Planning for Growth in Mature Industries

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Consider the following business landscape:

• With an enormous range of options, investors increasingly seek exceptional performance at the expense of security, and shift their portfolios toward high-growth industries and companies.

• Despite poor industry fundamentals, leading competitors deliver superior returns and continuously „raise the bar“ on performance by publicly establishing stretch goals.

• Performance-based remuneration for corporate executives and many employees has become the norm, with returns to shareholders relative to competition the most heavily weighted determinant of compensation.

• Share performance is increasingly influenced by perceptions of management’s ability to sustain growth in earnings and cash flow.

• The prevailing industry sentiment is that the „easy“ route to enhanced earnings – through cost cutting and reengineering – has run its course.

• The most talented workers seek careers in growth businesses and readily jump ship when their employers falter.

Welcome to 1997 and the realities faced by companies operating in mature industries. Over the past five years, the top performers in these industries have significantly reduced costs, grown earnings, and in some cases produced shareholder returns that have handily outpaced broad market indices. In many instances, executives of these firms have reaped large bonuses and exercised options at eye-popping values.

Shareholders (including employees) have grown accustomed to high double-digit returns, and competitors, having learned the cost-cutting lesson, are producing substantial gains from low bases. The pressure on management to sustain such performance is enormous. What new rabbit can they pull out of the hat? To paraphrase President Clinton’s 1992 election mantra – it’s growth, stupid!

But before we rush to buy the next recipe for instant success, let’s remind ourselves – we have had it all along. The fact is, the reengineering rabbit trick has obscured what’s always been the essential strategic challenge: we must continuously examine our business processes and cost structures, but also grow the business, build and sustain competitive advantage, and focus the organization on short-, medium-, and long-term performance.

But We’re in a Mature Industry!

In mature businesses, where industry-wide growth tracks GDP at best, is it realistic to hope to sustain exceptional growth? The short answer is „yes.“ Numerous companies in mature industries have achieved double-digit shareholder returns over long periods, even while avoiding the dangerous waters of diversification, which sank so many businesses in the 1970s and 1980s.

Although there is no „cookbook“ for growth – no substitute for maintaining a deep strategic understanding of industry dynamics and the strengths and weaknesses of one’s own businesses and those of existing and potential competitors – there are lessons to be drawn from others. From our research and consulting work, we’ve created a „playbook“ for growth in mature industries, which, when used judiciously and with a keen understanding of one’s own „playing field,“ can help mature businesses grow.

The Basic Building Blocks for Growth

We have learned that in mature industries there are four basic building blocks for growth (Exhibit 1). Companies in these industries must:

• *Build* a *strong foundation* by creating the lowest possible cost structure, a highly focused asset base, and a robust balance sheet.

• *Establish and embed a growth-oriented vision* throughout the company by ensuring the alignment of key thought leaders.

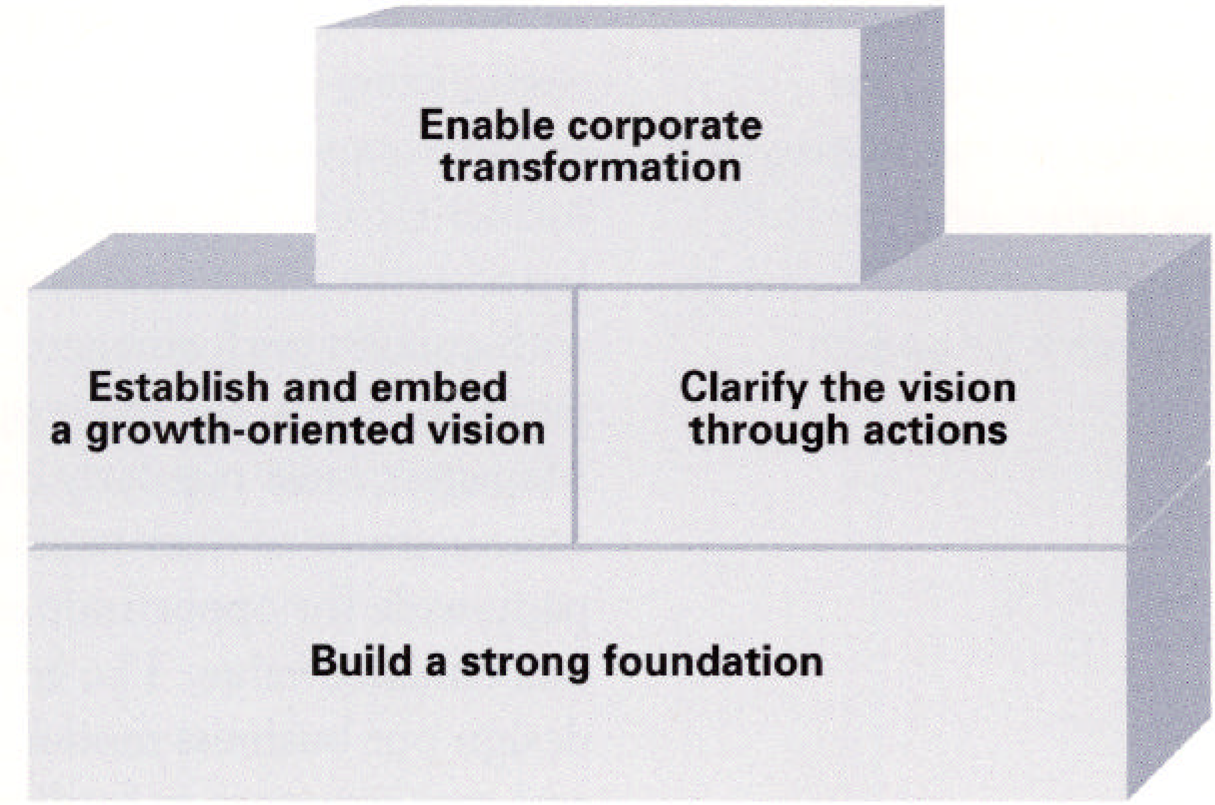
• *Clarify the vision through actions* that are visible and communicated to shareholders, employees, and other key stakeholders.

• *Enable corporate transformation* by building a growth-oriented governance system and encouraging the behaviors, values, and standards of performance among leadership that will engender growth.

Building a Strong Foundation. Over the last few years, the relentless drive for reengineering and cost-cutting has sometimes seemed an end unto itself. But this phase of industry history has served an important function. Only with appropriate cost structures in place can companies effectively take on new phases of growth. As managers of internal business units embark on their growth agendas, they must be assured that corporate cost structures are appropriate, that technological, outsourcing, and alliance opportunities will be realized continuously, and that costs will stay under control as the company grows. Shareholders and potential alliance partners will also demand these assurances.

Exhibit 1

The Building Blocks of Growth



The corporate center and its associated costs play a significant psychological role in this equation. Mature business units struggling to return cash to the corporation so that it can invest in growth opportunities, as well as embryonic business units pressed to create near-term earnings while investing for growth, must be confident that their efforts are not being dissipated by a corporate center that adds little apparent value in relation to its costs. Many leading corporations – including ABB, British Petroleum, Chevron, GE, and Hoechst – are limiting the size of their corporate centers (often to less than 200 people) and ensuring that they stay focused on those activities that clearly add value to the corporate whole. These actions help concentrate the company's energies on the external challenges of meeting customers' needs and conquering the competitive landscape.

In mature industries, companies must use continuous cost-cutting as an engine for generating the cash flow and earnings necessary for growth. As David Simon, former CEO of British Petroleum, once wrote in a letter to the *Harvard Business Review*, „Strategy starts with current performance.... The better current performance is, the more options are created."[1] Managers must regularly conduct forward-looking examinations of their business models, searching company-wide for opportunities to improve efficiencies and enhance value. The key question is: How can we design our business model, key business processes, and cost structure to facilitate growth and support our business strategies, without adding to costs and complexity as our business horizons expand?

Cleaning up the balance sheet through aggressive portfolio management is also a must. Except in special situations, the market will not tolerate high debt/equity ratios for companies in mature industries and will be suspicious of growth efforts financed with debt. Nor can growth accelerate when large amounts of capital long embedded in a company's portfolio are generating low returns. Mature and aging businesses, which once may have been at the core of the company's success, must still „pull their weight" and generate the earnings and cash flow needed to fund and nurture growth opportunities. Assets producing consistently poor returns, despite their historical significance, must be rigorously and aggressively purged. Management can then redeploy the cash from these „harvested“ assets into growth businesses and concentrate the firm's energies on finding and realizing growth opportunities.

It takes courage to divest historically successful businesses in advance of the full flowering of new additions. But to convey the seriousness of a growth agenda, few actions are more powerful than selling a „sacred cow.“ Such actions need not be as dramatic as that of Primark, which transformed itself from a gas utility into a leading information services company. And not every company will need to dispose of its hallmark operations, as Corning intends to do with its house-wares division. But in mature industries, continuous review and churning of the business portfolio is an essential tool for sustaining growth. British Petroleum and Mobil have each culled billions of dollars worth of assets from their portfolios over the past five years, in many instances divesting non-core assets and redeploying those funds into core businesses that hold the promise of future growth. These actions have helped dramatically increase earnings and operating cash flows. The companies' returns to shareholders have handily exceeded industry averages.

Establishing and Embedding a Growth-Oriented Vision. Having hunkered down in the cost-cutting mindset for so long, many companies in mature industries find it difficult to envisage a future of growth and prosperity. Too often, senior management understands the need for growth but lacks the passion to lead the search for it. We often hear top management of such companies saying, „We are committed to growth – find us the opportunities.“ Clearly, the unspoken message is, „It's been so long, we're not sure we know how to do it.“ Meanwhile, middle management is saying, „*Yes*, they claim they want growth, but we'll believe it when we see it. Every time we come up with an opportunity, it's too risky, it doesn't meet their criteria, or it costs too much!“

Given the recent history of cost reduction and reengineering in most companies, it is absolutely critical that the CEO and his/her direct reports deal with „the vision thing“ to reenergize the company for growth. Sustained long-term business growth can come only from the aligned actions of a myriad of people around the company – there is rarely a silver bullet! We have found the following to be the critical elements in establishing and embedding a growth vision:

• Establish core vision and values that have personal relevance and commitment for top leadership and which are credible to thought leaders at lower levels of the organization.

• Visibly demonstrate commitment and passion for that vision through continuous communication and „walking the talk.“

• Establish measurable, aspirational goals in terms of competitive position, earnings, or shareholder returns, at levels which the organization does not yet know how to meet.

• Commit substantial executive time to a process that aligns the corporation's thought leaders with the overall direction – testing and modifying the details as the dialogue proceeds.

• Foster an organizational environment that supports innovative thought, particularly around the creation of growth opportunities consistent with the vision and values.

• Align all internal and external communications with the vision and values.

• Refuse to tolerate behaviors that conflict with the vision and values.

In developing their visions, companies should also consider scenario planning and other visioning techniques that help them search for discontinuities in the marketplace that may create the business opportunities of the future. By looking at the world from a different angle and identifying „wrinkles“ in the competitive topology, companies can gain significant advantage – as ABB and Enron have done so successfully.[2]

Our colleague Bryan Smith has described a number of alternative processes that can help create a „shared vision.“[3] One of his key messages is that a vision must live in the hearts and minds of an organization's people, and not on carefully wordsmithed plaques in the lobby.

Clarifying the Vision Through Action. Immediately after developing a growth vision, corporate leadership must produce tangible evidence that they are serious about their new direction. Visions that remain mere words have a shelf life of only a few months before they atrophy in the hearts and minds of employees and shareholders alike.

As noted above, asset restructuring is a powerful means for demonstrating the commitment to change. Disposals and acquisitions have a profound effect on corporate psychology. Because they are clearly sanctioned by the CEO, yield early results, and are public and often dramatic, they have an immediate impact that other initiatives can rarely match. But for the vision to endure, leadership must institutionalize the mindset that initiates these „one-off“ actions in the company's strategic management process.

To clarify the vision, senior management must also consolidate or achieve leadership in one or more business dimensions in which they anticipate future growth. GE's commitment to be number one or number two in each of its businesses provides focus and direction for its management and employees throughout its far-flung enterprise. Other companies have established their leadership ambitions in terms of technologies: Honda commits to leadership in engines and drive trains or processes, Rubbermaid to leadership in the new product development process. The power of a leadership ambition is that it corrals the random motion of an organization's ingenuity, directs it toward its chosen growth dimension, and highlights the investments or divestments needed to demonstrate commitment to the new path for growth.

For example, for many mature businesses, the most promising sources of long-term growth are the emerging markets of Latin America, Asia-Pacific, and the Former Soviet Union. But too many companies approach these markets on an opportunistic basis, signing up for one-off projects to prove „commitment" without establishing a clear and compelling vision of what future leadership in these regions will require. In contrast, witness how Coca-Cola's clear leadership vision, committed senior executives, and coherent agenda of demonstrable actions designed to establish and sustain market leadership have established an unparalleled track record in building sustainable growth in international markets.

Enabling Corporate Transformation. An organization cannot reach its full growth potential unless it deliberately establishes a corporate strategic governance system and culture that encourage personal and collective responsibility, innovation, and prudent risk-taking. We define corporate strategic governance to include the key business processes, individual roles, organizational structures, and behaviors by which the Board and executive management provide leadership to the organization (Exhibit 2). While most companies signal new directions by changing their organizational structures, redesigning their governance processes would often prove a more powerful and lasting means for generating growth. We find it useful for companies to ask themselves the following questions when considering whether their governance systems and corporate cultures are tailored for growth:

• *Does our strategy-development process clearly identify where growth will come from and how it will be funded?* The strategy-development process should provide corporate management with fundamental strategic options around which they can build a dynamic and growth-oriented business portfolio. Strategy development and portfolio management processes – and not historic budgeting and capital project approval processes – should determine the allocation of resources, including money, people, and systems. Hoechst, the international chemical company, has completely redesigned its strategic management process to improve the management of its business portfolio. Its operating businesses must clearly identify themselves as invest, reinvest, or cash businesses and meet strict financial and strategic goals consistent with these designations. To focus on growth-oriented markets, operating businesses that do not meet financial targets will be ventured or sold. The corporation will manage the portfolio, allocating capital, technology, and human resources. This evolving structure is designed to provide greater autonomy to business unit leaders, while still maintaining the benefits of an integrated portfolio.

Exhibit 2

The Elements of Strategic Governance

Processes	Structural Relationships	Roles
• Fiduciary control/legal compliance • Corporate strategy development • Performance measurement, evaluation, and reward • Allocation of resources • Management succession • Communications/ relationship building • Organizational capability development	• Board • Executive management • Business units • Corporate center	• Board • CEO • Executive vice presidents • Business unit heads • Corporate center vice presidents

Processes

• *Does our performance measurement, evaluation, and reward process really stimulate behavior that will enhance the business portfolio?* Performance expectations and rewards should be set in accordance with the strategic positioning of each business. They should also adequately reward those who take on personal risks to grow the business. British Petroleum, for instance, has instituted a system of performance contracts tailored specifically to the growth and performance objectives of specific asset groups. This process helps ensure that the management of each business unit is focused on its specific expectations.

• *Are we effectively communicating our commitment to growth to all our stakeholders – our customers, shareholders, and employees – and providing them with adequate information and milestones to measure our progress?* Many companies are embarking on more intensive communications to all stakeholders to ensure that stakeholders understand their growth story and clearly recognize progress toward their goals.

• *Do we encourage partnering internally and with others to achieve our growth goals?* Dupont and Dow have recently combined their elastomers businesses into a global, growth-oriented partnership. Each has contributed its strengths – market position and technology, respectively – and the partnership has created exceptionally clear purposes and goals.

• *Both at the corporate level and in the business units, do we have the right processes and process management model in place to identify, develop, and sponsor the capabilities we will need to sustain future business growth?* These capabilities may include technology and innovation, venture structuring and partnering, government and public relations, and risk management. Rubbermaid, for instance, has built its growth strategy around its ability to deliver a constant stream of new products to its customers. „Our objective," says CEO Wolfgang Schmitt, „is to bury competitors in such a profusion of products that they can't copy us."[4] They have carefully cultivated throughout the company a process and a capability to create new products that is unmatched in the mature household goods industry.

• *Have we built into all our governance processes a learning loop that will ensure that we continuously improve and adapt these processes to changing business conditions?* Every company should create a systematic process for sharing learnings and best practices among business units, allowing the entire company to take advantage of innovative ideas. Companies must also strive to create cultures that, while encouraging candor about the current reality of existing businesses, reward managers with a bias for action and a penchant for considering radical change.

In 1992, GE Plastics, the industry leader in engineering plastics, recognized the potential of the business equipment market relative to its historical automotive position. Driven by new applications development and a growth-oriented culture, the company has achieved exceptional results, with both top- and bottom-line growth well ahead of the industry.

• *Is corporate leadership demonstrating the behaviors that will create growth?* Leaders must personally champion, and not simply „manage," the inherently risky investments needed to stimulate growth. They must also build the multicultural teams that can grasp the opportunities of global business. Lucio Noto at Mobil and Roberto Goizueta at Coca-Cola are noted both within their companies and by competitors for their tireless personal efforts to support their companies' worldwide growth initiatives.

Since the CEOs in these leading companies travel continuously, regional management will have more interaction in less formal settings than in those companies in which top management stays at headquarters. Weaker companies scramble to fill overseas posts and tend to forget about the executives they send to them. The returnees are often greeted with, „Oh, are you still with the company?" Adding injury to insult, these transplanted executives find they have fatally lost ground in the corporate jockeying for position.

• *Are we considering innovative organizational structures to remove internal barriers, attack new business areas, and aggressively develop partner and government relationships at the corporate and local level?* Several companies currently noted for their aggressive growth are placing considerable emphasis on matrix management. ABB is rightly famous for its „double solid line" structure, which balances the interests of regional markets and global product lines and enforces cooperation across product lines to create integrated service offerings. Other companies may find this structure difficult to emulate. But if they are to leverage their capabilities in an increasingly complex world, they must establish their own formal or informal mechanisms for managing the complex interactions of business lines, processes, geography, and functions.

The Challenge for Leaders

Let's not underestimate the challenge the growth imperative sets for executives in mature industries. The transition from a single-minded focus on cost reduction and operational process improvement to a balanced focus on cost reduction and growth, on improving operational processes, and on changing governance processes, is fraught with difficulties. Most notably, even if there is no change in the organizational structure, senior managers will be thrust into new roles, many of which will be unfamiliar and beyond their comfort zones

(Exhibit 3).

For corporate executives who have built their careers around administering large but narrowly focused business segments, it will be difficult and uncomfortable to take collective responsibility, together with colleagues, for the overall success of the enterprise. Business unit heads have traditionally been advocates within the corporate court for their local interests. Their challenge now will be to take full ownership of their business units and inspire their people to deliver on agreed-upon goals, while participating more extensively in the broader issues of the corporate strategic debate. Corporate center executives and staff have been accustomed to second-guessing business unit decisions and laying down rules. Their new roles – those of facilitators, mentors, and service providers – will remain highly challenging, but will lack some of the traditional rewards of positional power and may therefore feel demeaning. Nevertheless, organizations will find it necessary to redefine traditional roles along these lines if they are to create companies „fit for growth.“

Exhibit 3

The Changing Role of Executives

	From...	To...
Executive management	• Operational responsibility for a single segment • Manager • Internal oversight • Judge	• Strategic responsibility for the business portfolio • Leader • External advocate • Coach and mentor
Corporate staff	• Analyst • Reviewer • Filter • Oversight	• Facilitator • Service provider • Integrator • Expert functional mentor • Support to executive
Operating company management	• Business advocate • Presenter of plans • Planner • Protector of turf	• Business unit leader • Commitment to targets • Option creator • Internal partner

Getting Growing

The task of accelerating growth in a mature business can be so daunting that many executives hardly know where to start. In our experience, however, the employee is often ahead of the CEO in recognizing the imperative for growth (after all, his or her future career and ESOP holdings are every bit as important as the CEO's). And many middle managers, after a decade of dealing with downsizing and reengineering, will be rejuvenated by a clearly articulated vision for growth, demonstrated by executive support and commitment to change. The right place to start will be determined by the company's current performance and asset portfolio, as well as its culture and competitive environment. But at the heart of the issue is establishing and instilling vision, and demonstrating its power through rapid, deliberate, and decisive action. It is never too early – or too late – to start.

[1] Harvard Business Review, *January/February, 1995 issue, Vol. 73, number 1, p. 142.*

[2] *See: „Scenario Thinking: Planning for the Futures You Want (And the Futures You Just Might Get),“ by Christopher E.H. Ross, J. Ladd Greeno, and Albert Sherman in this issue of* Prism.

[3] The Fifth Discipline Fieldbook, *Doubleday, 1994, pp.312-332.*

[4] *J.P. Deschamps and PR. Nayak,* Product Juggernauts*, Harvard Business School Press, 1995, p. 69.*

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