Growth can only come from the CEO

By

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To create value, it is necessary to grow faster than 10% a year. To reach such a rate, the role of Top Management is critical. Without it, growth ambitions cannot be achieved. Leaving them up to the organization generally results in failure. How can Top Management create a growth dynamic?

The value of growth

Value creation is not related to profitability. It is related to profitable growth. An analysis conducted on any stock exchange, no matter the period, will show the correlation between TSR [(1)] and growth (at a given level of profitability) (see Table).

This relationship between the two indicators is extremely strong: a point of long-term growth generates more than 1 point of TSR.

For a shareholder, this means that over 10 years an investment will have earned 2.5x the amount originally contributed for a TSR at 10%, whereas it will have earned 4x the amount for a TSR at 15%. The 5 points difference will have permitted to double the gain (net of the original investment). Hence, the stakes are significant. The most discriminating view in terms of value creation is not the magnitude of growth, but its length.

That is what groups like Inditex (Zara), H&M, The Home Depot, Assa Abloy, Nike, Hermès, Essilor or Safran have managed to achieve for more than 20 years.

The engines of long-term growth

To continue to grow over a long period, it is necessary to anticipate and predict the moves to make. The same business model can rarely support long-term, sustainable growth.

Therefore, different levers must be activated consecutively; they must be adapted to the positions of the company, the maturity of its markets, etc.: positioning on markets which are growing in the long term, innovation and new business models, expansion to new customers, internationalization in mature countries, globalization of the volumes associated with increased scale and experience effects, development in emerging countries, active concentration of the industry, expansion of the business scope to adjacent activities (upstream or downstream), macro mergers, redefinition of the business portfolio, diversifications, etc.

Businesses which remain bound to the same growth levers cannot grow in the long term. Such a business may enjoy a growth phase during which the levers it uses are relevant, but if it does not change its model, it will slow down together with its underlying market.

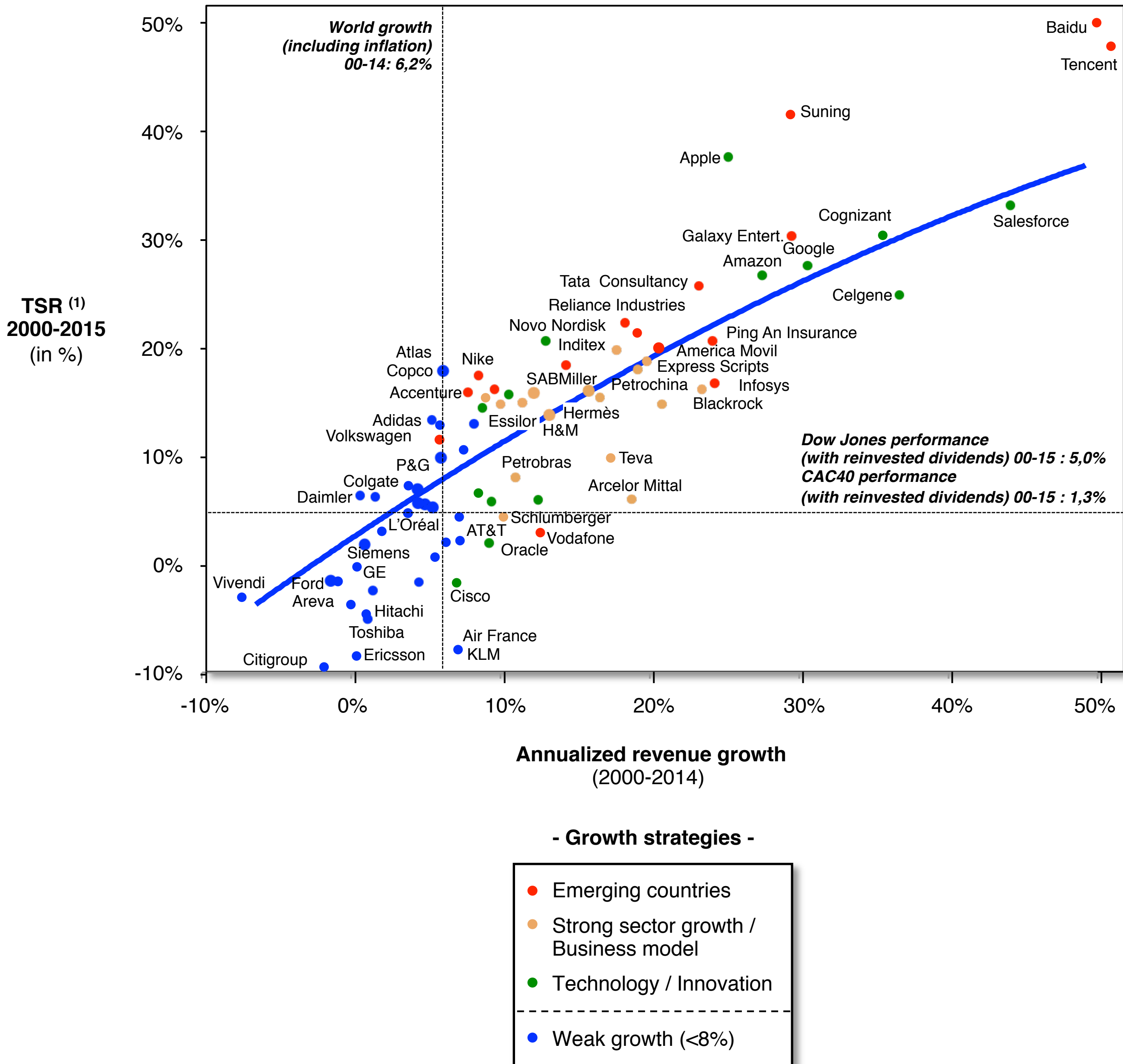
This is especially true when the Group is large and has historically enjoyed strong growth and success in its business model.

The key issue for Top Management is therefore the identification of the right levers and the positioning with adequate force and ambition.

The limits of the Organization as a growth vector

In our experience, organizations can only offer marginal changes and improvements within the limit or at the margin of their existing activities. They cannot be sources of long-term growth if they are not strongly pushed by Top Management.

- To create value, it is necessary to grow -



Note: Sample of the 150 largest worldwide listed corporations by market capitalization, completed with the main leaders by sector
TSR: Total Shareholder Return (capital gains or losses, dividends, free share distribution), assuming dividends are reinvested in the company's shares
(1) Start date: 31/12/2000 or listing date. End date: 30/09/15; (2) In local currency
Sources: Estin & Co analyses and estimates

It is unrealistic to ask divisions, business units, etc. to improve profitability, maintain strong positions, defend cash flows and deliver strong growth all at the same time. If the market is growing strongly or if the division has developed a business model which delivers structural growth, the division will be able to grow strongly and to have an impact on the Group. Otherwise, growth will be low.

As a general rule, organizations, naturally and as a result of performance indicators, focus on improving competitiveness and operational performance rather than on improving the growth dynamics.

Without major moves, competitiveness and growth in the coming years are determined to a large extent by choices and investments which may no longer be foregone.

Growth plans constructed as the sum of the ambitions of each division are generally inadequate. They do not allow for major changes in growth, in the business model, etc. By nature, they are too conservative. They lack ambition.

The role of Top Management

The role of Top Management is therefore critical to the success of growth strategies. It must be structured around:

- *The definition of the growth ambitions.* Growth comes to those who will and dare. Growth is a choice. Top Management must define the level of ambition in terms of TSR, growth and evolution of profitability. This choice is fundamental and must infuse the culture of the company.
- *The definition of growth options* and the choice of growth priorities. Most of large European groups are not growing because they are not positioned in growing businesses or geographies.

  The portfolio of businesses and geographies is a constraint in the short term. However, it is a choice in the medium and long term. This choice requires pulling out from some activities, redeploying resources and choosing the axes of growth–and as such, it requires foregoing other equally attractive ones. It can only be taken by Top Management.
- *An allocation of human and financial resources in areas of high growth.* Growth is not possible if less than 50% of investments is in growing areas. At the division level, this approach is inadequate because it is not followed upon or it is dilutive. Only a vision at Group level is relevant. This issue is of course an allocation of financial resources but also one of the most critical resource of management: its time.
- *A culture of growth.* Top Management must develop such a culture through its behavior, engagement levers and the management style of the company.

What to conclude?

Growing is a choice. It is the choice of shareholders and Top Management. If the CEO does not make this choice and is not a protagonist, then it will not happen. The organization generates profits and is paid to keep it that way and to make them grow, but only moderately. The CEO must impulse major changes, make trade-offs between investment opportunities and put in place the conditions for growth. Ultimately, he will make the difference for the company between being among the winners and losing independence.

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Estin & Co is an international strategy consulting firm based in Paris, London, Zurich, New York and Shanghai. The firm assists CEOs and senior executives of European, North American and Asian corporations in the formulation and implementation of growth strategies, as well as managers of private equity funds in the analysis and valuation of their investments.

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(1) Total Shareholder Return