GROWING A BUSINESS

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STRATEGIES FOR LEADERS & ENTREPRENEURS

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Introduction: the trouble with growth

THE FOUR FOUNDERS of a software resale and implementation business receive an offer to buy their company. They did not know that it was for sale. As they think things through, it occurs to at least one of them that they had not intended to found a business in the first place. They had all been made redundant by the same company at the same time, and as part of their redundancy package they had been allowed to see some projects through to completion; but a few projects had turned into a few more, and soon they were winning new clients, providing new services, recruiting more staff and finding offices.

The offer to buy the business forces these accidental entrepreneurs to think hard about the business and what they want to do with it. It also forces them to think about themselves. One founder argues that accepting the offer is the obvious thing to do: they had not intended to found a business and now someone is offering a decent sum of money for it; surely they should take the money and get on with the rest of their lives. Another thinks differently: the business has only just started; imagine how much more could be done with it over the next few years. The other two do not know what to think, but they do know that since the offer letter arrived they have gone from building the business to arguing about whether to sell it, and in so doing they have ceased to pay attention to the business itself.

Not having been in this situation before, the four founders do not know that the decisions the offer to buy the business is forcing

on them are typical of the decisions asked of countless other managers in successful growing businesses. Selling the business is the easy thing to do: the problems of growth will be passed on to another set of stakeholders and the founders can go their separate ways. The implications of not selling the business are much more complex. For example, what will they do with the business? Should they invest in more service lines and products? Should they sell into different industries? Should they sell overseas? Do they need more office space? Rather than sell the company, should they look to buy someone else's? Is one type of growth better than another? What led them to contemplate accepting the offer to buy? Are they worried about things changing? How much does a business change as it grows, or does it just get bigger? If it does change, how? To what extent could and should they control the rate of growth in the business? What are the real costs of growth: not just the financial costs but the personal costs, particularly to those inside the organisation? What are the enablers of next year's growth, and are there levers they could pull that would help the business grow further and faster? What are the barriers to future growth? Is growth necessary? Is growth desirable?

Part of the problem is the unstable nature of the subject; managers, particularly those ambitious for growth, have to get used to thinking about organisations as transient, in a permanent state of flux. Too much business thinking implies a future state when the business will have "arrived"; more than just achieving stability, it will have reached a stage where the principal management challenge will be to keep it going. But this sort of stasis, even in a successful company, is illusory. Many experienced managers will remember their younger, ambitious selves walking into a new organisation and quickly forming a view of what is wrong with it. "When I'm in charge I'll sort out this and correct that and fire him and promote her – and everything will then be fine." But with the benefit of experience and hindsight these individuals realise that management is not that simple; that problems change even as you attempt to solve them; and that next year's problem is

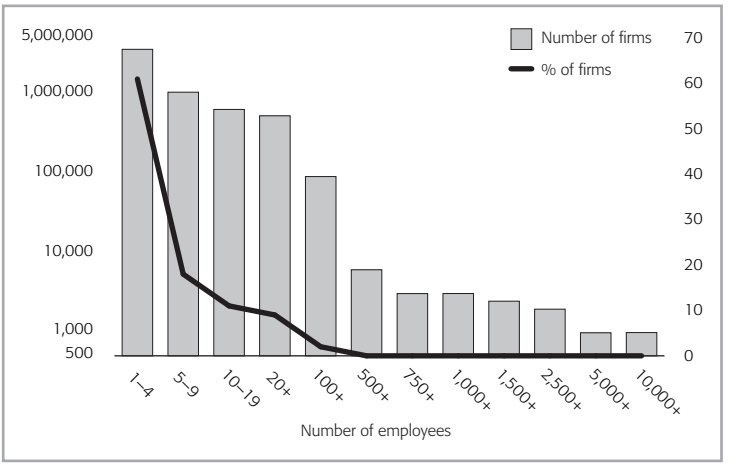
complicated by rather than resolved by the solution to last year's problem. Even if growth is a consequence of success, it brings organisational challenges that threaten the success that caused it. Conversely, to sustain growth it is important to realise that what worked last year will not necessarily work next year; an organisation that wants to manage growth successfully needs to change things that are not yet broken.

The problems brought by change inside an organisation are compounded by changes outside it. Indeed, growth in a business itself often triggers change in a market and industry, which in turn demands further change in the business. Growth may attract competitors, competing technologies and regulators, as well as customers from different markets with different expectations.

Growth gives rise to problems for businesses of all sizes. Different divisions in a big business evolve at different speeds and may therefore be at different stages of evolution, each with its own problems, presenting additional challenges to the organisation as a whole: how to reconcile the competing and contradictory plans of one division with another is a particular growth challenge for the bigger business. Mergers, joint ventures and acquisitions – inorganic rather than organic growth options – present even more challenges, not least with integration. Small businesses have their own particular sort of growth challenge as they seek to establish credibility as well as culture, brand and identity; develop secure lines of supply and sustainable relationships with customers, suppliers and financiers; and manage the changing relationship between owners and managers. An established business in one country investing in a small venture in another needs to acknowledge not just the legal and cultural differences between the two countries, but also the differences between managing a large, corporate business and a small entrepreneurial firm.

Businesses that fail to manage growth become its victims. Some businesses go bust, not for lack of potential, but because they fail to manage the consequences of the growth they have

FIG 1.1 **US business registrations: number of employees, 2008**



Source: US Census Bureau

achieved. Not least of the problems created by growth is the financial pressure it causes.

Summarised like this it is amazing that any business bothers growing at all. Many cannot or just do not. Figure 1.1 shows that of some 5.9 million businesses registered in the US as having any employees during 2008, over 3.6 million (61%) had fewer than five. As a percentage of all businesses, those with more than 500 employees scarcely register on the graph.

Of course, there are thousands of small businesses around the world, many of which no doubt provide satisfactory returns to those who run them, who have no wish for the business to grow. However, for every business that is content with its current size, there are many with ambitions to grow which struggle with the issues that growth presents.

This book is for them. It draws on the thinking of academics and business people as well as the experience of those working in business in its aim to help managers in their pursuit of growth. It

covers a variety of subjects – strategy, performance measurement and management, people management, sales and marketing, finance – and takes into account differences in business size, sector and location. Above all, this book argues that managers and owners who anticipate and manage the challenges of growth give themselves the best chance of ensuring that growth is secure and sustainable.

The four individuals described at the beginning of this chapter took advice and evaluated the offer to buy the business. The amount seemed large, but in reality it significantly undervalued the business. They all agreed that the best option was to grow the business themselves, but in a disciplined and structured manner. They drew up a plan for growth for the next three years; they identified market opportunities open to them and selected the most promising, thus ensuring their efforts were focused; they estimated how fast they could realistically expect to grow funding from internally generated cash flow, thus obviating the need to take external finance; they identified key resource constraints and drew up short- and medium-term plans, including recruitment plans, for addressing these.

They also considered their own ambitions. The founder who had initially argued in favour of the sale decided that he was happiest as a project leader and client-facing manager. He did not want to pay the personal price that growth would have demanded of him, so he stepped back from the senior team, keeping his equity but taking less in pay and bonuses. The other three allocated specific senior roles and responsibilities among themselves and recruited to fill any gaps. They monitored progress against their plan at six-monthly intervals. Some three years after the initial offer to buy the company they sold it, but to a different acquirer. This time the decision to sell was theirs, and the amount they got for the company was many times that originally offered. Two of the four founders stayed with the company after the sale and looked forward to a new set of growth challenges.

2

Stages of growth

WHEN BUSINESSES GROW they do not just get bigger. Growth delivers qualitative as well as quantitative change. A changing business makes changing demands of its managers. Is it possible to generalise about these changes? If so, might it be possible to anticipate the problems that growth will bring in the future and thus reduce the risks associated with it?

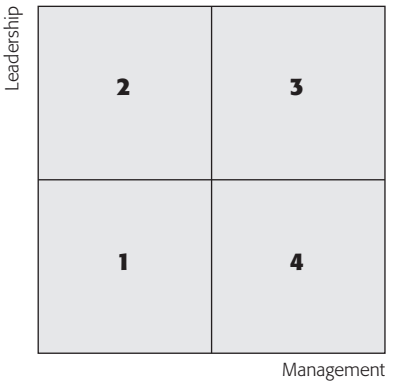
From leadership to management

A good place to start considering the changes caused by growth is to look at the changing role of the founder.

Abraham Zaleznik, then on the faculty of Harvard Business School, was, in 1977, one of the earliest management writers to draw a distinction between creative, inspirational and enthusiastic types, and organised, disciplined, sensible managerial types, using the labels "leader" for the former and "manager" for the latter. Figure 2.1 shows this distinction using the leadership/management matrix from John Kotter's book, *Leading Change*.[1] It is a distinction that has also been used to contrast entrepreneurs in new businesses and other members of the management team in growing businesses.

Most businesses start high on leadership and low on management. If businesses are to stand a chance of developing into something sustainable, they will need even more of these leadership qualities – energy, inspiration and creativity. A business in its early stages will thus move from 1 to 2 if it is to evolve, dominated

FIG 2.1 **The leadership/management matrix**



Source: Author

by individuals with these foundational qualities of leadership. Organisation, discipline and governance in these early stages are often closely associated with the force of personality of the founder. Indeed, the organisation hardly exists as a separate entity at all, and the business is wholly identified with its founders and owners.

But things have to change as the business grows. In 1997 Jeremy Newman, former CEO of BDO International, wrote:[2]

> *New businesses are started by entrepreneurs who, through some combination of wisdom and luck, create and implement a successful business strategy. The business expands and profits grow and with this comes the need to hire professional managers. So people are recruited and promoted to manage, to cope with the growing bureaucracy and to prevent things getting out of control. And so the organisation grows and management grows to cope with it.*

The introduction of "management" heralds reporting timetables, appraisal schemes, formal agendas and other

manifestations of the way to run a "proper" business. From an organisation that thrives on the high octane of entrepreneurship and the excitement of chasing after the next sale, the new business has to evolve into one in which the disciplines of management have far more influence. On the matrix, the business moves from 2 to 3, where leadership and management are in balance; where there is enough business discipline and governance to sustain the business, but not so much that the qualities of entrepreneurship and leadership are threatened or damaged.

For many businesses, staying in 3 sounds good in theory but is difficult to achieve in practice. Some entrepreneurs ("leaders") feel obliged to turn themselves into managers, or at least develop management capability, acknowledging both a fundamental change in role and the need to acquire and utilise new skills. But although people can change and develop, it is rare to find an individual who can operate comfortably at both ends of the leadership/management spectrum.

Rather than take on the managerial role themselves, entrepreneurs often best serve their own and their business's interests by seeking to recruit the necessary management expertise. But in doing this, entrepreneurs should realise that their own role is still likely to need to change. Entrepreneurs and their new managers may not see eye-to-eye, and entrepreneurs who do not adapt to their new organisational circumstances are heading for conflict with their new management teams. This often results in damage to the business and the acrimonious departure of either the manager or the entrepreneur. Too often, a reluctance to face up to the consequences of what is an inevitable tension leads some businesses to duck the problem in the first place by deferring the necessary change until a crisis forces it on them. But businesses serious about sustainable growth must introduce a management infrastructure. Family businesses can be particularly prone to deferring this kind of management professionalisation.

Many people with a managerial bent assume that the management force is more important than the entrepreneurial

one. Indeed, this is a tendency in much business thinking. As Newman says:

> *This in turn stifles leadership and encourages management and because the business is successful, managers begin to believe that they are the best and their idiosyncrasies become part of the culture of the organisation.*

Although it is true that a business without decent management will not survive for long, a business in which the management impulse takes over and the entrepreneurial spirit is squeezed out will become yet another over-managed, under-inspired, middle-aged business on a glide-path to history. Premature ageing in an organisation is almost as worrying as a refusal to let it mature. This is often a characteristic of start-ups established by large companies, as a result of the mistaken assumption that the start-up is just a small version of the big one. In the case of a stand-alone joint venture established by two UK listed companies (one a retailer, the other a broadcaster), the new chief executive was keen to "establish an entrepreneurial culture" but said that his first priority was to discuss implementing a pension scheme for himself and his team. Such a worry about retirement might be prudent but is a sure sign of a business on its way to being old before its time. That it is common for the finance director to succeed the entrepreneur as chief executive in a growing business would seem to illustrate how managers take over from leaders and how the sober discipline of accountancy is likely to supersede the energy, creativity and propensity to take risk of the founder. According to a survey reported on by Grant Thornton in December 2014, some 85% of those in US *Fortune* 1000 corporations believe the chief finance officer would be the most appropriate choice for succeeding the chief executive.

As well as highlighting a contrast between the entrepreneur and the more managerially and governance-minded members of a team, the tension between leadership and management might be turned into a model outlining what is for many businesses a

key transformation in their growth and development. The model is primarily about different types of people, but indirectly it hints at different stages of development that all businesses have to pass through as they grow, and suggests how the managerial, organisational, strategic and operational imperatives differ significantly from one stage to the next. In short, as well as growing, businesses have to grow up.

Modelling growth

When those who study business growth have attempted to generalise about its implications, their thinking has often taken the form of a growth model, an analytic framework that describes the stages that businesses pass through as they evolve, the characteristics of each stage, and the changes necessary to facilitate the move of the company from one stage to the next. The remainder of this chapter outlines some of the best-known growth models and explores how useful they are for those trying to grow their businesses or deal with the consequences of growth.

Evolution and revolution: the Greiner model

Larry E. Greiner, professor of management and organisation at Marshall School of Business at the University of Southern California, published his article "Evolution and Revolution as Organisations Grow" in 1972.[3] It is not the first growth model, but it is the earliest one still in common use in the classroom and in the business strategist's office. Greiner initially proposed five phases of growth through which businesses pass, adding a sixth stage in 1998.

Although each of Greiner's phases starts with a period of evolution, it ends in revolution, a period of "substantial organisational turmoil and change". How each revolutionary period is resolved determines whether or not the organisation will develop further.

The periods of revolution are at the heart of the model. Greiner's