Why do some companies stop growing?

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After years of steady and significant growth, at 10% or even 15% per year over 15 or 20 years, some companies stop growing. This has a major impact (see tables 1 and 2). For example, a company that used to grow at 10% per year over a long period and then suddenly stops growing sees its PER[1] drop from 30x to 10x – in the current low-rate environment.

One might think that such an evolution is inevitable. But it is not (see tables 3 and 4). What are the usual reasons for such a slowdown?

The good and the bad reasons

Bad reason: the market is no longer growing.

The market has matured. Growth is slowing down.

This is a bad reason. The company can continue growing by concentrating the market (organic market share gains or acquisitions), or by replicating its model in another geography/region, or by extending the playing field to other nearby segments, or by expanding in the same business at other stages of the value chain.

Major groups have achieved growth rates of 12% to 15% per year over 30 to 40 years in markets that are structurally growing at 3% by pursuing such strategies (AB Inbev, Essilor, Ecolab, Assa Abloy...).

Good reason: the business is being substituted by a better concept or technology.

The company's concept loses ground to other, more consumer-oriented concepts, or its technology is replaced by a new, more efficient one. The situation is challenging. The only question is whether to develop a new concept (or technology) – or even a better concept – and accelerate the substitution of the current business, or let others do it.

In that situation, some companies have a simple anticipatory strategy, particularly in fast-moving businesses: systematically buy out all small competitors before they become a threat and/or before their valuation becomes high (Google, Microsoft, Facebook, Cisco, or even Honeywell with Elster[2] , Coca-Cola with Honest Tea...).

Bad reason: potential acquisitions are too expensive.

Acquisitions for the purpose of further growth seem highly expensive, especially if they involve high-margin, high-growth leaders. The company may decide to defer such acquisitions until a more favorable opportunity window arises. As a result, growth slows, and valuation multiples decrease – both in absolute terms and relative to other competitors or acquisition targets. In just a few years, the company goes from concentrating the industry to being an acquisition target.

Growth through concentration (market share gains or acquisitions) is always valuable and can be costly in businesses where there is strong value to market share (scale effects…). In these

[1] PER (Price Earnings Ratio) : market capitalization to net income.
[2] 201 5 ; intelligents meters / intelligent measuring devices

businesses, any acquisition goodwill is offset by synergies, provided that at least 80% of them are rapidly implemented.

On the other hand, in businesses where there is no value to market share, acquisitions with a high acquisition premium are not attractive, as premiums are difficult to recover due to the lack of synergies. In any case, the acquisition is too expensive. It is the business itself that is not attractive in the long run, and it is better not to invest heavily in it.

Good reason: growth has become dilutive.

Profitability declines because the company can no longer recover its growth investments (sales, marketing, R&D costs…); the synergies needed to offset goodwill resulting from acquisitions do not materialize quickly enough; the company grows in client or product segments which are structurally less and less profitable; it over-invests in the wrong levers to force growth; or it does not invest sufficiently to take leadership positions and maintains mediocre profitability.

When profitability is high, trading off less profitability for more growth creates value. But if profitability falls sharply and reaching a level close to or below the cost of capital, it is better to halt growth, realign the business model, the management and the organization, the cost structures and the integration modes of acquisitions, and first and foremost restore profitability. There can be no value-creating growth without significant profitability.

Bad reason: the management has no incentive to develop the business.

Motivation systems and managers' objectives in the various business lines and regions are sometimes inconsistent with the group strategy, or insufficiently differentiated by activity. They simply need to be realigned.

Often, the company confuses the issues that fall within the remit of business line management with those that should be handled solely by the group's head office. At a certain size, when more than half of growth can only come from major acquisitions, it is better to ask field managers to focus on profitability, with moderate growth, and leave significant growth through acquisitions exclusively to head office teams.

Bad reason: the management needs to define or refine its vision of the company's growth model and the related challenges.

The growth model is not explicitly defined and shared. It is not regularly reviewed as the company's growth and size change. The proportion of organic growth, bolt-on acquisitions and major acquisitions remains opportunistic. There is no consensus on acceptable acquisition prices. There is no experience curve process for integrating targets and implementing synergies. Growth comes in fits and starts. Acquisitions turn out to be random successes or failures.

This is an essential reason, rarely explicit, for the slowdown and change in trajectory of a major group.

Good reason: the company has outgrown any new opportunities.

This situation is rare, but it does occur for large businesses, and all the more so that the company was successful in the past. The company has experienced strong growth and has already concentrated its market (Walmart…). The impact of a new development (organic or by acquisition) will only be significant (on sales, EBITDA or share price) in several years' time.

This situation can be anticipated, even if it is culturally counter-intuitive. A long-term growth strategy requires planning not only for the immediate five-year wave, but also for the next wave ten years ahead.

Otherwise, the cycles, and the fits and starts, of the revenue evolution weaken the development and internal dynamics of teams and talents. They also reduce valuation.

In certain extreme cases, if acquiring No. 3 or 4 is not sufficient or has already been done, a merger with No. 2 may enable growth to continue at an adequate pace for several years, thanks to complementarities and synergies (EssilorLuxottica, AB InBev…).

In any case, if the company has stopped growing, it is necessary to cut all costs of growth that built up over time but are not necessary anymore, and to maximize EBITDA and generated cash flows (reducing and optimizing marketing and R&D costs, drastically reducing the multiple layers of SG&A, rationalizing product ranges, rationalizing commercial costs, optimizing the capacities of industrial sites…). In many cases, this drastic reduction of the costs of growth can generate 2 to 5 points of EBITDA margin.

Good reason: financing growth becomes incompatible with the shareholders' investment thesis.

Given their portfolio strategy and risk profile, shareholders may wish to pay higher dividends to limit their exposure to the company, or to repay their debt (leveraged investment funds).

There can be no long-term growth strategy if there is no match between the company's strategy and its investment thesis, the acceptable level of risk and the shareholder's time horizon.

Restructuring the company's capital is a possible and sometimes necessary step in its long-term development. It is useful for the management and the board of directors to discuss several possible growth options on a regular basis, and not just the management's option, depending on the risk profile, liquidity and value for shareholders.

The challenges

The real challenge of long-term growth is not strategic or financial. It is cultural. A company's culture reflects its historical mix of its growth drivers and business sectors. There can be no growth without significant changes to this combination over the long term, and therefore without regular changes of its culture.

The levers

Growth in any business is always based on a combination of innovation or differentiation, market share gains, bolt-on acquisitions, major strategic acquisitions, and even mergers. Over a long period, this mix of levers characterizes the company's growth and development model, and determines its management style. This mix can be expressed analytically, and medium-term objectives set on that basis (% organic growth vs. % bolt-on acquisitions vs. % strategic acquisitions).

As a company develops, that its size increases, that it matures and concentrates its market, this mix needs to evolve. Initially, a company will grow through innovation, and twenty or thirty years later it will "end up" growing through acquisitions. In this respect, the larger the company, the larger or the more numerous (in the case of a build-up) its acquisitions need to be. Otherwise, they have no impact.

Nothing is more difficult for management than to make this mix evolve over time, because it constitutes the company's history, culture and managerial skills. But if this mix does not evolve, the company cannot grow.

The businesses

There is no such thing as a growing and attractive business for all eternity. With the exception of new, highly structuring businesses, a company that grows over the long term starts out as a specialist, and over the long term becomes a group or even a holding of different businesses, some of which develop rapidly while others reach maturity. The fit between the company and a particular business, even if defined in the broadest sense, becomes less pronounced, especially as regular trade-offs have to be made within the portfolio.

Management modes, governance modes and motivation modes of managers and teams must evolve accordingly, as must the company's core identity. As with growth levers, if this mix does not evolve over time, there can be no long-term growth.

Long-term growth involves changes in the strategy, management, organization, culture and even the shareholding structure.

Every company should regularly check that its growth model is still fit for purpose, so that it can continue growing in the years to come. In this respect, it is best to be paranoid: what are the reasons why the company might stop growing in the medium term? What needs to be adjusted now?

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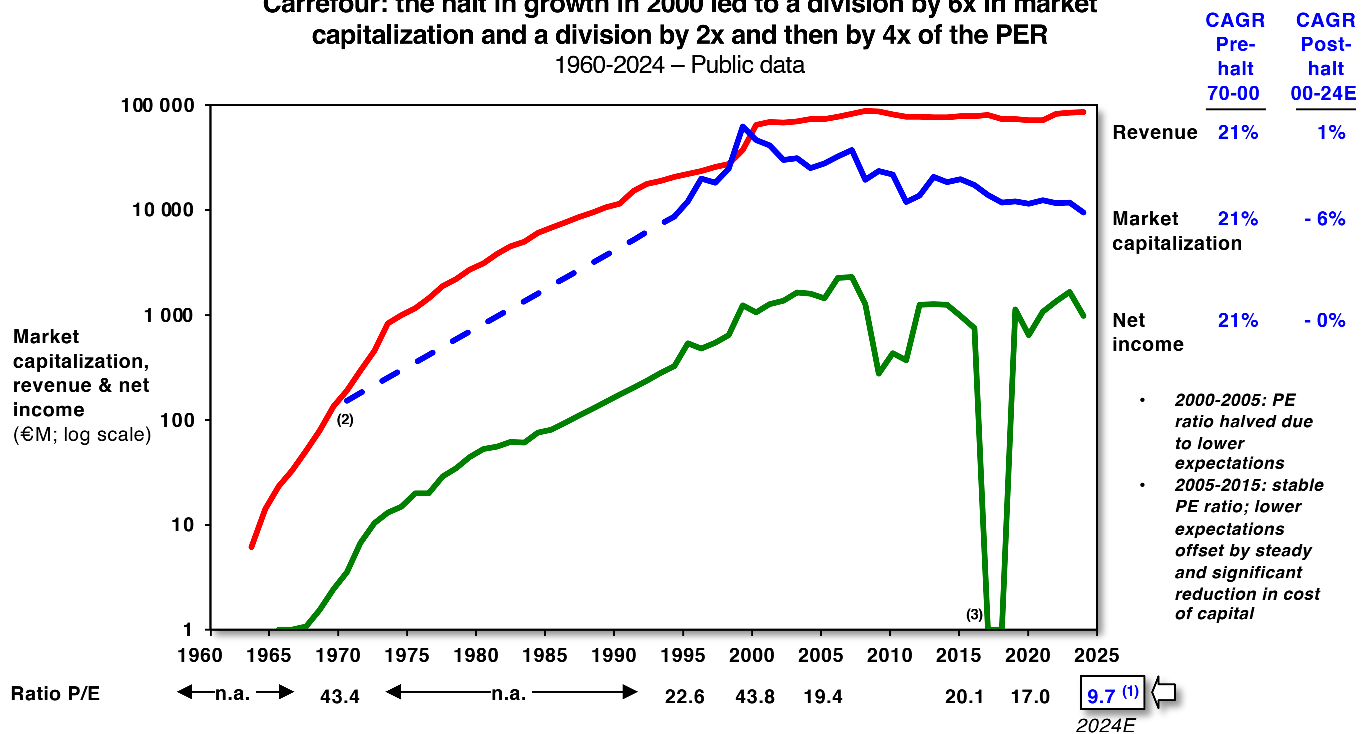
Estin & Co is an international strategy consulting firm, with offices in Paris, London, Zurich, New York and Shanghai. The company assists senior executives of major European, North American and Asian corporations with their growth strategies, and managers of private equity firms with the analysis and valuation of their investments.

- Table 1 -

Carrefour: the halt in growth in 2000 led to a division by 6x in market capitalization and a division by 2x and then by 4x of the PER

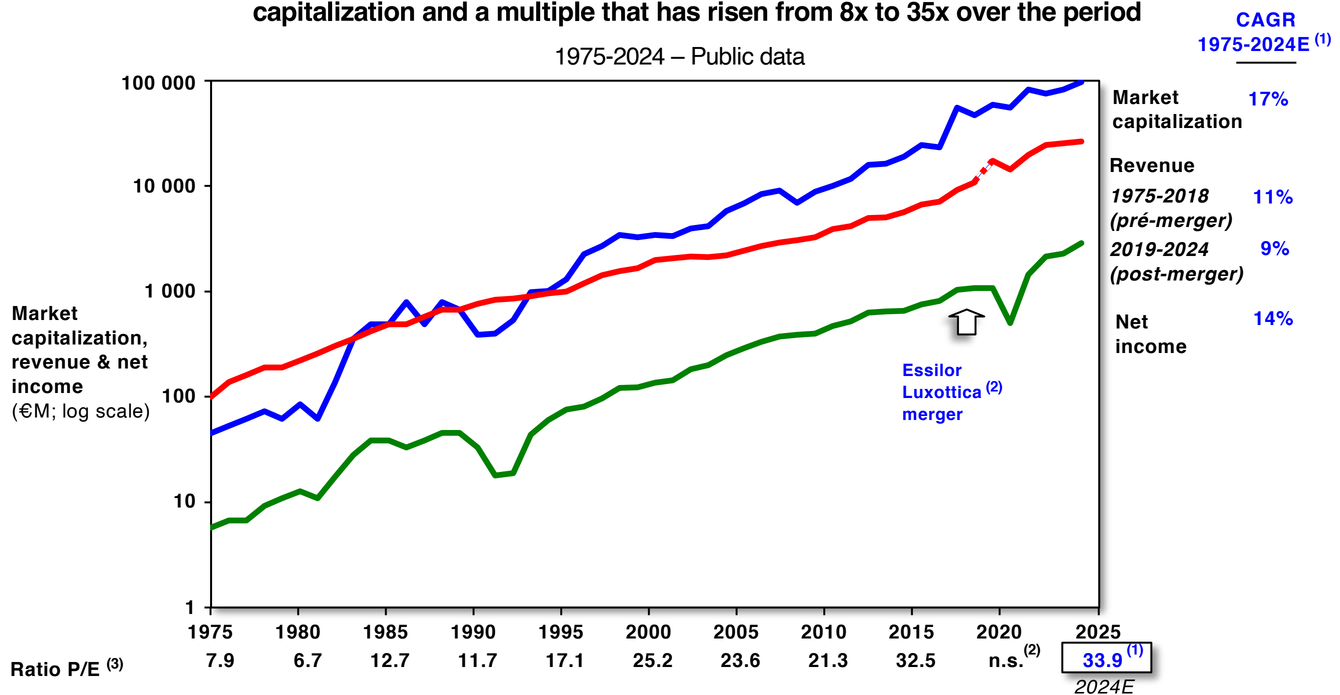
1960-2024 – Public data



Note: constant Franc/Euro exchange rate of 0.152 applied to pre-1998 data.
(1) 2024 estimates based on brokers' consensus at August 23, 2024. Market capitalization at August 23, 2024; (2) At the time of its IPO, Carrefour was valued at FF 1B, or €156M; (3) 2017: - €530M, 2018: - €561M; "Carrefour 2022" restructuring plan
Sources: LSEG Workspace, desk research, annual reports, Estin & Co analysis and estimates

- Table 2 -

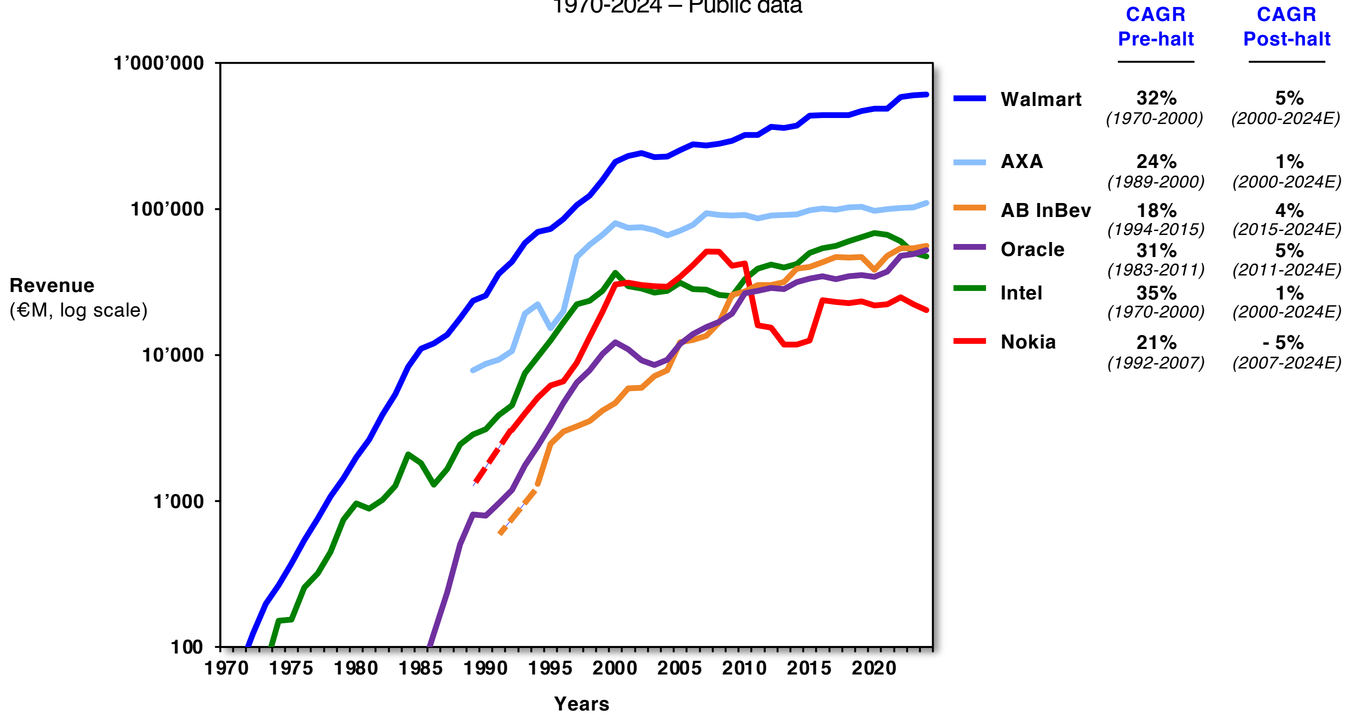
Essilor: continued growth over 50 years has led to a >2,000x increase in market capitalization and a multiple that has risen from 8x to 35x over the period



Note: financial results and market capitalization of Essilor, which merged with Luxottica to become EssilorLuxottica as of 2018; market capitalization CAGR of 16% p.a. over 1975-2024E, adjusted for the merger with Luxottica (view of a historical Essilor shareholder)
(1) 2024 estimates based on brokers' consensus at August 23, 2024. Market capitalization at August 23, 2024; (2) Net income 2020: 85 M€ (graph not to scale); P/E ratio 2020: 659x; (3) Historical P/E ratios over fiscal years
Sources: LSEG Workspace (2017-2024E), Bloomberg (1990-2017), Essilor investor presentations (1975-1990), Estin & Co analysis and estimates

- Table 3 -
Examples of companies with strong growth over a long period, then a halt in growth

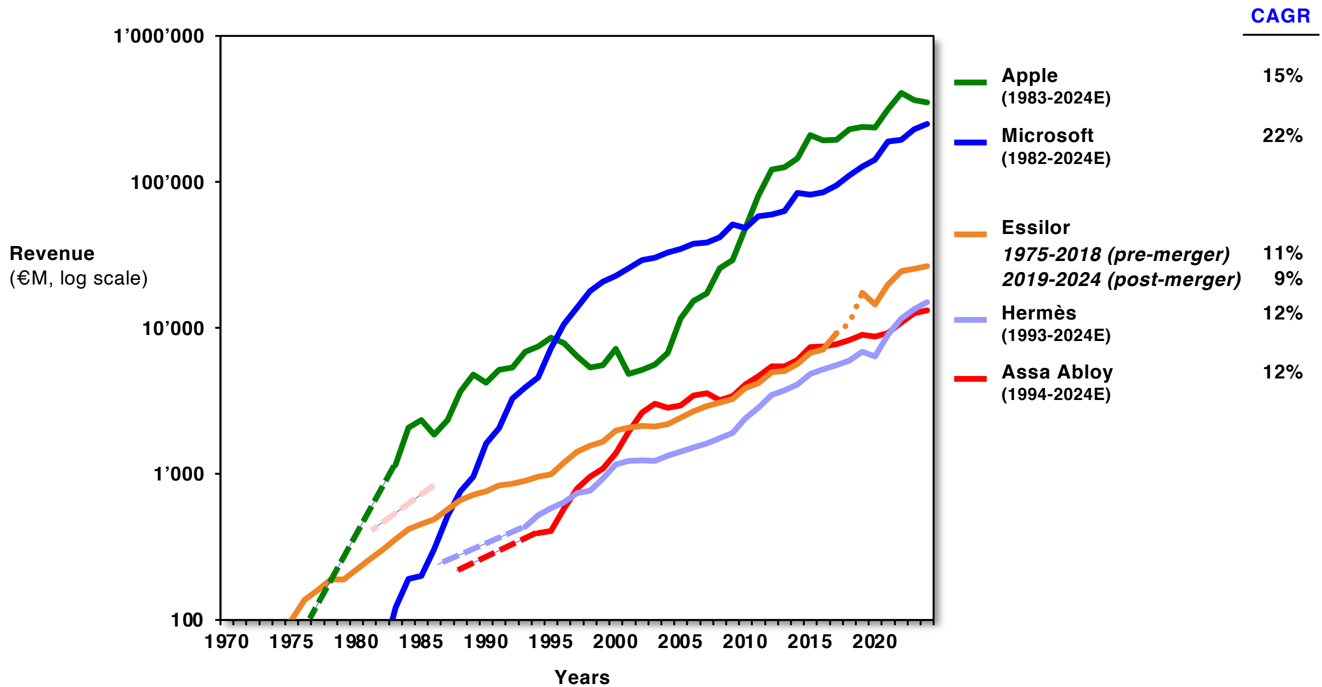
1970-2024 – Public data



Note 1: at current exchange rates. 2024 revenue estimates based on brokers' consensus of August 23, 2024.
Sources: LSEG Workspace, IMF, Estin & Co analysis and estimates

- Table 4 -
Examples of resilient high-growth companies (to date)

1970-2024 – Public data



Notes: at current exchange rates. 2024 revenue estimates based on brokers' consensus at August 23, 2024.
Sources: LSEG Workspace, IMF, Estin & Co analysis and estimates