

“In search of lost growth...”

How do you manage your company's growth as a process rather than an art form? Most companies improve productivity by implementing suitable programmes: TPM, JAT, Six Sigma, Lean, Kaizen... All of these acronyms share a point in common: the implementation of a structured project to maximise the impact of cost-cutting measures. Few companies use this type of approach to manage their growth targets and they would be mistaken.

How can these profitability goals be reached in a lasting and reliable manner?

Most companies introduce consistent and systematic cost-cutting programmes by activating and coordinating all of the levers possible: purchasing, layoffs, stock reduction, etc. During a cost-cutting programme, there is not therefore just one action but a group of actions which allows for the goals to be reached. It is not, for example, one SMED^[1] which allows the Just-in-Time approach to be introduced, but a combination of measures which apply to all key levers so as to reduce costs and stock levels while satisfying customers: production planning, operator independence, management of procedures, etc. Likewise, the other cost-oriented methods - Lean, Six Sigma, Kaizen - all aim to coordinate actions to reduce non-added value and swiftly achieve a specific result.

Current approaches to growth

However, paradoxically, growth, which constitutes the other lever to fulfil these profitability goals, is not the subject of such a systematic approach. In this area, the company generally has far fewer resources and its actions are disordered. The associated levers are generally used but are often not optimised and, in particular, not coordinated. Three main approaches are usually used to reach these growth targets: 'surfing' growth, 'hot air balloon' growth and growth 'on a prayer'.

'Surfing' growth

If the company's sector is experiencing strong growth, this is sufficient for the leader and its shareholders, in particular. Even if the company does not over-perform in this situation and loses market share, profitability associated with turnover which is growing 'naturally' may suffice. However, the majority of industrial sectors are now faced with an economic situation in which 'natural' growth is becoming more difficult: either the sector in question has seen a slowdown in its market's growth rate (e.g. telecoms, automotive, etc.) or the sector is experiencing greater competitive pressure, particularly due to the emergence of new Low Cost or Low Price entrants. As soon as this arises, the company can no longer content itself with its sector's growth but must outperform the market to keep its shareholders happy.

[1] Single Minute Exchange Die: rapid change of tools on a machine which minimises downtime and renders the machine more flexible to the client's requirements

Hot air balloon' growth

The company grows by buying firms in its geographical market or internationally. Through external growth, it often shifts growth issues onto the cost synergies which will be possible after the merger while minimising the loss of consolidated turnover. In this case, it is no longer a growth problem that has to be managed but a cost-cutting programme. One need look no further than the communications which follow the announcement of a merger which focus far more on cost synergies than turnover synergies. The problem is that companies are now competing with private equity funds which are making price multiples rise. The profitability of an acquisition then becomes more difficult to obtain on a financial level. Furthermore, a recent study has shown that excessive growth caused by acquisitions was the main reason for the insolvency of companies. This is borne out by the fact that the turnover of the energy broker Enron experienced a heady 2000% rise between 1997 and 2001 and the conglomerate Tyco swallowed up more than 200 companies per year at the peak of its period of hyperactivity.

Growth 'on a prayer'...

The company places all of its hope in a new product or offer. This approach can work, think Apple with the iPod, Peugeot with the 205, Renault and the Espace, or fail, think Apple with Newton, Vivendi and Vizzavi, etc. With a new product, pressure falls on the shoulders of the product manager, who becomes all powerful...if he succeeds. Mid 1993, Apple launched the Newton, based on an idea from the CEO, John Sculley, who wanted a computer on which 'ideas could be noted down'. The computer was tiny - the first mass-market personal organiser - as it was based on a notebook, which explained the integrated stylus. Once sold on a mass scale, the Newton was quickly criticised for its poor ability to recognise the user's handwriting. Sales quickly started to fall. The adaptations and peripherals lagged and early buyers, who had bought the Newton on the premise that they would be subsequently released, became impatient and gave the machine a bad press. Steve Jobs, who had since rejoined the firm, finally put an end to Newton in February 1998.

The Temple of Growth®

It is a mistake: growth must be managed as carefully as cost-cutting. In our experience, two key principles should be borne in mind to ensure rapid and lasting growth: on the one hand, growth opportunities have to be managed under transversal programmes and, on the other hand, a 'war machine' has to be put in place which is capable of transforming company culture into one which is growth-oriented.

The 'Temple of Growth' (see figure 1), designed by Hemeria, means significant results can be achieved: +30% operating margin on certain product lines of a stationer, + 2 to 5 additional EBIT points for a car manufacturer, +25% of EBIT per year for a specialised distributor. Each of the subjects covering organic growth¹ may be considered as the optimisation of one or more processes, by associating, in particular, a measurable indicator to it (see figure 2) on the basis of which a progress-based approach can be built (Plan-Do-Check-Act). We can distinguish between the operating processes linked to a business or a product represented on the graph by the column and the support processes which apply to the whole company.

¹ For external growth, two other columns have to be added: company acquisition management (screening, deal making, etc.) and integration.

Figure 1 : The Temple of Growth®

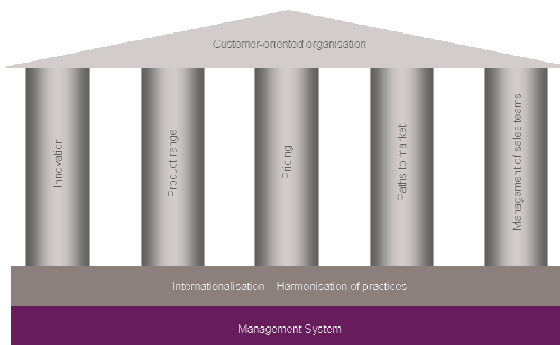


Figure 2 : Performance Indicator on each key lever

Process	Associated indicator
Innovation	% of TO achieved with products launched in the past X months*
Product Range	Market share by TO / market share by number of reference units sold.
Pricing	Margin based on target customer
Paths to market	Purchasing cost (or path cost) / TO
Management of sales teams	Market share according to customers who represent 80% of TO
Customer-oriented organization	NPS (Net Promoter Score®) = % promoting customers - % of detracting customers
Internationalisation – Harmonisation of practices	Development of above indicators for each geographic unit or country
Management System	Rapidity in the development of indicators of other processes

There are three levers which concern the product. The first lever concerns the innovation processes: upstream innovation (market and technology watch, generation and structuring of ideas, project selection and prioritisation) and downstream innovation (product development, launch onto the market and monitoring). Even in commodities, there are possibilities for innovation which can meet the customers' expressed or underlying needs. In all cases, the performance of innovation in the areas of Products and Services depends heavily on the quality of the interface between the Technical and Marketing departments.

The second lever concerns the product range: an architecture of the range has to be defined which ensures an optimal solution between a response to customer needs and the cost of complexity: too simple and it does not cover the entire market but allows management costs to be cut. Too complex and it risks being illegible and bringing about manufacturing and marketing overruns. A complex product range kills profitability but there are levers to bring the Market share vs. Profitability optimum closer.

The third lever is concerned with the products' pricing policy, often referred to just as pricing. On the one hand, it is important for pricing to be as close to the value perceived by the customer and, on the other hand, responsibilities for this policy have to be split: who is responsible for pricing in the organisation? A number of practical examples are given at the end of this article.

In addition to these 'product' levers, the way in which the product is sold must be optimised: paths to market encompass three dimensions: customer segment / product / channel ranging from demand generation to customer support.

The challenge for these paths is to optimise the Path cost / TO ratio while ensuring that the cost is amortized by the margins made and defined in the 'Pricing' lever.

Furthermore, it is also important to manage and steer the performance of the sales channels. Marketing goals are to be translated into sales goals while incorporating the activities and considering resource constraints. On the basis of this definition, it involves putting in place the monitoring procedures for these goals while remaining reactive in the case of a deviation.

Finally, three cross-company levers are essential for any desire for growth: customer focus groups the customer interface management processes, optimising customer satisfaction at the lowest cost. Who are the customers? How can they be divided according to their expectations? How can they be best served according to their needs? These are the areas looked at here. The second lever deals with the internationalisation and harmonisation of practices. This involves replicating a business model which works well in other countries while making sure managerial and marketing practices are applied correctly. Finally, the management system is the basis for any progress in the company. This lever's performance is measured on the basis of the development of the temple's other 'brick' indicators shown in figure 2. It is always good to recall and implement a few basic facts: your payment system only reflects your ambitions; 'go ahead' is cowardly, 'let's go' is unsatisfactory but 'follow me' is exemplary!!

Carrying out transversal programmes

Growth will be limited by the lever which performs least well - the weakest link - and by a lack of coordination between the temple's bricks: a single faulty brick can undermine the whole structure even if the others are sound. At this point, it is important to analyse practices on each lever through maturity grids which permit a rapid diagnosis. On each occasion, the approach consists in being as pragmatic and as little dogmatic as possible: it is rare to find a single lever to fulfil the goals. On the contrary, at least initially, the 'bricks' should be sorted carefully and systematically so as to build an improvement plan which includes the impact of all of the proposals while making sure of their consistency. What is the impact of a great marketing strategy if it has not been adapted to a sales plan? What is the point in developing a new product which is not supported by the sales system? What is the logic behind launching an offer at the same time as a sales force productivity plan?

Instigating a dialogue between sales, marketing and logistics on a common subject is far too often a tour de force. Each department has its own view of the problem in the face of sluggish growth: should the advertising budget or the number of direct marketing employees be increased? Does the problem concern motivating sales partners? Should a new promotion be launched? Is the offer considered too expensive, something which the salespeople consistently complain about? Is the offer not suited to the market?

To protect its main activity, namely photographic films, the Eastman Kodak group completely ignored the trend towards digital technology. In 2004, photographic film still represented 80% of its turnover despite the fact that the market was in decline. In comparison, its competitors made the most of growth in the digital market. In such a situation, the sales force can make every effort possible and be the best but they will not perform well as they do not have the offer suited to the market's demands.

However, there have been cases in which companies have had problems despite a good product. The now well-known example of Sega and its Saturn and later Dreamcast game consoles in the 1990s shows that despite these products, which performed better than those of the competitors, the company lost its place as market leader in a few years to Sony and its PlayStation. There were several reasons for this: Sony attracted the biggest development studios through larger royalties on the sale of games thereby making Sega's games library far smaller than its own; furthermore, Sony opened the game up to the mass market while Sega continued to target 'seasoned' gamers. Saturn thereby took 6% of market share instead of the planned 70%! All of these factors meant a new standard was born linked to the size of the Sony fleet that Dreamcast would not be able to beat when faced by PS2^[1]. By coordinating all of the levers it is thereby possible to over-perform and achieve strong growth.

^[1] In 2001, Sega announced the withdrawal of Dreamcast, the end to its game console business and its repositioning in the area of games publishing.

Introducing a war machine

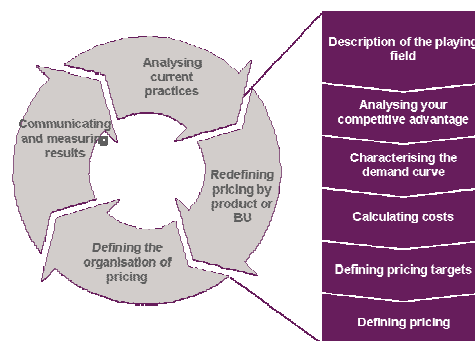
Once the 'Temple of Growth' has been put in place for a product or a Business Unit, the company must entrench this growth culture at all hierarchical levels. The economist, Edith Penrose, showed in her book, 'The Theory of the Growth of the Firm' (1959) that growth is essential for all firms but that it cannot be too strong for too long otherwise control may be lost (see 'Hot air balloon growth' above). Theory dictates that a company's growth rate should not exceed a value known as the Sustainable Growth Rate (SGR)¹, so as to retain the positive effects on the company's profitability and value. For example, Siemens took this line of approach in the 1990s. Over the past ten years, its turnover has increased by 6.2% per year, a figure which reflects its SGR almost exactly. This growth was obtained by activating all of the levers, including the purchasing of targeted acquisitions financed by the sale of less attractive sectors, i.e. Infineon, and a cost cutting programme.

Likewise, General Electric introduced a systematic growth approach. Known worldwide for its exceptional levels of performance and its charismatic former CEO, Jack Welch, over several years GE has applied an implacable cost cutting strategy. An arsenal of tools was designed and deployed to give a common framework to all of the group's firms to fulfil profitability goals: Six Sigma, Crotonville Customer Programs, Work-out, Process Mapping, etc. The new GE CEO, Jeffrey Immelt, appointed in September 2001, used this high performance culture, based on a focus on processes and the ability to deploy management tools, by applying it to increasing turnover. As a goal he set a growth rate which would be twice the size of the sector's average, namely, 8% per year. To achieve this, he deployed a set of tools, 'Execute for Growth', which would support a systematic management process for growth levers with adapted tools, such as CECOR, Lean Showcases and Acquisition Integration Framework. Their programme is structured around six key subjects: technology, commercial excellence, globalisation, growth leaders, customer value and innovation.

An example: the price war is not lost

Does market price always rule? Should we not worry about being competent in this area? To illustrate a possible approach on the 'Pricing' brick of the 'Temple of Growth', the various processes to be optimised are shown in the figure below. Too many companies believe that they have little or even no power over pricing and that prices are inexorably pushed downwards under the effect of uncontrollable external and well-known parameters. Traditionally, the pricing 'function' is neglected: very often, decisions, capacities and information are divided between the various departments (Marketing? Finance? Sales?), regions and business units. A wide range of different prices for each customer frequently reveals anomalies: there is a weak correlation between the net price paid and the size or value of the customer.

Figure 3 : Processes associated with the Pricing lever



¹ For information purposes, this rate is calculated accordingly: $SGR = ROE \times (1 - \text{Dividend Payout Ratio})$, where the ratio is the Net result divided by the Equity amount, multiplied by the proportion of the net turnover not paid in the form of dividends. It corresponds to the threshold above which an increase in funds is necessary (by increasing capital or taking on debt).

Below are a few illustrations of margins of manoeuvre put in place for some of our clients:

Idea No. 1: setting prices according to the value given to customers

A metal parts manufacturer realised that the same product could be priced differently depending on its end use by the customer. Certain customers insert the metal parts into technical products requiring highly specific tolerance levels. For this type of customer, the manufacturer developed products which had been very slightly modified with a warranty on the specifications. This meant the company could significantly increase its prices, without a drop in volume, and achieve a margin which was three times higher.

Idea No.2: optimising the product mix

For a paper producer, products in stock represent a 30% to 50% higher margin than made-to-order products sold through very competitive bids for tenders; the two types of paper are produced on the same machine but the pricing decisions are taken independently by two business units. Furthermore, to retain its rapid delivery capacity and win a bid for tenders for made-to-order products, the manufacturer must often stop production of in-stock products. What was the solution? A tool which permitted the pricing of responses to bids for tenders in line with the production schedule foreseen and the availability of the machines; a modification of the discounts for customers who purchase products in stock so as to reach their volume target more easily. The product mix considerably evolved without a rise in prices; the global margin rose by 15% with an EBIT gain of five points.

Idea No.3: selling services

An industrial company in a commodities market benefits from a price premium in relation to its competitors without knowing the real reasons why. It makes the most of this advantage and develops different service options for its clients: progressive invoicing of a premium for services which customers valued and were ready to pay for (small order, special packaging, guarantee of delivery times), a drop in prices for customers not interested in these services, elimination of some services such as on-site technical assistance which was only valued by a few, small customers, etc. The end result? A rise in the average price, cost cutting and an increase in market share.

Idea No.4: taking care of after-sales pricing

A car manufacturer reviewed its spare parts pricing policy. Each parts group was reassessed in line with the level of competition in the group and the impact on the cost of the SRA¹ basket. The EBIT margin for spare parts rose by two points.

And you?

Whether the sales approach for the offer is that of a deal-based sale (long, complex and technical contracts with service and numerous participants) or one which is closer to the sale of commodities (simple products or services, repeated sales from stock or made-to-order with short lead times), there are veritable levers for growth and the improvement of margins. As the ability to grow becomes increasingly complex, it is important to structure and professionalize growth approaches. Just as we launch cost cutting programmes, the company must optimise its key levers across the entire firm. Rather than having a 'Hara-kiri' approach to productivity which is too systematic, introducing this growth culture which is adapted to all levels within the structure means a significant impact on the company's business can be achieved. To summarise, business leaders, what is your company's hidden potential and when do you plan to capitalise on it?

¹ SRA: sample of parts considered by insurance firms to establish the premium amount for each vehicle