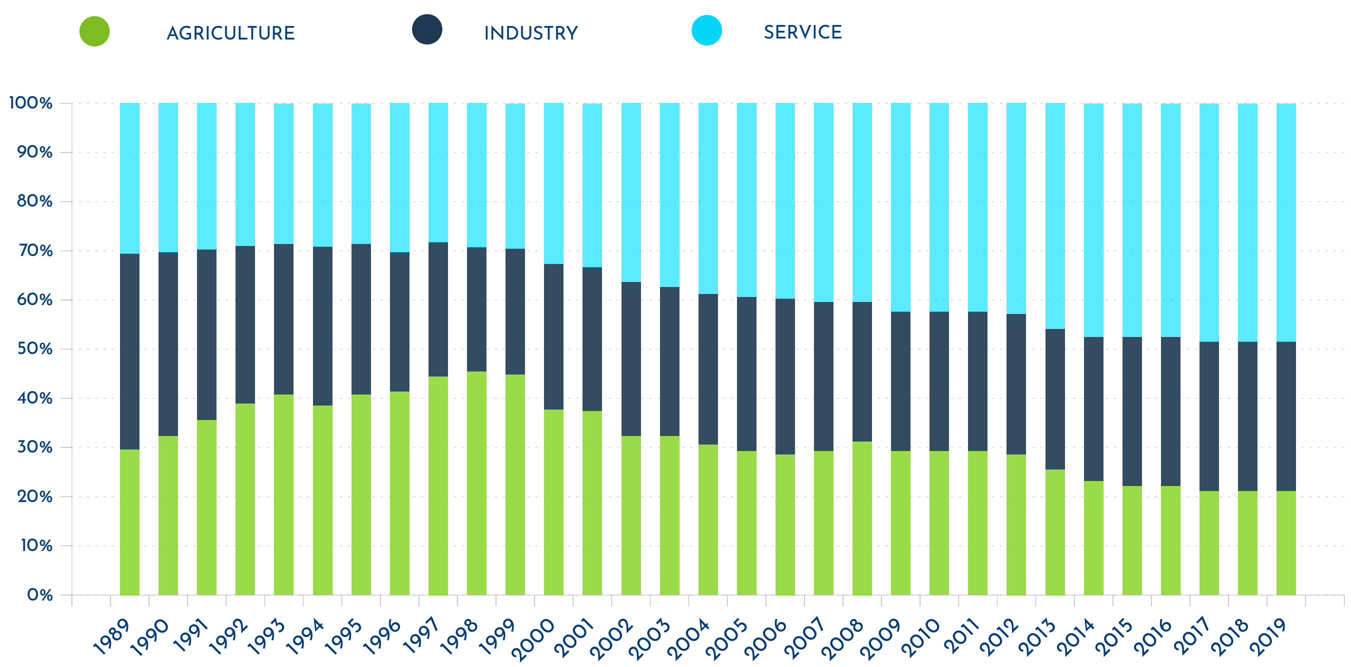
ROMANIA'S PATH

Lacking a national strategy for development, most things simply flowed towards the point of least resistance. In this case, that was domestic demand, often of imported goods, and the service economy. To an extent it did provide an avenue for growth, but it also effectively left almost half of the population in a state of deep underdevelopment, often tied to an agricultural sector which didn't provide well paying jobs or jobs at all. This has resulted in a rate of 36% of the population which may be consider either poor or at risk of poverty, with only 65% of the population even having access to banking to begin with. The social cost of this passive choice has been enormous by most understanding of the term.

65

PERCENTAGE OF THE ROMANIAN POPULATION WHICH IS CLASSED AS HAVING A BANK ACCOUNT

WORLD BANK



COMPOSITION OF WORKFORCE EMPLOYMENT BY SECTOR

WORLD BANK

30

PERCENTAGE OF ROMANIAN PUPILS WHO UNDERPERFORMED IN ALL PISA CATEGORIES

OECD

This in turn has led to longer-term scarring effects in the economy, in particular in terms of the degree to which the rural population has access to what may be regarded as the minimal education required to make a transition towards a modern economy.

Quite simply, close to half of Romanian pupils are regarded as functionally illiterate, the vast majority of which may be found in rural areas. This population, close to half of the future workforce, ultimately have little to offer to future labour markets.

This in turn limits the degree to which current companies have access to the talent needed to actually become export competitive. The result has been an economy – and a set of family businesses at the top of it – which reflect these parameters : construction and furniture, reflecting the tremendous amount of cash flowing back and into real estate from sometimes questionable activities, general household goods and basic utilities such as telecoms – over and above the initial crop of businesses developed in the 1990s.

13

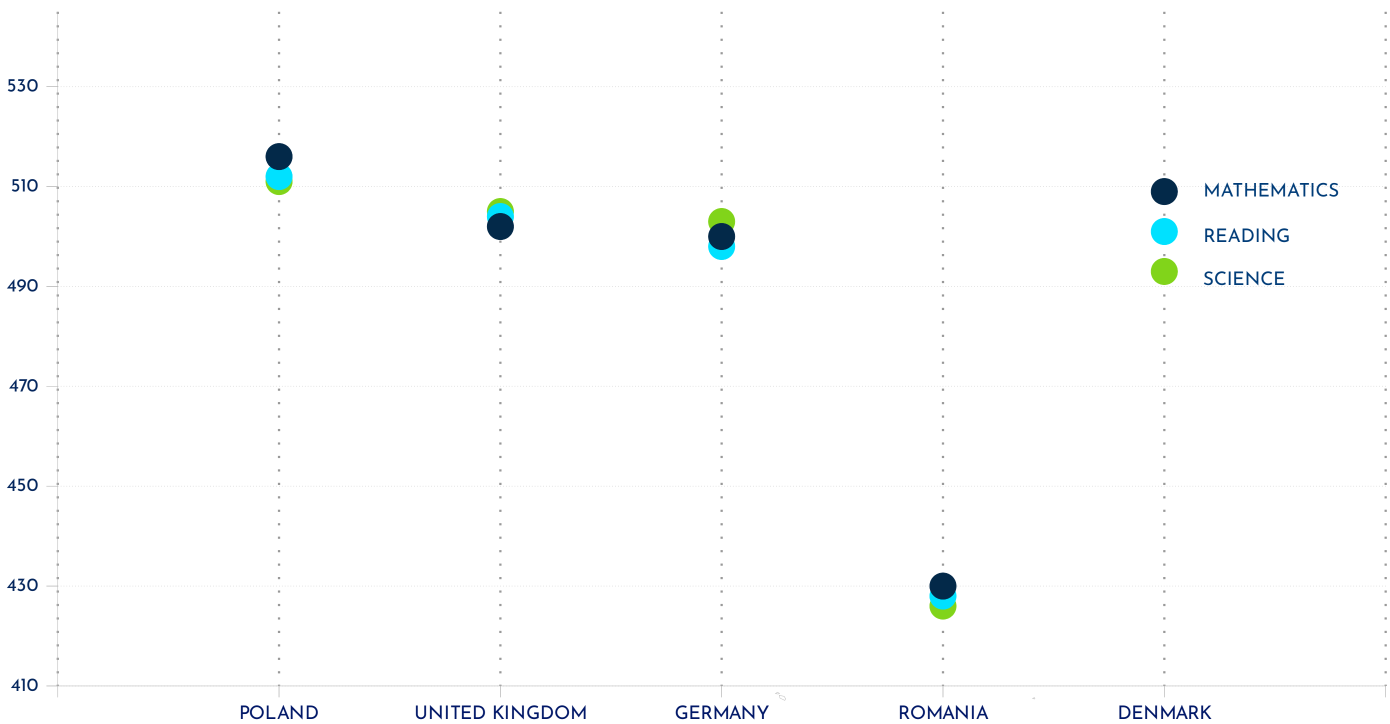
PERCENTAGE OF THE ROMANIAN WORKFORCE OVER THE AGE OF 25 WHICH IS CLASSED AS HAVING COMPLETED TERTIARY EDUCATION

WORK BANK

2.7

BILLION EUROS TRANSFERRED BY THE ROMANIAN DIASPORA BACK INTO ROMANIA, IN 2019

EUROSTAT



PISA SCORES, 2018, SELECTED COUNTRIES

OECD

631

SOUTH KOREA

HSBC

NUMBER OF ROBOTS INVOLVED IN INDUSTRY PER 10,000 EMPLOYEES, 2018

346

GERMANY

Needless to say, this bodes ill for Romania's top business families and the East Asian model again serves as a positive example.

Foremost, they are almost wholly dependent on an economy whose prospects are limited, at best. With a poorly educated workforce, little research and development, one of the most stark cases of population ageing globally, the Romanian market represents an almost Pyrrhic victory. By contrast, East Asia's 'superclans' often built fortunes by competing directly with the top Western companies – first by copying perhaps, but often quickly surpassing their rivals in both production cost and research. Their respective economies were often as much shaped by this as by direct government policy, first by providing an avenue out of rural poverty for millions and then by providing an incentive for study through the research and managerial strengths which their respective companies needed to compete in global markets.

Quite simply, the East Asian economic miracle can often be traced, at least partially, to a fairly limited number of family businesses. It may be said that there's little in the face of Romania's top family businesses acting in the same manner, the aim of export competitiveness being the first step and membership of the European single market a self-evident opportunity.

80

PERCENTAGE OF CEE ECONOMIC GROWTH WHICH IS SEEN AS DRIVEN BY CONSUMPTION, IN 2015

MCKINSEY

70

PERCENTAGE OF PEOPLE IN ADVANCED ECONOMIES WHO ARE ESTIMATED TO HAVE EXPERIENCED NO INCOME GROWTH BETWEEN 2005 AND 2014

MCKINSEY

WEALTH TOPOLOGY

A look the topology of wealth distributions in selected Central and Eastern Europe countries, with an overview of the countries' top business families.

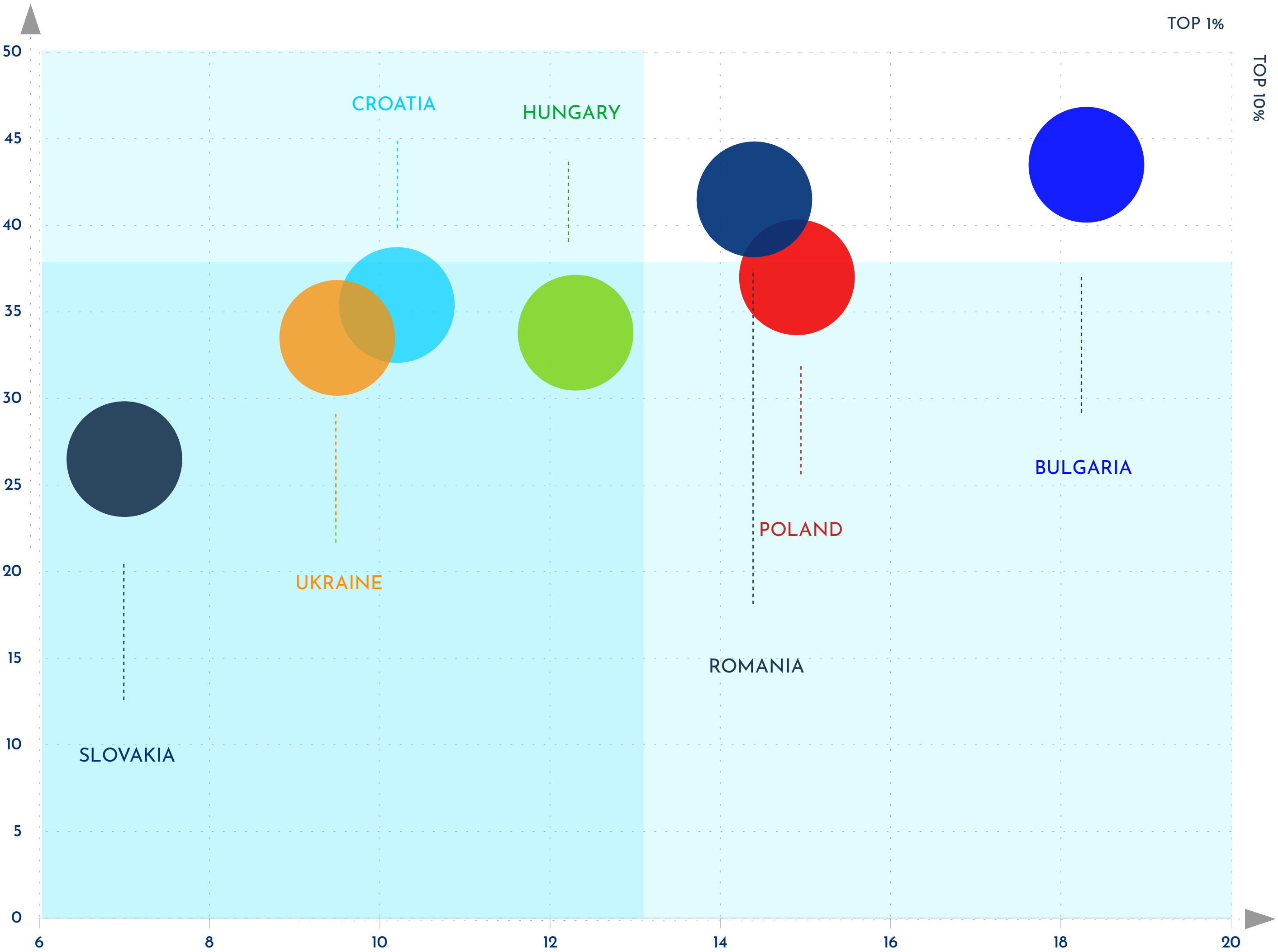
OVERVIEW

Broadly-speaking, CEE wealth distributions have two aspects : temporal and geographic. Temporally, business families may be differentiated between those who've built fortunes in the immediate aftermath of Soviet collapse, often larger than life personalities with horizontally-integrated conglomerates, those who've built fortunes in the context of the 2000s and 2010s consumption-led economic boom, often in housing-correlated sectors or consumer middle-class trappings, as well as the outliers who've often come from the technology sectors and tend to be significantly more low key. Geographically, we may differentiate on two gradients : percentage of national income actually recorded for tax purposes and its distribution in the population.

37

AVERAGE OF NATIONAL INCOME EARNED BY THE TOP 10% ACROSS EASTERN EUROPE, REPORTED INCOME

WID



A COMBINATION CHART WHERE ON THE VERTICAL AXIS IS THE THE PERCENTAGE OF NATIONAL INCOME EARNED BY THE TOP 1% OF EARNERS AND ON THE HORIZONTAL AXIS THE PERCENTAGE OF NATIONAL INCOME EARNED BY THE TOP 10% OF EARNERS. EACH COUNTRY-SIZE HAS BEEN HELD CONSTANT.. EASTERN EUROPEAN AVERAGES ARE DELINEATED IN LIGHT BLUE.

WID

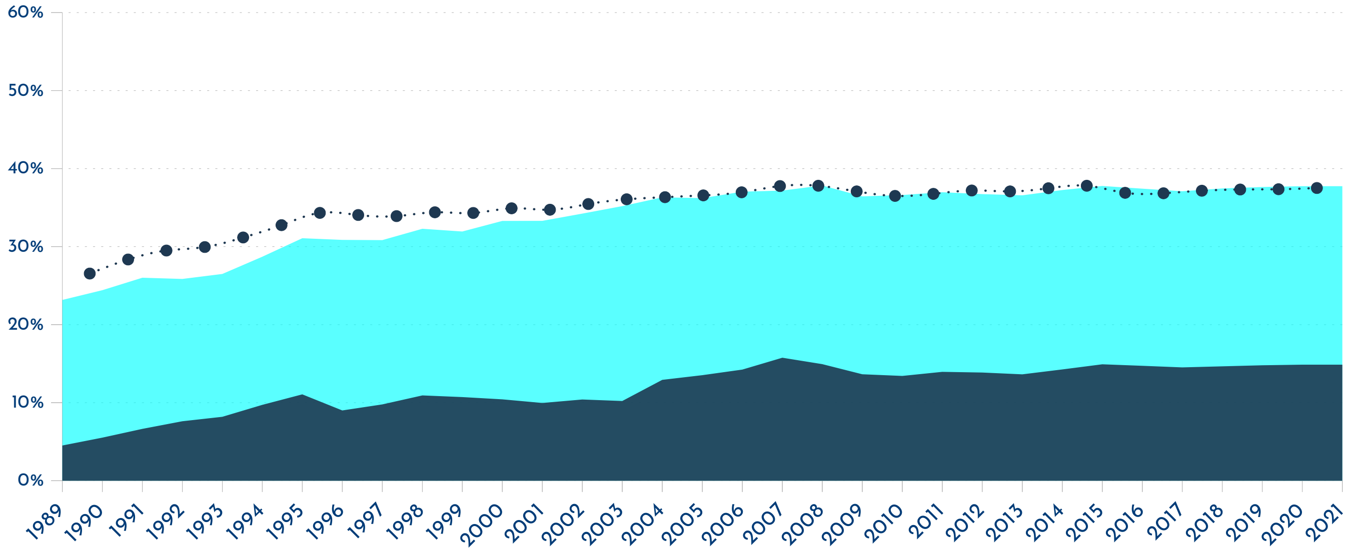
POLAND

CONTEXT

The great success story of transitions from communism, the Polish economy both took most opportunities available to it in its historic context and avoided most traps others have fallen into. More export oriented than the German economy, with falling income inequality alongside rising educational achievement, the Polish economy has produced a notable business class that successfully holds its own on the world stage.

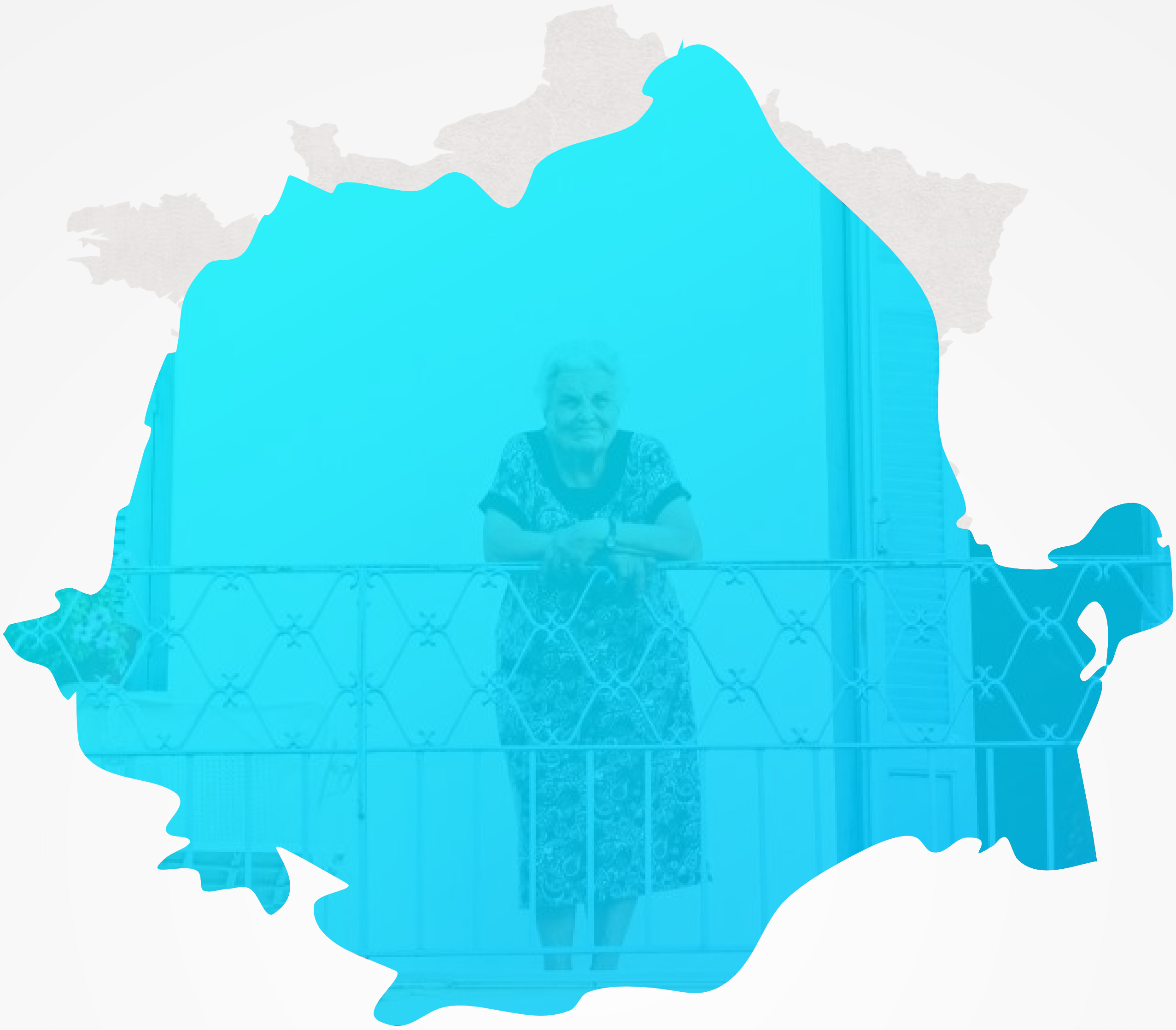
OVERVIEW

In constraint with its slight distinctness among CEE economies, Poland presents a fairly typical business class at its upper levels – albeit it must be qualified that, atypically, it has a significant number of exporters at a mid level and below which makes distributions somewhat more equal. It is also one the few economies in Central and Eastern Europe boasting what may one of the first successful 'supercan' in the areas, namely the Kulczyk family – composed of the late Jan Kulczyk, who followed a fairly standard post-Communist domestically-oriented conglomerate model with interests ranging from oil refining to telecommunications, as well as his son, Sebastian Kulczyk and daughter, Dominika Kulczyk. They are quickly followed by fairly typical entrepreneurs such as the Solowow family, highly diversified but whose wealth is polarised in housing-related industries such as ceramics, the Czarnecki family, with a wide array of successful banking and finance companies, as well as the Solorz-Żak family, with another conglomerate model focused primarily on broadcasting as well as energy generation.



PERCENTAGES OF NATIONAL INCOME EARNED BY THE TOP 1%, IN BLUE, AND TOP 10%, IN LIGHT BLUE. THE DOTTED LINE IS THE MOVING AVERAGE ACROSS EASTERN EUROPE FOR THE 10%.

WORLD INEQUALITY DATABASE



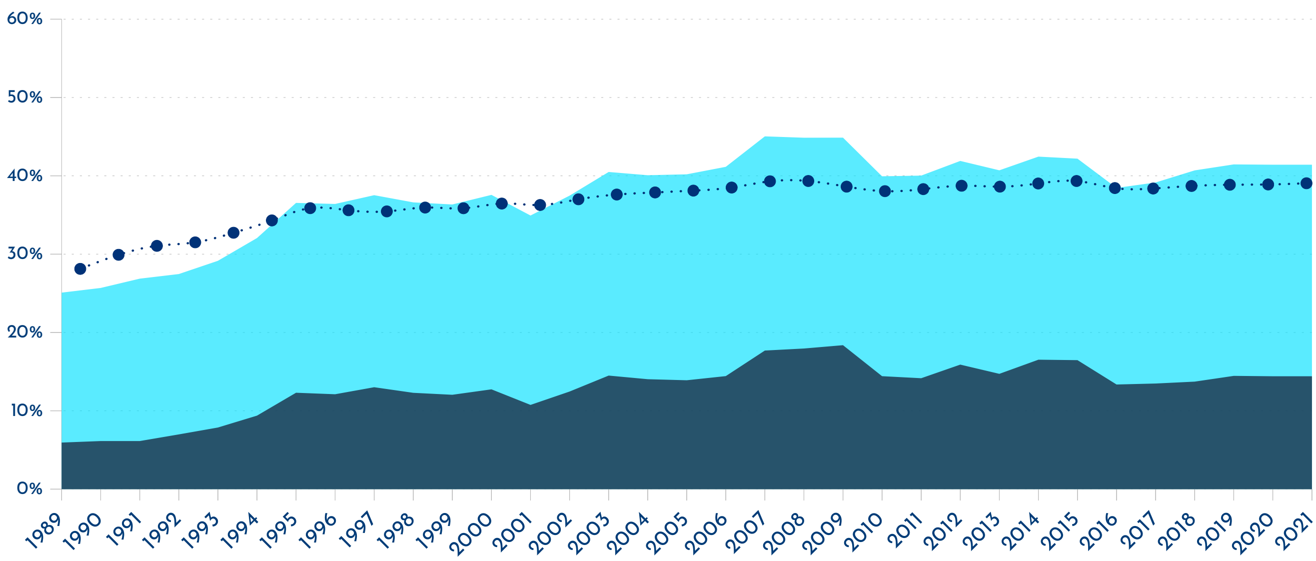
ROMANIA

CONTEXT

The Romanian economy may be marked by the de-industrialisation path taken, with a heavy emphasis on a consumption-led economy, growth in the service sector and a political focus on integration into Western political structures. This is reflected in a highly divergent rural-urban sets of outcomes, one of the highest rates of emigration relative to population size and a domestically-oriented, consumption-led economy with few exports but also one of the highest rates of home-ownership in the world as a legacy of Communism.

OVERVIEW

The Romanian business class, particularity its upper echelons, are reflections of this. The top remains dominated by the initial post-Soviet business class, often overseeing conglomerate business models in multiple sectors and financed primarily by debt capital as well as internal capital. In sectoral terms, one may differentiate between those who made their fortunes in the immediate post-Communist context and those who rose in the context of the 2000s as incomes began converging with Western Europe. The first set is dominated by the Tiriac family with a sprawling financial empire worth over EUR 1.5 billion, the Niculae family, with a heterogeneous empire worth near EUR 700 million and the Stoica family, which leads in industrial transport with a fortune of over EUR 500 million. The second set may be seen as a consequence of the rising parameters of the initial conditions, namely the Paval family who own Dedeman, the market leader in home refurbishments, and the Teszári family, which rose to prominence offering broadband and telecommunications. As outliers, there are two software companies : the Dines family, who own UiPath and are considered the wealthiest family in Romania, alongside the Talpes family, who own Bitdefender.



PERCENTAGES OF NATIONAL INCOME EARNED BY THE TOP 1%, IN BLUE, AND TOP 10%, IN LIGHT BLUE.
THE DOTTED LINE IS THE MOVING AVERAGE ACROSS EASTERN EUROPE FOR THE 10%.

WORLD INEQUALITY DATABASE

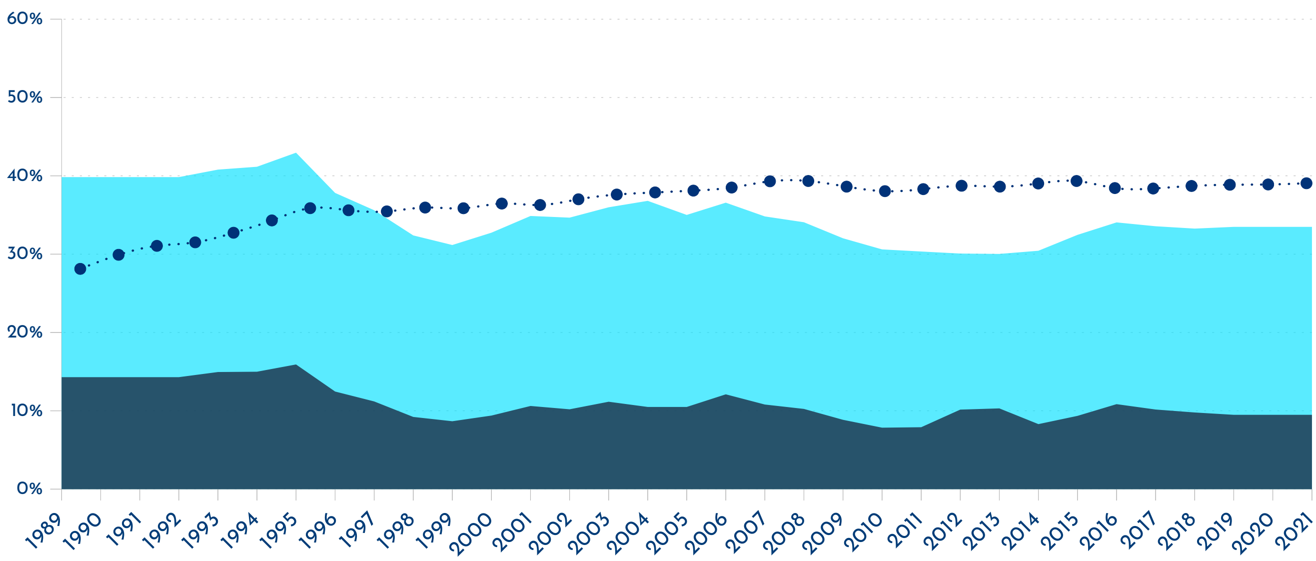
UKRAINE

CONTEXT

If Poland may be described as Central and Eastern Europe's most visible success story in terms of transitions to a market economy, Ukraine stands in contrast as an economy which has had everything wrong go for it. Its main threats, premature de-industrialization and corruption, came to pass, its main opportunities, export competitiveness and education did not, while its strengths, access to lower energy prices making manufacture highly price competitive were not utilised. This has resulted in a wealth polarization which reported income doesn't fully capture as well as a business environment which isn't always for the faint of heart.

OVERVIEW

The result has been a somewhat volatile business class which follows the 1990s model almost entirely, which is to say dominated by conglomerate model business, horizontally spread out and focused primarily on domestic market share rather than exports. The top of the wealth ranking are dominated by steel producers, understandably in the context in which Ukraine had preferential access to low energy prices for most of its post-Soviet history. These are the Akhmetov family, with over USD 7.5 billion in assets, the Pinchuck family with assets estimated at over USD 2.5 billion, and the Novinsky family, whose assets extent to almost 1.5 billion. Additionally, related industries dominate, most notably in the Zhevago family's mining interests. As outliers to some extent are Ukrainian-Israeli businesspeople, focused on banking, namely the Kolomoyskyi family and the Boholyubov family, whose assets extent to nearly USD 2 billion each as well as the former president of the country, whose family is estimated at having over USD 1.5 billion in assets.



PERCENTAGES OF NATIONAL INCOME EARNED BY THE TOP 1%, IN BLUE, AND TOP 10%, IN LIGHT BLUE.
THE DOTTED LINE IS THE MOVING AVERAGE ACROSS EASTERN EUROPE FOR THE 10%.

WORLD INEQUALITY DATABASE

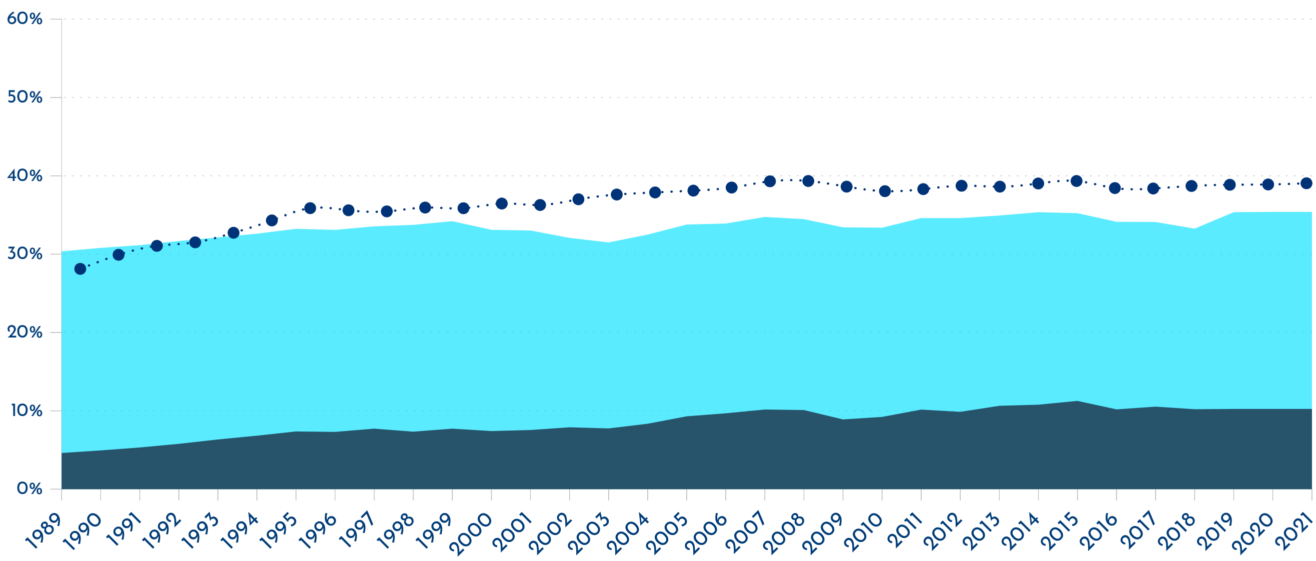
CROATIA

CONTEXT

The Croatian economy is another minor success story across the Central and East European region, alongside the likes of Slovakia, in the sense that it achieved high income status, has a fairly wide income distribution across the population, has successfully generated a second wave business class from consumer industries and does relatively well both in terms of debt ratings, business environment – being 51 on the World Bank's East of Doing Business Index - and economic growth, despite being affected by common ills across CEE economies, such as brain drain, emigration and incomes which remain below European Union averages.

OVERVIEW

The Croatian business class, primarily composed of second wave businesspeople which rose during the late 1990s and 2000s consumption-led economic boom, are highly heterogeneous across sectors but primarily reflect exposure to the aforementioned rise in incomes and consumer spending, being essentially correlated with middle class development and reflecting this. The rankings themselves are dominated by consumer products and may be regarded as notable due to a larger than average number of companies actually being listed as public companies on stock exchanges – in itself a remarkable achievement. On top is the Todorić family, whose wealth of an estimated EUR 600 million is principally tied with retail, food and beverages. Closely following are the Rajic family, with previous interests in agricultural production, the Grgic family's almost EUR 200 million focused on banking, the Cuccurin family's EUR 140 million diversified across real estate, tobacco and tourism as well as the Zubak family's automobile fortune of about EUR 110 million



PERCENTAGES OF NATIONAL INCOME EARNED BY THE TOP 1%, IN BLUE, AND TOP 10%, IN LIGHT BLUE.
THE DOTTED LINE IS THE MOVING AVERAGE ACROSS EASTERN EUROPE FOR THE 10%.

WORLD INEQUALITY DATABASE

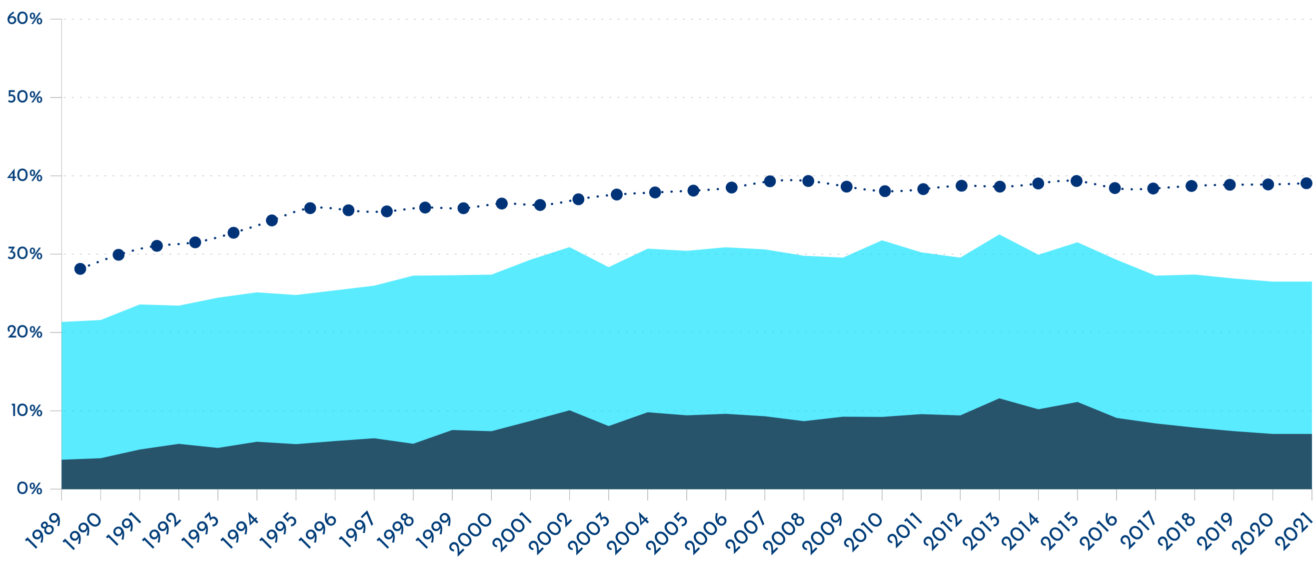
SLOVAKIA

CONTEXT

The Slovakian economy was never as large as Poland's and thus never served as a notable example for Central and East European countries but is nevertheless very much notable by avoiding most of the pitfalls that CEE countries fell at some point or another. After an amicable divorce out of the former Czechoslovakia, it did not follow the route of rapid privatisation producing illicit wealth, nor did it become the preserve of a debt-financed, domestically oriented business class where patronage networks trumped competitiveness. 45 on the World Bank's Ease of Doing Business Index, Slovakia is another CEE success story, however small compared to some of its neighbours

OVERVIEW

The upper echelons of the Slovak business class may be regarded as notable by primarily coming from the second wave of wealth generation in Eastern Europe, namely the 2000s boom in incomes and economic growth, rather than the first wave of privatisations and winner-takes-all markets which spawned the typical sprawling conglomerates often observed. While poverty remains an issue, as it does across Eastern Europe, and this issue is voiced by civil society and political parties alike, economic growth nevertheless led to a general rise in incomes. That rise was enough to support a domestically created business class of the second wave, exposed both to public pressure as well as government institutional workings, perhaps reflected in the degree to which it seeks public goodwill and Slovakia's far more equitable wealth distribution relative to other CEE countries and East European averages. It is is dominated by real estate, specifically the Chrenko family's EUR 650 million empire, and investments, notably the Kůšik family's EUR 420 billion fortune as well as Slovakia's own budding 'superclan', the father and son team of Jozef and Patrik Tkáč whose assets stand at EUR 380 million



PERCENTAGES OF NATIONAL INCOME EARNED BY THE TOP 1%, IN BLUE, AND TOP 10%, IN LIGHT BLUE.
THE DOTTED LINE IS THE MOVING AVERAGE ACROSS EASTERN EUROPE FOR THE 10%.

WORLD INEQUALITY DATABASE

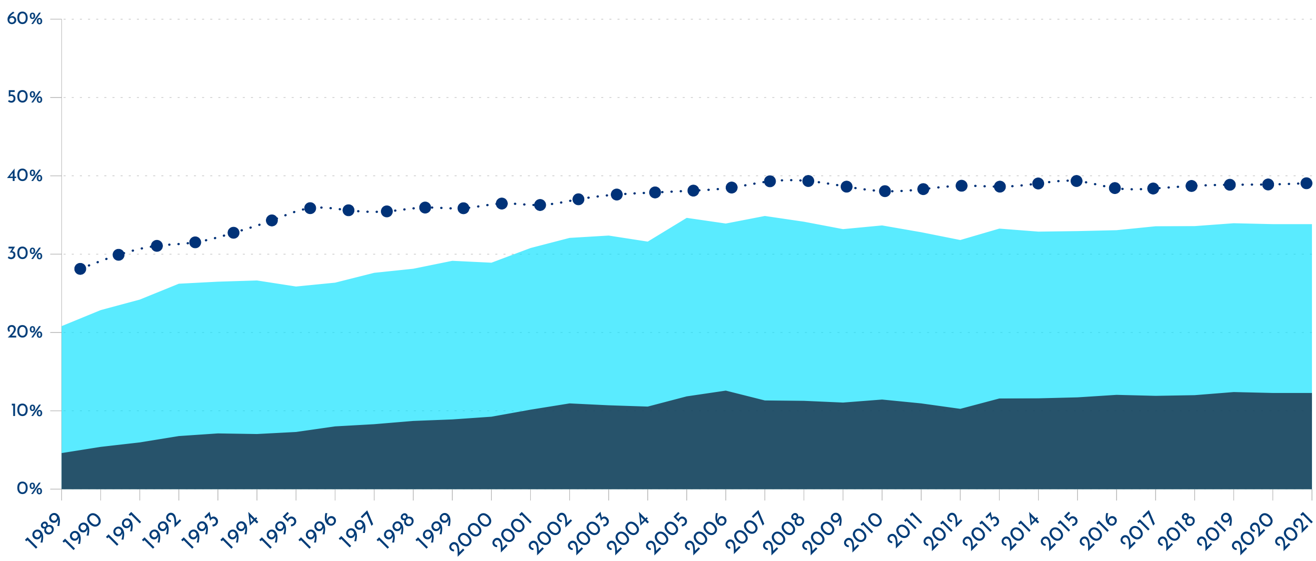
HUNGARY

CONTEXT

The Hungarian economy in part reflects its history as both at the centre of Europe and too fractured to remain one of the great powers of Europe. Highly geographically diversified due to its populations outside its post-Trianion borders it utilised this, as well as its highly successful American diaspora, to attract almost a third of FDI into Eastern Europe. This is turn created a fairly open, export-oriented economy with links across its neighbourhood despite relative stagnation in incomes over the past decade.

OVERVIEW

The Hungarian business class, in particular its upper levels, reflect this 'diaspora with a country' model. There are actually more Hungarian billionaires outside of Hungary than within its post-Trianion borders and links with these successful Hungarians have always been pivotal to the country's post-Soviet growth and development, reflected in its highly heterogeneous industries of its business class : while most CEE elites can be seen as a reflection of initial domestic parameters, the Hungarian one is a reflection of taking every small opportunity available and at times "swimming up the river". Domestically, the Csányi family is noted in banking, with almost EUR 1.5 billion in assets, the Demján family in real estate, with over EUR 500 million in assets, the Széles family in transport, with just under EUR 500 million in assets and the Bige family in chemicals, with almost EUR 400 million in assets. Most notable is the Hungarian diaspora. This includes Thomas Peterffy, with almost USD 20 billion in investments, the Schwartz family (also known as Soros) with an estimated USD 8 billion in investments, the Simonyi family with USD 2 billion from IT as well as the Udvar-Házy family with almost USD 4 billion in finance.



PERCENTAGES OF NATIONAL INCOME EARNED BY THE TOP 1%, IN BLUE, AND TOP 10%, IN LIGHT BLUE. THE DOTTED LINE IS THE MOVING AVERAGE ACROSS EASTERN EUROPE FOR THE 10%.

WORLD INEQUALITY DATABASE

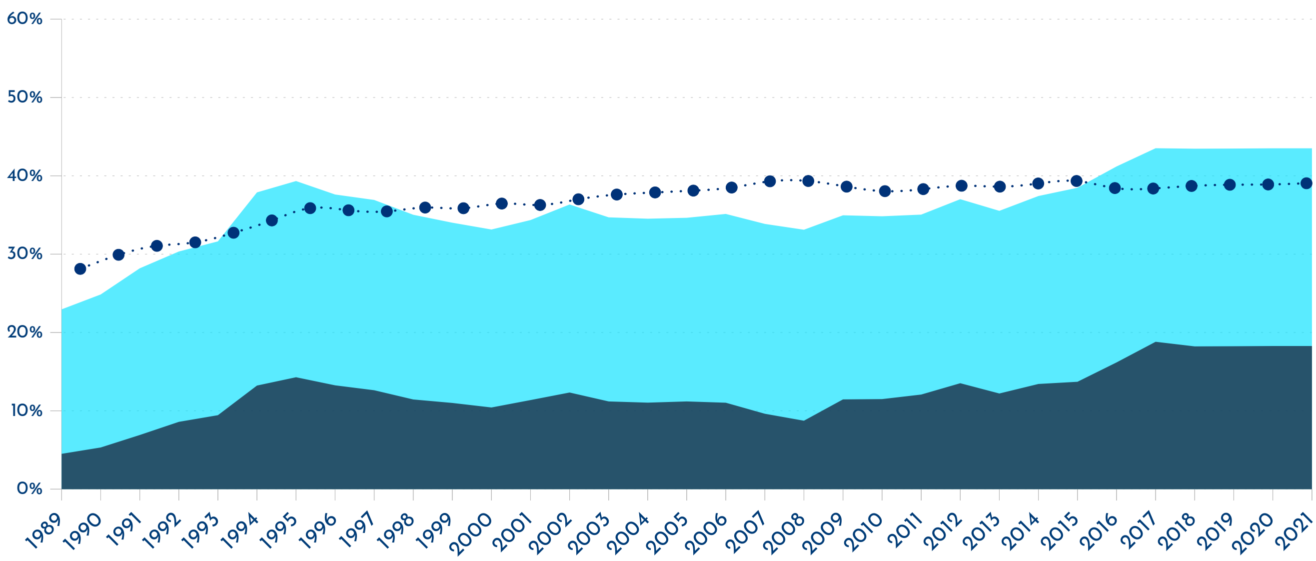
BULGARIA

CONTEXT

The Bulgarian economy, like its neighbouring Romania's, remains in a partial transition from Soviet times, with a highly tumultuous 1990s giving way to a free market which ensured some degree of consumption-led economic growth but mediocre by emerging market standards and unevenly shared. With its best demographic days behind and income levels remaining well below European averages, the lack of a broad middle class acerbated institutional decay and failed to prop-up a second wave business class

OVERVIEW

The low growth in incomes did not allow for a second wave of businesspersons to rise during the consumption-led boom experienced by Central and Eastern Europe during the 2000s and early 2010s, leaving many sections of the business class composed primarily of sprawling conglomerates and shareholders in public companies. With an underdeveloped equity market, a high reliance on debt capital and relatively weak rule of law, the business class may often find itself needing too much political capital to ensure that an otherwise stellar performance in terms of the World Bank's Ease of Doing Business or business taxation is reflected in the composition of even mid-level business actors. Consequently, its upper echelons are dominated by the Kovachki family in energy, whose wealth is estimated at about EUR 400 million, the Bozhkov family, with an estimated wealth of about EUR 700 million in a wide array of concerns and the Sabev family, with an estimated EUR 300 million in sectors ranging from air travel to casinos and entertainment.



PERCENTAGES OF NATIONAL INCOME EARNED BY THE TOP 1%, IN BLUE, AND TOP 10%, IN LIGHT BLUE.
THE DOTTED LINE IS THE MOVING AVERAGE ACROSS EASTERN EUROPE FOR THE 10%.

WORLD INEQUALITY DATABASE

This project was written with the kind support of Banca Transilvania.

THIS REPORT HAS BEEN SUPPORTED BY BANCA TRANSILVANIA

COPYRIGHT

WRITING STAFF

MATERIAL WAS WRITTEN BY RADU GHEORGHE MAGDIN, WHO RETAINS AUTHORSHIP RIGHTS.

GRAPHICS

GRAPHICS AND IMAGES LICENSED UNDER A NON-ATTRIBUTION CREATIVE COMMONS LICENSE WERE USED, AUTHORSHIP REMAINS WITH EACH ARTWORK'S RESPECTIVE AUTHOR.

DATA

DATA LICENSED UNDER A CREATIVE COMMONS LICENSE WAS PROVIDED BY THE WORLD BANK, THE INTERNATIONAL MONETARY FUND AND THE ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT.

ECONOMETRIC ANALYSIS

ECONOMETRIC ANALYSIS AND STATISTICAL RESEARCH WAS PROVIDED BY SMARTLINK DATA STAFF.

SMARTLINK COMMUNICATIONS

2 GARA HERASTAU

2ndt DISTRICT

BUCHAREST