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unstoppable

FINDING HIDDEN ASSETS TO
RENEW THE CORE AND FUEL
PROFITABLE GROWTH



Chris Zook

Author of *Profit from the Core* and *Beyond the Core*

BAIN & COMPANY, INC.

UNSTOPPABLE

Finding Hidden Assets
to Renew the Core
and Fuel Profitable Growth

CHRIS ZOOK

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Introduction

Something has changed fundamentally in the world of business. Although few people seem to have internalized this shift, the effect is startling and profound. Ten years from now, one in three companies will no longer be independent because of bankruptcy or takeover, and another one in three will be completely different at its core, maybe even having a different core. Only one in three will resemble what it looks like today.

What is this change? It seems that for a majority of businesses today, fundamental threats to the core have moved from rare events to nearly common occurrences. And most businesses are not prepared for what that means. In many industries, it appears that the weather patterns of business have changed from a temperate climate punctuated by periodic storms to a norm of frequent storms punctuated by periodic monsoons. Will this situation be true forever? Possibly, but who knows? What is certain is that it will be the case over the next decade.

My first two books with Harvard Business School Press—*Profit from the Core* (2001) and *Beyond the Core* (2004)—were about the search for sustained and profitable growth. This body of work over a five-year period studied how often companies fail to recognize the full potential of their core business and, as a result, prematurely abandon it in the pursuit of hot markets or sexy new ideas, only to realize their error—often, when it is too late. The books described a

systematic way to assess your full potential and to make sure that you do not fall into this common, and typically human, trap.

Yet what happens when the core itself comes under severe threat? How do you recognize the magnitude of that threat before it is too late? How do you make sensible changes in the fundamentals of your business to reignite a new wave of growth rather than risk stalling or even worse? What do you do when it seems that your success formula is starting to reach a limit sooner than you expected?

How to make fundamental change in your business model, while still running your business, is what this book is about. It is about how all businesses ultimately approach a natural limit to their growth formulas, something that demands changes in strategy or even in the core itself. Why then is this book called *Unstoppable*? Shouldn't its title reflect endings, rather than persistence? The reason for the title is that the companies we chose to study and profile most closely are those that beat the odds. We also analyzed patterns of failure and estimated the odds of success offered by various paths in various situations. Many of those statistical findings are reported throughout the book. But in the narrative, we focused on the case studies and accounts of the executive teams that, for a period of years, fought their way through severe threats to their core and found a way to renew their trajectory of profitable growth.

This does not mean that these companies are forever unstoppable. No company is. In fact, our data suggests that an increasing percentage of companies will experience fundamental threats to their core strategies as the world speeds up. Strategies are becoming obsolete faster than ever before. But the companies we feature found a way to go from unsustainable to unstoppable, against the odds, for a significant period.

The central finding brings with it a positive and surprising message. Virtually all the success stories built their renewal on a company's "hidden assets," which previously had been undervalued, unrecognized, or underutilized. These hidden assets were not central to the strategy of the past, but they held the key to the future. Furthermore, the older and more complex the company, the greater was the likelihood of finding promising hidden assets. This does not

mean that new capabilities, ideas, or technologies from outside your four walls are not critical ingredients—quite the contrary. But it does mean that many companies already hold most of the cards for a winning hand but do not realize it. It is a lot easier to win in poker—a game also blending skill, luck, and intuition—if you know that you already hold a few aces than if you are relying on the dealer for a whole new set of cards.

The alternatives to looking deep within your own core to redefine your strategy prove to be much more risky. They include entering the race for the next hot market, or buying in to the lottery for the next big technology, or bidding in the auction for the next big transforming acquisition, or hoping that your company miraculously will become more “innovative,” thereby neutralizing the strategic threat without even confronting it. Although these routes sometimes lead to fame and fortune, we find that the odds of success are low and the risks to the organization are often high. To rely on these risky pathways alone is to fall under the spell of seductive, but dangerous, siren songs.

My conviction to write this book crystallized at the annual partner meeting for my firm, Bain & Company. At this meeting each industry practice group holds day-long sessions to describe its point of view on the dynamics of its industry and on the strategies being followed by various competitors. As I wandered from room to room, sampling presentations, something began to dawn on me. Almost all our clients and their competitors were confronting more fundamental and more frequent threats to their core businesses—requiring much broader thinking about the strategies of the future—than before. It was true in airlines, where low-cost carriers were finally triggering fundamental moves by the majors. It was true in media, where businesses from film production to newspapers were seeing their success formulas of past decades hitting the wall and seeing their stock prices tank. It was true in telecommunications, where convergence and the Internet were causing seismic shifts, and where once-impregnable fortresses such as AT&T had fallen and been acquired, and the foundations of the new fortresses were still shaky. It was true even in many basic industrial businesses,

which were encountering new levels of turbulence, often related to the emergence of competitors in China and its ripple effect on supply chains and cost structures around the world.

I felt this acutely, as it relates to the topic of this book, when I was on a bus visiting Suzhou Industrial Park outside Shanghai. Suddenly, out the window I saw a long dark band, like a Möbius strip, winding its way around many buildings. What was it? As the bus moved closer, I realized that the dark band was a line of thousands of people, two abreast, quietly inching toward a large open window. It was a massive job fair for the industrial park. This seemingly endless ribbon of humanity was supplying labor to a park that was expanding seven miles in each direction each year and adding a new factory every four days. I reflected that only about 10 years ago, the Suzhou park had been a big rice paddy. Now it was a city of more than half a million people, a Chinese version of a gold rush town.

It has been said that the U.S. industrial revolution took one hundred years, the development of a modern economy in Japan took thirty years, and the equivalent level of change in China will take about fifteen years. Transforming the nation's "core" at the highest level, China found that its people, unshackled and unleashed, were the ultimate hidden asset. Given this pace of change, it is no wonder that the strategy cycles of the companies that fuel the world's economy are shortening.

I realized that more companies than ever were going to enter a period when their historic core was no longer enough, in its current state, to sustain profitable growth and that a fundamental strategic change was inevitable. Such change can be daunting for companies that have tens of thousands of employees, hundreds of products, serving millions of customers all over the world.

I began this research with a series of conversations with business executives, many of them, over a short period. Each echoed the same themes, though in very different industries—from personal computers to global logistics to retail to the newspaper business.

One such conversation went back and forth, thrust and parry, point and counterpoint until suddenly it stopped. A profound question hung in the air. It had been asked by Victor Fung, CEO and group chairman of Li & Fung, one of the leading supply-chain management companies in the world. Li & Fung is a symbol of the rise of modern China and an example of a company that has drawn on hidden assets to reinvent its core. I was speaking to Dr. Fung in his Hong Kong office overlooking an endless procession of cargo ships in the harbor below. It had struck me that the ships were like determined carpenter ants playing their assigned roles in reconstructing the world. We were talking about the challenges of fundamental change, and his question was this: “There is an old Chinese proverb: ‘Sometimes to be reborn, you first must die.’ In a world that is speeding up, how will companies change enough without crisis?”

I had no answer then for Dr. Fung. It wasn’t until we examined the data for this book that we found the real key to redefinition: those hidden assets. And there is a lot of data. This book is based on the largest study I am aware of on the patterns and risks of making deep, fundamental change in a business’s strategic direction. The main sources of information were as follows:

- A fifteen-year database tracking the performance of 8,400 companies in the G-7 economies.
- An examination of five hundred U.S. public companies from 1995 to 2004, focusing both on their financial performance and on changes that they made in their core.
- Analysis of the fifteen largest “big-bang” strategies announced and pursued by major corporations in the past ten years, along with a scorecard of current results.
- Two global surveys of business executives conducted with the Economist Intelligence Unit. One, titled Growth Survey, was conducted in October 2004; it asked 259 executives about the challenges and barriers to growth in their core business. The

other, Capability Survey, took place in November 2005. This one asked 240 executives about their needs for new capabilities as part of a competitive strategy.

- In-depth case studies of twenty-five carefully selected companies around the world that have successfully confronted issues of core redefinition. This research included extensive in-person interviews with the CEOs and other members of the management teams.

The appendix describes our research methodology.

This book completes a trilogy of sorts on the topic of how companies define and grow their core (*Profit from the Core*) and push out their boundaries into new territory (*Beyond the Core*), only to one day discover that they need to redefine and renew their core (*Unstoppable*). I undertook this research at Bain & Company, where I am a leader of the Global Strategy Practice. What I failed to realize, early in the process, was how the “focus-expand-redefine” cycle of growth was accelerating. As a result, many more management teams will spend much more time than ever before confronting fundamental issues, even incipient crises, deep in their cores.

This book examines how companies can improve their ability to recognize the need to redefine their business model and lays out proven methods to improve the chances of successfully accomplishing this risky, but often essential, mission.

Unstoppable exists at the intersection of three bodies of work. The first is the literature on turnarounds, epitomized by *Good to Great*, by Jim Collins. That book focuses on management, leadership, and organization. *Unstoppable* examines the strategic dimension of performance renewal.

The second body of work that this book builds on is the search for growth opportunities in difficult and low-growth markets. *How to Grow When Markets Don't*, by Adrian J. Slywotsky and Richard Wise, is a key contribution. *Unstoppable* differs from that book in its examination not only of low-growth markets but also of the full range of

situations when a strategy reaches a limit, fundamentals of the business are called into question, and the question is what to do next.

The third area that this book spans is strategic innovation. This work has two strands. One focuses on the critical importance of having a novel point of view of the future that you can translate into strategic changes, along with investments in the right new core capabilities, ahead of competitors. *Competing for the Future*, a 1994 book by Gary Hamel and C. K. Prahalad, is the business classic in examining this issue. The other stream of thought explores ways that companies can innovate within their core business model to find untapped markets—"white spaces" or "blue oceans," in some authors' lexicons. *Blue Ocean Strategy*, by W. Chan Kim and Renée Mauborgne, is a successful recent book that suggests one approach to find these untapped pockets of market opportunity. *Unstoppable* is different from this literature in its provision of empirical data on success rates of various possible paths, and most of all by its focus on the use of hidden assets to improve the odds and generate innovative new strategic alternatives. This book also offers a methodology for attacking the difficult issue of what to do when your past strategy starts to reach a limit. Because it connects to, and completes, a series of three books on the topic of sustained and profitable growth, it is unique in the breadth of the approach it recommends and the range of its demonstrated practical application by management teams.

A key, and somewhat surprising, finding is that the best blueprint for core renewal seldom requires leaps to distant and hot new markets, mandates being the first adopter of a pioneering new technology, or demands a "big-bang" acquisition. Rather, the most successful companies at redefining their core strategies use assets that they already have at hand or to which they have easy access. In our case studies, we found that pivotal assets often proved to have been hidden. Yet exploiting these hidden assets allowed these businesses, for a while, to move from unsustainable to unstoppable.

This book provides a simple framework for understanding how hidden assets can become the keys to transformation and identifies the best techniques for detecting and using them in your own business.

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Unsustainable to Unstoppable

Diamonds. “Tears of the gods.” The most concentrated form of wealth known to humanity. Few objects conjure such a range of experience and emotion. Searing heat in deep layers of the earth’s mantle yields the product called *ice*. Miners in hardscrabble African villages and polishers in India’s bustling diamond centers create gemstones worn by the world’s elite. A product often associated with bleak and poor regions, diamonds have become a symbol of enduring love.

For all the emotions evoked by the gems and their production, the business world of diamonds was, for decades, more like diamond itself: colorless and highly stable. De Beers Consolidated Mines, descendant of a company founded in 1880 by explorer and adventurer Cecil Rhodes, reigned over the world’s diamond supply, parceling out the gems to dealers in a manner designed to maintain prices and protect profits. Sir Ernest Oppenheimer, chairman of the company that controlled perhaps three-quarters of all diamonds mined and sold in the twentieth century, described the strategy explicitly: “Only by limiting the quantity of diamonds put on the market, in accordance with the demand, and by selling through one channel, can the stability of the diamond trade be maintained.”¹

Yet by 1999, De Beers's run of success, like all good things, seemed to have come to an end. New Chairman Nicky Oppenheimer and new Group Managing Director Gary Ralfe were looking at a company whose market value had declined substantially, whose market growth rate had turned negative, whose profit margins were hovering close to zero, and whose share of global production had dropped to around 40 percent. As Oppenheimer and Ralfe discussed the situation with shareholders, the other board members, outside analysts, and the management team, they found no shortage of opinions about how to tackle the situation.

Some observers felt that the market would turn around. It was thought that the key was to hold the course for a bit longer, cutting costs and using De Beers's industry scale to resuscitate the century-old formula of supply control. But hadn't things changed forever with the entrance of new competitors? Others believed that the answer was to attempt to recoup market share of production by acquiring competitors or by investing in new mines. Of course, De Beers was already investing in new mines. The question was, How would further investment revive the company's performance in a new competitive environment, where the development of synthetic diamonds was on the rise? Was it possible that De Beers's primary source of past differentiation as the controller of supply was finally reaching some natural limit?

One of De Beers's unique and most valuable assets was a \$5 billion stockpile of rough diamonds that it could draw on to stabilize prices in the marketplace. Yet even this massive asset was no longer an effective tool, and it was becoming difficult to maintain given its enormous economic opportunity cost. A few mavericks suggested that perhaps De Beers should begin to diversify into new areas, recognizing that the market for diamonds was not what it used to be. But wasn't that the riskiest strategy of all? De Beers was diamonds.

As the financial pressure mounted, the management team concluded that the situation De Beers faced would not be reversed by following a strategy close to the one it had followed in the past.

Maybe, they thought, the answer could be found in De Beers's many underutilized customer assets: its unique image in consumers' eyes as the custodian of what the company would come to call "the diamond dream" as well as the strong De Beers brand, the company's unique access to and reputation with customers at all points in the value chain, and its track record as the provider of the most valued gems in the world. Perhaps the company could find a way to shift from a supply-based source of competitive differentiation to a new strategy built on these hidden assets.

And find a way it did. De Beers shifted the strategic focus from its obvious asset—the mines and the huge stockpile of rough diamonds—to hidden assets rooted in the company's unique relationship with consumers and customers and the power of the De Beers brand, which is virtually synonymous with the finest diamond gemstones. These assets and their power were hidden, because the success of the supply-driven strategy had long compelled a focus on the supply-based assets. This focus was intensified by the formal, almost secretive relationship De Beers had with its customers, who purchased gems in lots they could not view beforehand at what were essentially take-it-or-leave-it prices. Once the notion surfaced to turn the strategy on its head, ideas came fast and furiously, as if bottled up for years: branding, retail, jewelry design, consumer segmentation, and the umbrella marketing concept of De Beers as global custodian for all time of the diamond dream.

In the months that followed, De Beers outlined and began to implement this strategy, a radical departure from its profit model. The company liquidated 80 percent of its diamond inventory and invested in new forms of generating demand and in getting closer to each customer segment. It invested in brand building. It developed new product ideas for its distributors and jewelers and new consumer advertising campaigns to market those ideas. For example, De Beers developed the three-stone ring (to celebrate the past, present, and future of a relationship, or the birth of a child), diamond rings for men, and the "right hand" ring for women—a diamond ring women bought themselves as a symbol of independence.