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The Physics of Business Growth

MINDSETS, SYSTEM & PROCESSES

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Chapter 1

Fighting the Physics of Growth

Ask managers at any level, in almost any organization, and they'll tell you that they struggle to produce the kind of profitable organic growth that investors demand. Consistently, organic growth is at the top of the list of challenges for business leaders—and at the top of their list of essential capabilities for ensuring success. And yet, there has been a surprising lack of attention to helping managers develop this ability. In fact, it is not even clear what the behaviors associated with successful growth leadership even *look like*—or what the organizational enablers of such behavior might be. That is why we have written this book.

For more than 15 years, we have been exploring—at first independently and recently together—how successful organic growth actually happens in organizations (See Notes on Authors below). Through our research and work with businesspeople from frontline managers to CEOs, we've concluded that organizations are often their own worst enemy. They don't give managers and employees the tools to find growth, their business mindset and processes don't support people who do somehow stumble upon growth opportunities, and their corporate cultures, measurements, and rewards seal the deal by turning growth into an unnatural act.

People, process, culture, measurements, and rewards—all of these, as they exist in most organizations today, are at odds with what we think of as the “physics of growth.” It is a physics that is radically different from the one we prepare managers to succeed in. Our aim here is to help you understand the difference between the physics of stability and the physics of growth, and to provide you with a map and a set of practical tools to navigate this brave new world.

What Do We Mean by the “Physics of Growth”?

After years of studying growth and working with managers at all levels trying to achieve it, we have come to believe that organic growth is, in fact, governed by its own *natural laws*, an underlying reality that sets the context for growth and innovation in much the same way that Einstein’s law of relativity accounts for the movement of objects in the space-time continuum—or the way the underlying economics of an industry drives the success of business models. The most fundamental natural law of organic growth is that the only certainty is *uncertainty*. The dominating forces are ambiguity and change; the processes at work involve exploration, invention, and experimentation. These elements, taken together, capture the distinct physics of organic growth.

Unfortunately, this physics is very different from the one that has long informed the design of business organizations; that physics is characterized by stability, predictability, and linearity. In both environments, people seek control over outcomes, but how they go about achieving that differs radically. Analysis, prediction, and rules usually work to achieve control in a stable, predictable environment where the process is geared for execution. But those approaches often backfire badly in the face of growth’s uncertainty. Ignoring the physics of growth is like ignoring gravity: through sheer courage and herculean effort, managers can make things happen, but in doing so they continuously fight relentless forces that slow them down and sap their energy. Courageous and naturally growth-oriented leaders may still find a way to produce the growth they are asked to deliver (we’ve studied them and how they accomplish this)—but these managers tend to be few and do not a strategic capability make.

Many of the cultural values, systems, and processes in large organizations fight the physics of growth and its emphasis on exploration and invention rather than execution. The

result is that growth leaders feel as if they are “swimming in molasses,”ⁱ as one manager described it. That is because even the best managed (perhaps *especially* the best managed) large organizations are beautifully designed to produce standardized, low-variance results through careful execution in an environment of predictability. They employ talented leaders at all levels who have learned (and may well be predisposed) to focus on efficiency and control. Because of this, they excel at execution—and at driving waste and variation out of the system—and they have a state-of-the-art tool kit for accomplishing this. Unfortunately, the pursuit of growth and innovation is inherently messy and inefficient. Unlike execution, exploration is a high-variance activity, and if, as work in the area of total quality management (TQM) would suggest, “variation is the mother of waste,” it is also often the mother of invention.

The mindset, culture, and processes that drive successful execution in an existing business can, if unexamined, drive innovation into the ground, exhausting and discouraging the very people who are trying hardest to accomplish it and killing inventive ideas before they see the light of day. Sporadic interventions and innovation consultants can help, as can people who courageously press on with innovation despite the odds. But these strategies work *in spite* of organizational forces, not because of them. Building a *strategic capability* for growth requires engaging the hearts and minds of employees at every level and giving them new tools to achieve a better balance between invention and execution. That’s what this book is all about.

Learning from Las Vegas and Silicon Valley

You can learn a lot about the physics of growth by comparing who wins and loses in a Las Vegas casino. When it comes to growth, most managers, sadly, are like the little old lady with a cup of quarters playing the slots, just pulling the handle and hoping for the best. Sophisticated growth leaders—those who understand and leverage the physics of growth—are

probably at the craps table. Craps is the preferred game of most professional gamblers (we are told) because it offers the most potential for making serious money—if you know how to play. It may *look* like the professional craps player is throwing the dice and hoping, just like the old lady at the slots, but there is a lot more going on. Discipline and focus, not luck, are the hallmarks of great craps players: they know how to manage the game in real time, assessing and sticking to what they can afford to lose, placing many bets, figuring out when to double down and when to get out, staying alert to emerging opportunities and new developments. Sure, the odds are still in favor of the house; that is the reality of the game. But the chances of beating the odds are a lot higher at the craps table than they are at the slot machines.

Closer to home, this physics of growth is well understood by venture capitalists. VC firms' track records are not stellar: somewhere around two of every ten investments turn out to be winners. Do VCs consider themselves dismal failures? No, because they understand that the force at play here is uncertainty. And so they see themselves as managing *portfolios* of growth opportunities. Some of these will do well, but most, they realize, will not. They also know that their ability to predict at the early stages *which* two ventures will succeed is poor. They do not attribute this to their personal failings; instead, they recognize that the inability to predict is a property of the uncertainty surrounding any new business. Like professional gamblers, they develop a set of practices that acknowledge this reality: they bet heavily on the individual leader of a new business and look for people with experience (expecting both some successes and some failures in their background), they try to keep their bets small and affordable until they have better data, and they develop approaches that help them get in and out of new ventures intelligently and swiftly. Their goal, in other words, is to succeed—or fail fast and cheap.

When large organizations pursue growth, their mindsets are often completely out of sync with the reality that guides both craps players and VCs. Chances are that these organizations expect ten out of ten projects not only to win, but to win big. They demand that their managers and employees produce growth, inadvertently thwart their attempts, and uphold a system in which pulling the plug on a failed growth opportunity is a career-threatening act. Would-be growth leaders in this environment are like professional gamblers who are unable to act independently but instead receive instructions from on high—from a source that has little information about what is happening *this* minute in *this* particular game. Not a formula likely to win at craps—or in business.

What is behind this mismatch of expectations and realities? We believe it a set of misconceptions about corporate growth. Let's look at what we know (or *think* we know) about how organizations achieve healthy growth.

Growth Myths

When it comes to growth, we have been taught the following “truths”: Businesses either grow or die; all growth is good; growing bigger is always better; and public companies should grow in a linear manner as evidenced by ever-increasing quarterly earnings. Surprisingly, these beliefs have been embraced without rigorous analysis about how well they describe the actual growth trajectories of robust businesses. Nonetheless, they are the foundation of the short-term business mentality dominant in many C-suites, boardrooms, and Wall Street firms. And they are pure and simple fiction. These beliefs ignore the physics of growth. Businesses do not have to grow to stay alive; growth is not always good; bigger is not always better; and continuous linear growth is the rare exception, not the rule. Blindly following the dictates of these myths can drive

bad corporate behaviors and inhibit real growth and innovation. It also can lead to artificially induced business volatility, lost opportunity, and premature destruction of businesses.

Yet, so powerful is the imperative for businesses to report growth that companies engage in a widely acknowledged “earnings game” to meet short-term projections instead of focusing on the hard work of managing portfolios of organic growth opportunities. This game takes the form of the “creation” of earnings through accounting elections, valuations, reserves, liberalizing credit policies, channel stuffing, deferring needed expenditures, selling assets, and myriad structured financial transactions. These non-authentic earnings are too often generated solely to meet Wall Street’s growth and earnings demands.

You don’t have to look far to see the downside of those demands: shareholder value squandered on overpriced and inappropriate acquisitions, managers chasing the wrong customers or cutting corners to meet inflated forecasts, CEOs with solid strategies hung out to dry for missing EPS projections by pennies. To satisfy Wall Street’s obsession with growth, businesses are encouraged to make imprudent decisions that can harm their fundamentals in the long term. And, in some cases, those decisions simply camouflage a business’s poor performance and underlying weaknesses. What is clear is that at its best, this earnings game makes it difficult for investors to assess the underlying strength of a business; at its worst, it incentivizes short-term profits to the detriment of a business’s long-term health.

The earnings game also influences the planning and budgeting processes that businesses put in place in the name of “growth”—processes that set revenue and profit targets for growth projects without asking about the new ideas behind them and whether they will create value for identifiable customers. Strategic planning processes, which often are no more than glorified budgeting exercises, almost invariably ignore the physics of growth. Even when managers do

attempt to put some real strategies behind the numbers, they often assume a one-to-one match between specific projects and financial flows. Thus, the strategy-making process pays little attention to the portfolio nature of growth investments. As one senior executive manager explained it:

“We have a portfolio view of our business. And by portfolio view I mean a PowerPoint slide. And that’s exactly what it is—it’s a PowerPoint slide. It does not drive our behavior. If we had ten product developments going on, we are banking on each one of those hitting at approximately the right time, generating revenue at the right time, for us to roll up and make a plan that we are then committed to. So, it’s not that we lack a strategic view of our business. I don’t think we take a strategic view of our portfolio of initiatives and say that really to be successful over time I need to make sure that at least two big bets are going to come off, and over the next five years I need to have at least two products that are going to generate \$50 million of revenue or \$100 million of revenue annually, therefore I need in my portfolio four of those types of developments. Somehow we don’t connect that kind of strategic view of the business and the markets with our portfolio of how we’re actually going to achieve that.”

The rallying cry becomes Supersize it! In a big organization, focus and control are key; too many new initiatives can dissipate corporate attention and resources. And so we don’t want to waste time with anything small. But at what cost? The bigger-is-better mentality holds the same risks for “healthy living” in organizations as it does in a fast food drive-thru. It actually *increases* the difficulty of finding good growth by increasing its riskiness, for obvious reasons: If it’s big, why hasn’t somebody already done it? And how do you tell in its infancy how big a new idea might become? Ask the folks at former PC market leader Compaq why they ignored the new business model offered by Dell and allowed themselves to lose leadership to an undergraduate starting out of his dorm room. We are betting that they will tell you that the opportunity to go direct to customers just didn’t look big *enough* to risk disrupting their existing distributor relationships. Neither did offering \$4 cups of coffee before Starbucks tried that small move. The impatience for big wins leads to expensive fiascos and missed opportunities.

With the obsession with size comes the notion that managers must “prove” the value of an idea before devoting any resources to it. This is, of course, a fool’s errand. We state the obvious when we point out that managers asked to prove the value of a business proposition that doesn’t yet exist will mostly never get out of the starting block. They would have to make up the numbers, and the only people generally allowed to do that and get away with it are expensive consultants (and until recently, investment bankers). So the best that mere managers can do is extrapolate from some data they’ve already got. But that kind of information is not very convincing, especially if the idea contains much that is innovative. It’s got all kinds of assumptions built into it that reflect the past and don’t necessarily have anything to do with the future. It’s easy to find fault with these kinds of data, and the ROI police generally do. The end result is that managers get caught in a debate about proof that never moves out of the conference room.

Making things worse, the hours spent in that conference room don’t make anybody any smarter. Managers in large organizations have been encouraged to stay inside for too long, doing analysis and trying to plan the future using data from the past. While some forecasting and planning based on historical data is certainly sound—after all, that is the only data we’ve got to start with—relying too heavily on this approach in uncertain situations interferes with the pursuit of healthy growth. It encourages managers to abandon potentially good initiatives that don’t have easily available existing data and to take more risk than is necessary (by staying with historical data rather than seeking new data from the market) in pursuing those that they do select. The kinds of processes that lead to good growth encourage employees to *leave* the building and *learn* something—from customers, collaborators, value chain partners, or even other industries.

The twin emphases on “big wins” and “proof” contribute to the disastrous prevalence of mergers and acquisitions. For decades, academic research has demonstrated that most

acquisitions fail to create value for shareholders—more often, they *destroy* value—yet this cold, hard reality has done little to dampen the acquisitive appetites of organizations desperate for growth. Why? Because acquisitions seem bigger and thus more apt to be “needle movers” than organic growth initiatives, and their value seems easier to “prove” with historical data—even though this value usually fails to materialize. Paradoxically, a strong record of M&A success can actually decrease managers’ appetites for the uncertainty surrounding organic growth.

Acquisitions seem more controllable and predictable—the revenue hit is certainly surer in the short term. In the long-term, however, paying big premiums for ideas that a company’s managers could have developed themselves seems crazy. Even more sobering, continuous acquisition in the absence of organic growth is akin to a drug addiction—it keeps taking bigger hits to get the same kick. But, in the short term, since we know that we can always fall back on the security of an acquisition when attempts at organic growth falter, there is less incentive to keep working at building a capability that seems risky and uncomfortable.

All Growth is Not Created Equal

Some kinds of growth are healthier than others. Healthy growth is based on the *real* physics of growth, not the mythological one. It is *sustainable* because it taps into the organization’s distinctive capabilities and resources to create enhanced value for customers and collaborators. This kind of growth is organic in the basic meaning of the word: related in a fundamental way to the other parts of the whole to which it belongs. Growing organically is much more than just *not* growing through mergers and acquisitions. High organic growth companies do make acquisitions, but they are generally small in size relative to the acquirer, and they serve a strategic purpose other than revenue. These acquisitions are not tacked on to the organization for a short-term high; they are fully connected to it and in service to the whole.

They establish new geographic footholds or new customer segments, or they add new technology, products, services, or capabilities that can be scaled through the acquiring company's much larger customer base.

We are not talking about walking away from the organization's existing skills at execution. We don't want to throw out the baby with the bath water. Failure to manage the existing business well will get a firm into trouble a lot faster than failing to grow some new ones. The goal is not to create "growth" organizations per se; it is to create *balanced* ones that have the capability set to excel at both invention and execution.

Most organizations today are decidedly out of balance. They look like body builders who do only pull-ups, so they have bulging biceps (those do the heavy lifting of execution) on top of underdeveloped quads in their painfully skinny legs, which inhibit speed and adaptability—and hence growth. We need to address this imbalance while accepting that the tension between managing an organization for efficiency and control and managing it for growth and innovation never goes away altogether. Leaders don't resolve it—they work through it every day.

Where Can We Turn for Advice on Growth?

If much of what we "know" about growth is wrong, where can business leaders facing growth mandates look for good advice? Instead of turning to economics, we suggest exploring a broader selection of sciences. Physics is not the only source of good advice. Fields like biology are based on assumptions of change, evolution, adaptation, feedback loops, nonlinearity, and unexpected results. Biology has spawned new theories of change and growth that comprise an area called *complexity theory*, which asserts that growth is an *experimental learning process*. According to the theory, organizations strive for fitness, defined as the ability to perceive, adjust, and adapt continuously to an unpredictable and changing environment.ⁱⁱ Scientists in this field

argue that we have a lot to learn about adaptation in the face of uncertainty from the most humble of creatures: the ant. Melanie Mitchell, a professor of computer science and a member of the science board at the Sante Fe Institute, describes ants' search for food in a process she calls "communication via sampling":

“Ant foraging uses a parallel-terraced-scan strategy: many ants initially explore random directions for food. If food is discovered in any of these directions, more of the system's resources (ants) are allocated, via feedback mechanisms, to explore those directions further...As in all adaptive systems, maintaining a correct balance between these two modes of exploring (random and focused) is essential. Indeed, the optimal balance shifts over time....As information is obtained and acted on, exploration gradually becomes more deterministic and focused in response to what has been perceived by the system.”ⁱⁱⁱ

Ants, it turns out, may have more useful advice for us than economists.

Building a “Whole Brain” Organization

Anatomy and new research on brain science are other sources of provocative insights. We've learned that the old right brain/left brain dichotomy is an oversimplification, but the fact remains that certain parts of our brain have a logical and analytical (let's just use “left brain” here as a shorthand) orientation, while others have a more expressive and creative (“right brain”) orientation. Both parts of the brain have to work together, but individuals usually exhibit a preference for one orientation or the other (again, recalling the equivalent of a mental bodybuilder with big biceps and skinny legs). With the help of business education and corporate cultures, we have honed our left brains and neglected our right brains, leaving them with the equivalent of very skinny legs. Consider these differences in orientation:

- *analytic* versus *creative*
- *rules* versus *tools*
- *logic* versus *emotion*
- *exploiting* versus *exploring*
- *capturing value* versus *creating value*
- *execution* versus *invention*

Think of which side your organization tends to fall on. We'd bet that it is mostly on the left. Invention falls squarely on the right, so is it any wonder that most businesses are not so good at it? Like individuals, organizations need both sides of their brains working together to create healthy growth. To build a "whole brain" organization, we had better get started on those skinny legs.

Learning from Growth Leaders

So far we've turned to gamblers, venture capitalists, ants, and neuroscientists for insights into growth. We now want to add our personal observations of successful growth companies and their managers. In an effort to provide managers with concrete advice on how to face and surmount their growth challenges, a group of colleagues at the Darden Graduate School of Business at the University of Virginia studied 22 high-growth companies and more than 60 successful growth leaders in order to uncover their "secret sauce" for growth.^{iv} These winners helped us to identify the physics of organic growth and pointed us toward successful strategies that worked *with* rather than against them. Out of this research, we have developed what we believe to be a best practice model for achieving sustainable "good growth." Before we describe that model, however, let's look at the highlights of what we learned.

We began our studies of growth companies with several hypotheses based on our strategy backgrounds. We expected that the companies we studied would likely possess the following characteristics:

- unique products and/or services
- the best talent
- visionary leaders
- superior innovation capabilities

Counter to our expectations, none of those characteristics was necessary to produce consistently high performance. In fact, our high-growth companies

- did not necessarily sell unique products or services
- did not always have the best talent (but did get exceptional performance from their employees)
- rarely had visionary, charismatic leaders
- were not the most innovative in their industries

What these successful companies had in common were highly engaged, loyal, and productive workforces who knew their customers very well. Their leaders often were humble and passionate. These companies were master learners and imitators. They had simple, focused strategies that all employees could understand. And they seemed to have a “be better” DNA. Interestingly, in studying these high organic growth companies, we found different kinds of cultures. Some were customer-centric, some were employee-centric, some were growth-centric, some were product-centric, and some were brand-centric. It did not seem to matter. What was important was that these consistently above-average growth companies had, over time, built an enabling internal system for growth—a *growth system*. (We’ll be taking a close look at that system in Chapter 3.)

Next, we studied individual growth leaders who had beaten the odds to find growth in mature markets, despite operating in big companies that often lacked the kind of growth-enabling system described above. These managers revealed to us additional aspects of the growth puzzle and gave us our early insights about the physics of growth versus the physics of stability, predictability, and control. These growth leaders had broad repertoires of business experience that had taught them to work hard to understand the customers for whom they wanted to create value. They wanted to understand these people’s lives and problems, not just sell them more stuff. This was critical to their ability to find not just new opportunities—but profitable ones that

allowed them to differentiate themselves. In addition, they were consummate corporate politicians, masters at end-running the existing system (usually one based on the physics of stability), which often inhibited, rather than facilitated, their efforts. We discovered that these *catalysts*, as we called them, also had a growth mindset, along with the ability to operate the way entrepreneurs do—taking action in spite of corporate restraints, learning by doing, and minimizing risk by using only the resources they could afford to lose.

In both the company-level and manager-level research conducted at Darden, it was clear that success came from managing risk in ways appropriate to an uncertain environment: by defining clear boundaries and then freeing employees to invent and experiment. Experimentation was essential in order to learn, adapt, minimize loss, and gather data for better investment decisions.

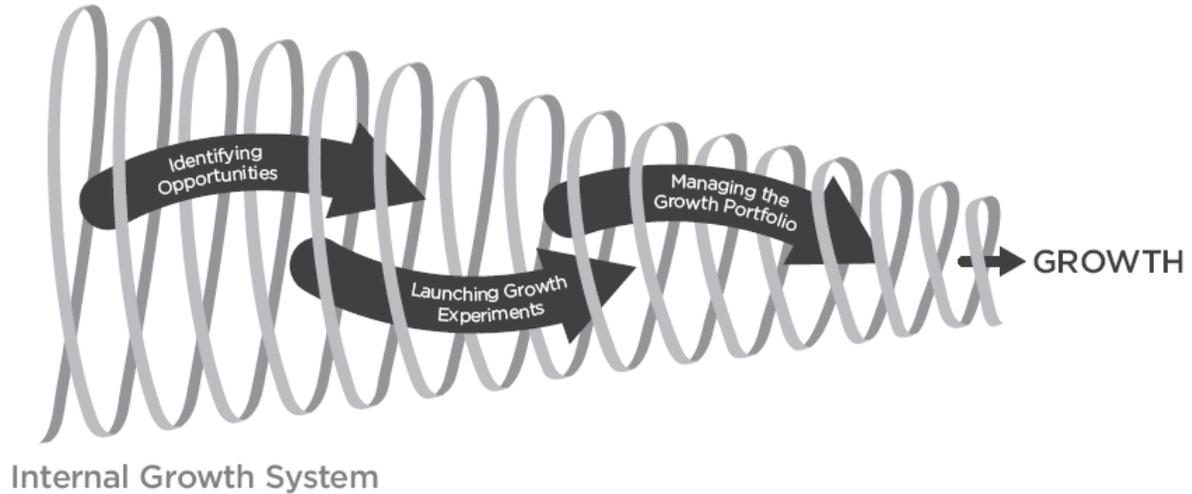
Our final significant insight from our combined research takes us back to Silicon Valley VCs: growth, we found, results from having and managing a portfolio of initiatives. The high-growth companies and managers created a pipeline of experiments that they managed across a timeline and risk profile. The size and composition of this portfolio varied depending on the size of the business and the life cycle of its products and services. Composing and then monitoring the portfolio was one of senior leaders' primary organic growth responsibilities.

This body of research has led us to develop a model—a growth formula—that captures the essential elements involved in creating a strategic capability for healthy growth:

GrowthFormula

MINDSETS + SYSTEM + PROCESSES

Prepared Minds



There are three key aspects of our growth formula: (1) preparing employees' minds, (2) building an internal system, and (3) putting in place a path that consists of three processes: identifying opportunities, launching growth experiments, and managing a growth portfolio. *Who* is responsible for *what* changes as specific ideas move along this path? *Senior leaders* must create and sustain the enabling infrastructure and compose and manage the portfolio of initiatives. It is the *managers'* and *employees'* jobs to be on the ground actually doing the work of identifying opportunities and moving them forward into experiments.

In the following chapters we will look at each of these activities individually, at the levels of both organizational and managerial action. Let us give you a brief preview of what the rest of the book looks like.

Chapter 2 Preview—Creating Prepared Minds

Growth depends on many human beings, with their cognitive limitations and biases, perceiving and processing information and communicating with one another along a path of exploration, invention, and experimentation amid constantly changing situations and supported by all components of the organization. Growth is an *outcome* of a set of behaviors on the part of *people*. To achieve it, individual employees need to take certain kinds of action. It is the role of the leadership of the organization to put in place an environment and a clear path that encourage those behaviors. It is also their role to ensure that the minds of employees are prepared to see and execute growth opportunities.

Scientist Louis Pasteur, explaining the role of discipline and preparation in scientific discoveries, observed that “chance favors the prepared mind.” Substitute the word “opportunity” for “chance” and you’ve got the basic idea about the first element of our growth system. The opportunities to grow are already there—but employees often aren’t able to *see* them. Seeing them—and then leading them—requires a *prepared* mind. Creating prepared minds among employees at all levels of the organization involves attention to an individual’s mindset, comfort with risk, repertoire of experiences, and “right brain” skill set for approaching the physics of uncertainty. In this world, creating prepared minds becomes much more crucial because you can’t specify the rules in advance like you can in a stable world. Three components stand out as critical for this preparation.

First is mindset—a person’s perspective on the world and outlook on life. Our choices reflect our mindset. For some of us, new situations are an opportunity to learn; for others, they are an opportunity to fail. Given all we’ve said so far about the uncertainty surrounding growth,

we can't overemphasize the importance of encouraging a learning mindset in all employees. Yet many corporate cultures do the opposite—they expect perfection and punish mistakes.

Second is repertoire. Successfully leading growth can look a lot like the game “can you name that tune?” All you get is a few measures and not much time to look for the pattern. When organizations allow people to operate in functional silos, they learn to recognize and play only one song—generally “the way we've always done it.” If, however, people work in a variety of functions and businesses as their careers develop, they can quickly and skillfully play a lot of different pieces of music. A broad repertoire can be an important enabler of growth.

Third is customer empathy. The word “empathy” is important here. Every company believes it cares about customers. But in many of the organizations we work with, being “customer focused” amounts to trying to shove products more effectively at people, using a variety of segmentation schemes and emotional advertising. An empathetic orientation toward customers looks quite different—it involves being deeply interested in the details of their lives as people, not categories of consumers. It is kind of a “customer inside” (to piggyback on Intel's famous “Intel inside”). This focus—and the research methods that accompany it—are much more likely to produce the kind of deep and original insights that inspire invention and lead to truly compelling and differentiated new value propositions. But detecting unarticulated needs is notoriously difficult. They don't show up in the text of market research reports based on surveys and focus groups. The successful techniques in use here are almost always ethnographic and involve close observation of what customers are trying to accomplish, not necessarily what they say they want. That is why the hearts and minds of employees throughout the organization, at every level, must be engaged in this activity.

Chapter 3 Preview—Building a Growth System

Here we will dive deep to lay out what a growth system looks like in detail and help you assess how your current system matches up. Recall that it was this kind of internal system—not new products, new strategies, or charismatic leaders—that characterized the high organic growth companies in our research.

For our purposes, we define a growth system as a seamless, consistent, self-reinforcing alignment of strategy, structure, culture, execution processes, leadership behaviors, HR policies, measurements, and rewards that promotes the behaviors necessary for growth—the behaviors that reflect the growth mindset we discuss in Chapter 2. Note that we said *behaviors*, not financial results. Financial results are outcomes that result from actions taken by people. Too often, in our experience, senior leaders jump immediately to a focus on financial results without first assessing and specifying the behaviors that can produce them.

So that’s where we start—by defining the behaviors (among all employees) that promote growth as well as those that thwart it. This can be a tricky exercise for many executives, but it’s a necessary first step. Asking for new behaviors in a system that still encourages, measures, and rewards the old behaviors is a complete waste of time or, worse, engenders cynicism and mistrust. For a good example of a growth-promoting and a growth-inhibiting behavior, consider the difference between saying “Yes, and” and “Yes, but.” The former propels a discussion, validating and building on others’ ideas. The latter is a sure conversation killer, the enemy of exploration and experimentation.

With a list of growth behaviors in hand, we then move on to building the components of the system: culture, structure, measurements and rewards, HR policies, and leadership behaviors. Often, there’s not one right approach—different kinds of culture and structure, for instance, can

encourage the behaviors you desire. The key is to figure out what's best for the organization. Note that changing a single element of a system to achieve new behaviors—introducing a new structure, for example, but not attempting to shift the culture or HR policies—rarely works. The elements must be perfectly aligned and self-reinforcing to encourage the desired behaviors. And senior leaders must begin by asking hard questions about their own behaviors. To inspire you to take on this challenge, we consider some powerful examples from UPS, IBM, Stryker, Sysco, Outback Steakhouse, and Best Buy.

Chapter 4 Preview—Identifying New Ideas

Now we move to action, to the processes of growth. The first is identifying opportunities. There are almost as many myths about creativity and idea generation as there are about growth. Here we dispel those myths by showing that being “innovative” is not the purview just of artsy types, creativity works best as a team sport, some of the best new ideas aren't in fact all that new, and the first great idea we think of isn't necessarily our best.

There are two stages of idea generation: discovery and concept development. Contrary to what many businesspeople assume, innovation does not begin by considering the future. Instead, it begins in the here and now. Discovery starts with the customer's current reality and looks through his or her eyes. During this stage, we ask customers about the job they are trying to accomplish, the outcomes they want to produce, and the constraints they face. We want to pay particular attention to emotional as well as functional needs. The outcomes of this stage are the criteria a new idea must meet in order to be successful.

In the concept development stage, we finally look to the future and new possibilities, taking our customer insights and developing them into concepts that can be tested.

Where do ideas come from? To gain some useful perspective on that, we turn to the world of design. While businesspeople tend to think in terms of constraints, designers add to that possibilities and uncertainties. We can illuminate new possibilities in eight ways: challenging, connecting, visualizing, collaborating, harmonizing, improvising, reframing, and playing.

In addition to discussing the *what* and the *how* of idea generation, we also consider the *who*. Because the key here is to gather as rich a trove of ideas as possible, the search for great growth ideas must come from many sources throughout the organization. People at all levels have important roles to play: Senior leaders identify a set of strategically targeted areas of opportunity. Middle managers go after the deep insight into customers. And P&L leaders create diverse teams to carry ideas into the experimentation phase.

Involvement should be broadly inclusive. The goal is to create and maintain engaging, transparent communication and evaluation processes to gather new ideas offered from throughout the organization, acknowledge their receipt, evaluate their merit, reward participation, and clearly explain why some ideas are chosen for further exploration. Who in any organization is best positioned to see ways to improve customers' lives? Those at the front line, of course—sales people, service employees, call center workers, and those in similar roles, who are often the most underutilized source for organic growth. Succeeding at organic growth is a volume game. Our work, as well as that of others,^v suggests that 1,000 ideas produce perhaps 100 early experiments (we'll call these Learning Launches) that translate into about 10 initiatives in your growth portfolio that produce one or two "doubles" and one "home run." The more eyes on the prize, the better.

Chapter 5 Preview—Learning Launches: Doing Growth Experiments

Having accumulated, from diverse sources, an array of new business ideas, you now need to learn more about them. You begin by determining which ideas look sufficiently promising to merit moving from traditional analysis, based on existing data, into more rigorous field experiments. Managers and employees then assess each idea's likelihood, based on what they know to be true today (half-baked beliefs masquerading as truth need not apply), of passing four "tests" that determine the value of a new business offering: (1) compelling value creation for customers, (2) distinctive execution by the firm, (3) defensibility from competitors, and (4) ability to be scaled (all four of which are not created equal in the life cycle of a new idea). This requires surfacing underlying assumptions, assessing what data you've already got to test them, and then identifying what further data you could go out and get that would help you explore the critical assumptions more thoroughly.

To accomplish this (a surprisingly tricky endeavor), we have created a formal technique that we call a Learning Launch: a small, fast, low-cost experiment designed to gather data you can use to make an informed decision about the viability of a growth idea. Learning Launches involve a sequence of small moves aimed at launching and learning simultaneously. They focus on generating data and insights quickly from direct market experience, rather than on "rolling-out" completed designs.

Learning Launches work because analysis has become so dominant a method for validating the worthiness of an idea and justifying the use of corporate resources to pursue it that we have lost sight of its weaknesses. There are limits to the power of analysis. Recall the physics of growth: identifying, assessing, and pursuing new growth opportunities always involves making choices under conditions of uncertainty. In most large organizations, managers pondering growth

ideas are expected to take data from a known past and connect it intelligently to an unknown future. Subjecting new growth initiatives to validation through the kind of rigorous analytics that large organizations crave is a major inhibitor of growth.

Learning Launches are based on risk-minimizing behaviors that limit upfront investment—using partners instead of bringing up new manufacturing facilities and relying on existing capabilities instead of acquiring wholly new ones. They emphasize keeping early moves simple and local—where feedback is immediate and unambiguous, where corporate politics and layers of translation don't get in the way of assessing the relationship between cause and effect.

While managers and employees are designing and conducting Learning Launches, the responsibility of senior leaders is to enable such experimentation by providing funding and decision-making processes that grant individual managers the autonomy and resources to identify and make small marketplace bets on promising growth ideas. Their role is not to screen, inspect, or attempt to manage or control individual Learning Launches early in their life. Such meddling, in our experience, slows down the process, increases fear, and generally wastes a lot of time.

Chapter 6 Preview—Creating and Managing a Growth Portfolio

In this third stage along the path, experiments will be extended and advanced as the new growth ideas that pass the four tests mentioned above are refined and commercialized by employees and gathered into a growth portfolio by senior leaders. This is when their window into the specific set of ideas being tested usually opens up. Their role is to compose and manage a portfolio of experiments in various states of refinement, with attention to creating a balanced

portfolio of initiatives that maximize short-term and long-term opportunities while minimizing risk.

Creating a balanced growth portfolio involves a series of choices: Do you focus primarily on improvement initiatives—getting better, faster, or cheaper? Do you focus on innovating new products or business models? Do you undertake an aggressive acquisition strategy to fill an innovation pipeline void?

Growth initiatives vary on many dimensions. Some produce results quickly; others do so slowly. Some have an impact on the top line; others on the bottom line. They vary in the likelihood of commercial success as well as the degree of financial risk. Growth initiatives may leverage existing capabilities or require building or buying new ones. All these variables factor into creating a customized portfolio designed to maximize the probability of producing the growth needed to replace declining revenue streams from mature offerings and to maintain your competitive viability.

Here we help you categorize growth opportunities and explore some of the issues you'll encounter in managing your growth portfolio—whether to centralize or decentralize its management, how often to review it, and how to think about levels of investment. We also share the story of Starbucks, which developed a robust and diversified portfolio of growth initiatives—to great effect.

As we move forward, keep in mind that our intent in this book is to explore the power of aligning people, system, and processes to the real, rather than mythological, physics of growth—to make growth a *natural* act by overcoming the proclivities of organizations and individuals' cognitive make-up and left brain emphasis and instead creating more “whole brain” organizations. We'll talk in more depth in each of the ensuing chapters about what it takes to

prepare managers to find and execute new opportunities, the kinds of process support they need, and the values and beliefs that underlie the system. We'll talk about how these come together to create a *strategic capability* for growth. So we are back to where we started: *people, system* and *processes*, the inhibitors—and potential enablers—of good growth. If only we understood the physics.

Notes on Authors

Edward D. Hess

As a former investment banker and strategy consultant, Ed began his organic growth research in 2002 at the Goizueta Business School at Emory University and continued his research of high growth public and private companies upon joining the Darden Graduate School of Business at the University of Virginia in 2007. When he began, he was surprised that organic growth was defined by size metrics or as being the opposite of acquisitive growth and was not widely researched by academics. He first developed the “Organic Growth Index,” a financial model designed to illuminate high organic growth companies. That led to his research of the characteristics of those 22 such companies, which was published in the book *The Road to Organic Growth: How Great Companies Consistently Grow Marketshare From Within* (New York: McGraw-Hill, 2007). That work, in turn, led to his collaboration with Jeanne in which they created the Darden Growth Model and he further developed his concepts of growth systems and growth portfolios. He followed that work with a multidisciplinary research project looking for the empirical basis of the commonly held beliefs about business growth. Those research findings—“The Myths of Growth”—were published in his book *Smart Growth: Building an Enduring Business by Managing the Risks of Growth*, (New York: Columbia University Press,

2010). In his private company research, Ed looked at the challenges faced by 54 high growth private companies and has published those findings in two books *Growing an Entrepreneurial Business: Concepts and Cases* (Stanford: Stanford University Press, 2011) and *Grow to Greatness: Smart Growth for Entrepreneurial Businesses* (Stanford: Stanford University Press, 2012).

Jeanne Liedtka

As a former consultant with BCG and then Strategy faculty member at the Darden Graduate School of Business at the University of Virginia, Jeanne struggled with how to help the managers she taught develop a skill set around producing organic growth. The scant academic research she found offered little in the way of insights—and even less in the way of tools. The traditional strategy frameworks taught to MBAs—SWOT analysis, 5 Forces, competitor analysis—didn’t seem to be very helpful in locating and exploiting new growth opportunities. And the leadership literature was no better—despite a torrent of work talking about “good leadership,” no one seemed to be even asking (much less answering) the obvious question: Was good *growth* leadership the same as just plain good leadership? With the support of Darden’s Batten Institute, Jeanne and several of her colleagues set out to explore how great growth leaders acted and who they were. Over a period of three years, they interviewed and assessed the personality and practices of more than 60 managers singled out for their ability to produce better than market growth in mature organizations. They published their findings in *The Catalyst: How You Can Become an Extraordinary Growth Leader*, with coauthors Robert Rosen and Robert Wiltbank (New York: Crown Business, 2009). What they learned astonished them: much of what managers were being taught, while appropriate for their roles in leading in stable and predictable environments, was just plain *wrong* when it came to succeeding at growth.

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- ⁱ All anonymous manager quotes in this chapter originally appeared in Jeanne Liedtka, “Growth Leaders Research Project,” Batten Institute, Darden School of Business, Charlottesville, 2005-2006.
- ⁱⁱ John Henry Clippinger III, ed., *The Biology of Business: Decoding the Natural Laws of Enterprise* (San Francisco: Jossey Bass, 1999), 7.
- ⁱⁱⁱ Melanie Mitchell, *Complexity: A Guided Tour* (New York: Oxford University Press, 2009), 182-183.
- ^{iv} Edward D. Hess, *The Road to Organic Growth: How Great Companies Consistently Grow Marketshare From Within* (New York: McGraw-Hill, 2007).
- ^v Gary Hamel, “Innovation’s New Math,” *Fortune*, July 9, 2001.