The Self Destructive Habits of Good Companies…and How to Break Them

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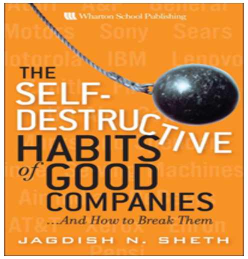
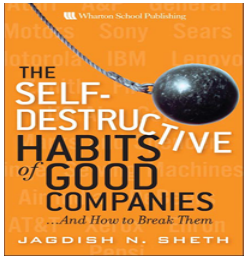


Why Do Good Companies Fail?

- The most insightful question I have ever been asked!

- Many good companies highly praised in <u>In Search of Excellence</u> in the eighties, were in serious trouble in the nineties. Why?

- Many companies used as role models for corporate leadership in <u>Good to Great</u> are also not doing as well despite Level Five Leadership.



The Declining Life Expectancy of Companies

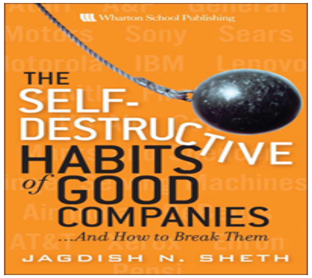
- One third of companies listed in the 1970 Fortune 500 List had vanished by 1983.

- The average corporate life expectancy in Japan and Europe is 12.5 years.

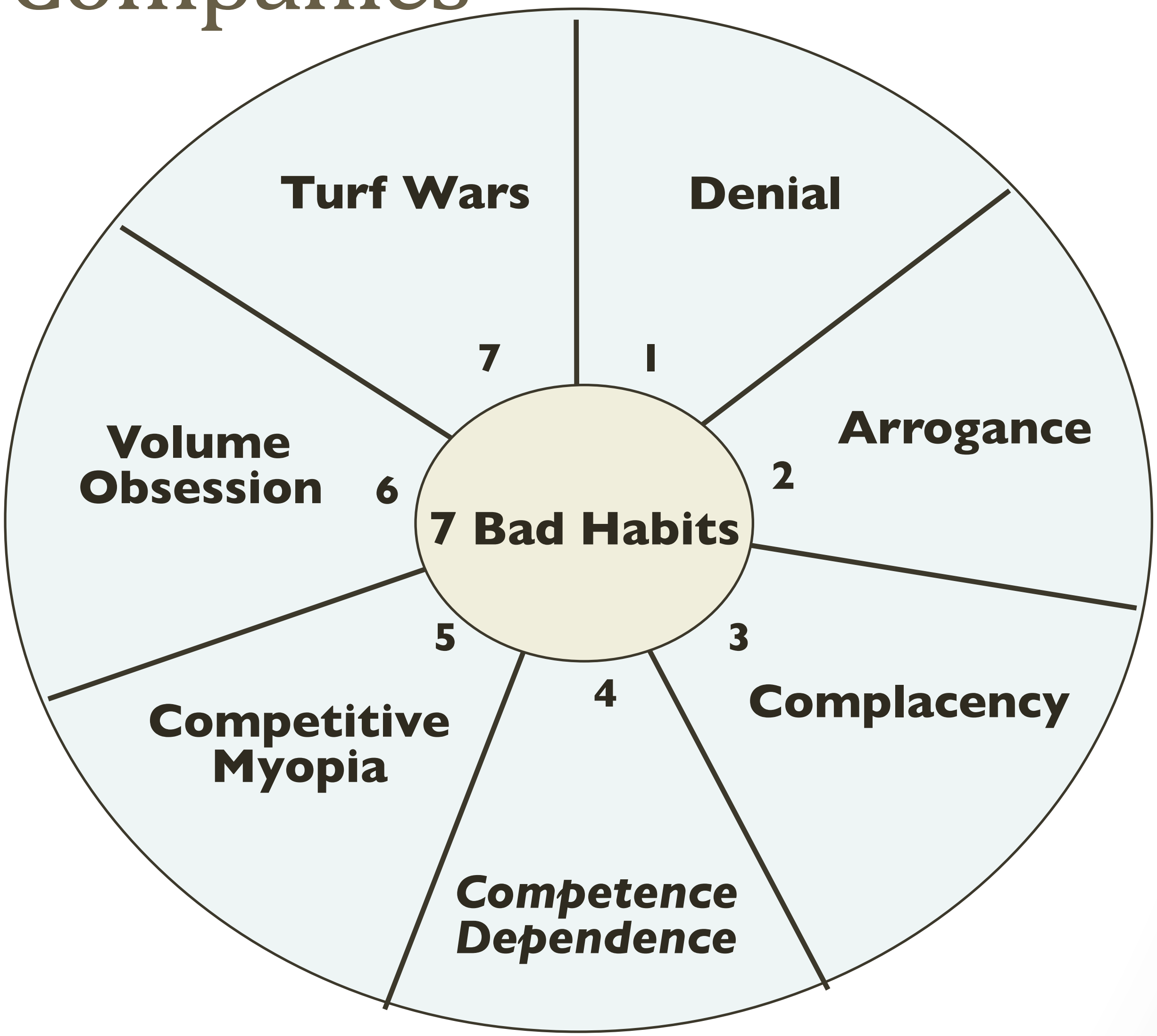
- Corporate life expectancy declined from 45 to 18 years in Germany and from 13 to 9 years in France and from 10 to 4 years in the United Kingdom.
(Source: Arie de Geus, The Living Company, 1997)

Is this an Inevitable Phenomenon?

- While it is predictable, it is not as inevitable as birth-growth-death cycle.
- It is also not a personal leadership issue. While some leaders are directly responsible for the decline or demise of a company, it is not a universal factor.
- What happens, I believe, is that companies develop bad habits as they evolve from survival to success and from becoming good to great companies.

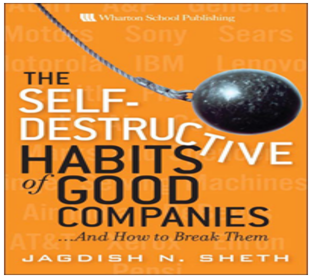


The Seven Bad Habits of Good Companies



Denial

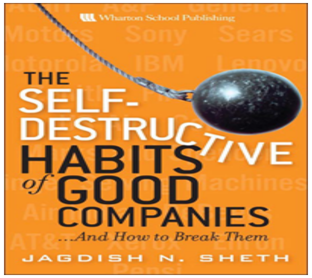
- Denial of new reality is probably the most prevalent bad habit of all good companies.
- Most companies succeed by being there. However, they create a cocoon of myth, ritual and orthodoxy to enhance company's success.
- Denials of three new realities are most dangerous: emerging disruptive technologies, changing consumer tastes and non traditional global competition.



Denial (cont.)

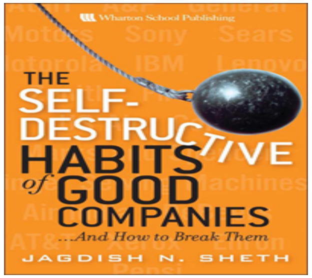
- A company is in a denial state when it believes “I am different”, “If it is not invented here it cannot be good”; and it uses rationalization or excuse for its fundamental problem.

- To break the Denial Habit, you must look for it, admit it, assess it and change it.



Arrogance

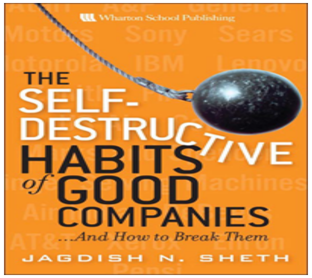
- Arrogance is an overblown self image of superiority and self importance.
- Under Alfred P. Sloan's successful leadership for 33 years, General Motors became arrogant.
- Companies become arrogant when they do exceptional achievement; when they are the David against a Goliath; when they pioneer an altogether new product or service; and when they are generally smarter than the other guys.



Arrogance (cont.)

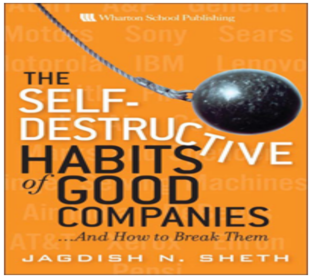
- The warning signs of arrogance are when you stop listening; when you flaunt; when you browbeat others and when you curry approval.

- The best way to break up arrogance is to rotate management into new challenges; implement non-traditional succession; diversify the talent pool; encourage outside perspectives; and if necessary, bring outside leadership at the top.



Complacency

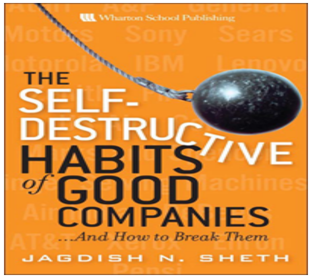
- Complacency is a sense of comfort and security that past success will continue indefinitely into the future.
- In other words, success breeds failure.
- The best example is the rise of complacency at IBM with its extraordinary success in mainframe computers.
- Complacency often arises when a company’s past success is due to its regulated monopoly position; or its distribution monopoly; or when you are chosen for success by the government; and when the government owns or controls the company.



Complacency (cont.)

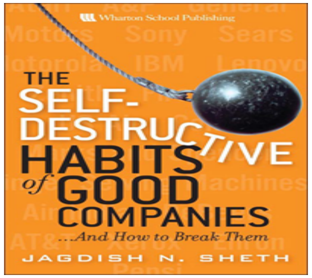
- The warning signs of complacency are when: you are in no hurry to make decisions; your processes are overly bureaucratic; you have a bottom up consensus-based culture; your cost structure is high; you are highly vertically integrated; and you have enormous cross subsidies across products, customers and functions.

- The best ways to break the complacency habit are to reengineer the company; reorganize it; divest noncore businesses; outsource noncore functions; or reenergize the company.



Competency Dependence

- When the core competency or the DNA of the company becomes a liability, it results in competency dependence.
- It is what I refer to as the curse of incumbency.
- It limits the vision like the Mao Zedung's frog at the bottom of the well.
- Classic examples of competency dependence are Singer sewing machines, A&P, Marks & Spencer and more recently Sears Roebuck.
- More contemporary examples include Xerox, Kodak and Microsoft.

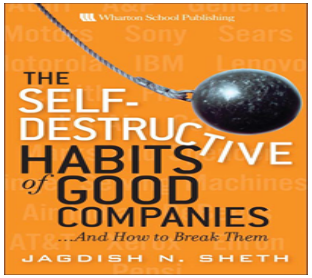


Competency Dependence (cont.)

- The warning signs of competency dependence are company's inability to transform itself; prevalence of malaise and inevitability; and when stakeholders are jumping ship.

- The best ways to break the competency dependence habit are to search for new applications and new markets.

- Also, moving downstream and upstream; developing altogether new competency; and refocusing resources on a global basis.

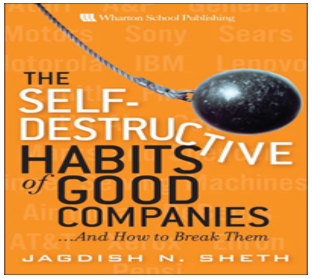


Competitive Myopia

- Competitive Myopia refers to the natural tendency of a company to narrow down the focus to one or two direct competitors.

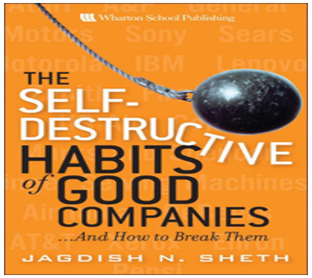
- This tendency is partly a consequence of natural evolution of the industry but also because of the co-location of major competitors into clusters.

- Competitive myopia also arises when the number one company is also a pioneer of the industry; and when the number two company becomes obsessive about challenging the number one company.



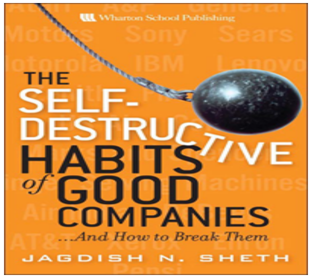
Competitive Myopia (cont.)

- There are several ways to break the habit of competitive myopia. These include redefining the competitive landscape; broadening the product or market scope; becoming industry consolidator; counterattacking non traditional competitors; and refocusing on the core business.



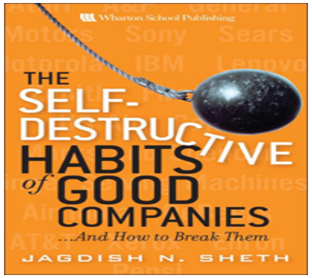
Volume Obsession (cont.)

- A company acquires the bad habit of volume obsession when:
  - It is the pioneer of a high margin business and margins collapse over time due to competition
  - It has a false understanding and metrics about economy of scale
  - It accumulates future obligations such as employee retirement and healthcare plans which are unsustainable
  - Its non operating costs (cost of capital, taxes, and dividends) become excessive.



Volume Obsession (cont.)

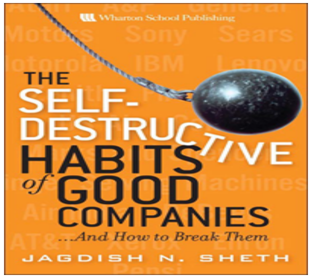
- There are several ways to break this habit: align costs with revenues; convert cost centers into revenue or profit centers; decentralize P&L to business and function units; shift vertical integration into virtual integration; outsource non core functions and activities; right size company management; implement target costing; practice lean operations; and become a world class customer.



The Turf Wars

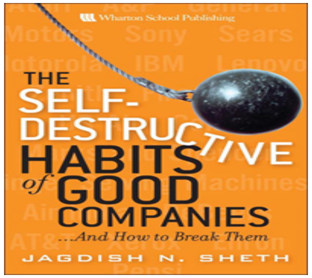
- The root cause of turf wars is the affinity and identity to a functional discipline above affinity and identity with the company and its vision and values.

- Turf wars arise due to organization design; when the company is dominated by a single functional culture; and when there is poor post merger integration.

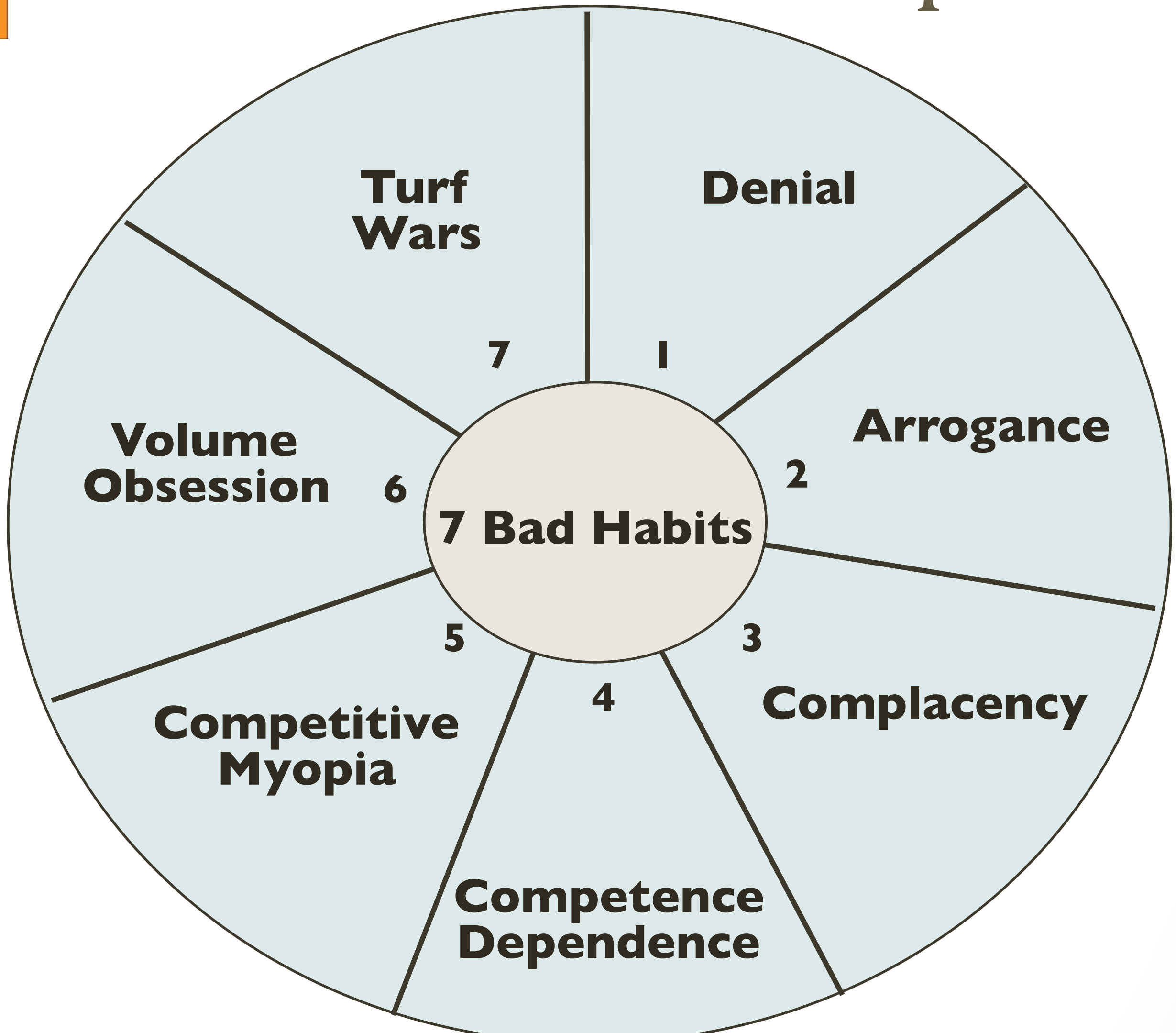


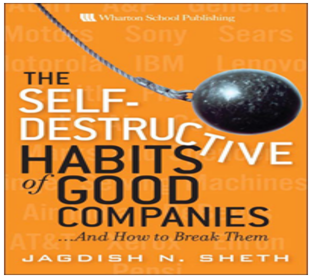
The Turf Wars (cont.)

- To break the habit of territorial impulse, it is important to invest in internal marketing; to push management out of their ivory towers; to create permanent cross discipline teams; to reorganize around customers or products; to automate and integrate functions; and to rotate leadership across functions.



In Summary: The Seven Bad Habits of Good Companies

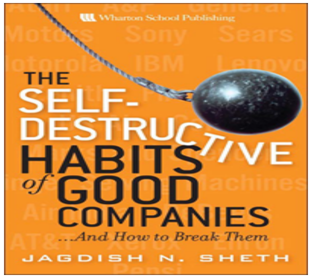




To Conclude

- All good companies on their way to success, acquire one or more of these seven bad habits.

- The Seven Bad Habits are:
  - Denial
  - Arrogance
  - Complacency
  - Competency Dependence
  - Competitive Myopia
  - Volume Obsession
  - Turf Wars



To Conclude (cont'd)

- In this presentation, I have discussed how each habit is acquired by good companies; what are the warning signals you should look for; and how to break that habit.
- Ultimately, it is all about leadership. The job of the leader is to constantly monitor the company's health and prevent it from learning bad habits. However, if a bad habit is discovered, it should be promptly destroyed.
- The best cure for a bad habit is no cure at all. It is preventing the company from acquiring the bad habit in the first place.