

BUILDING BUSINESSES IN THE NEW ECONOMY

Q&A WITH PROFESSOR LYNDA M. APPLGATE



HARVARD
BUSINESS
SCHOOL

EXECUTIVE EDUCATION

Battered by contracting markets and frozen credit, many businesses today are fighting for survival. Indeed, the current crisis provides a mandate for restructuring. But survival is not the end goal, says Harvard Business School (HBS) Professor Lynda M. Applegate, head of the Entrepreneurial Management Unit. In fact, cost cutting and restructuring are simply the first steps in repositioning and leading your company and industry through the crisis and in defining how business will be conducted in the future. In this interview, Professor Applegate explains how large and small companies can position themselves to survive—and thrive—in turbulent times.

Q: Why is innovation important today?

The global financial crisis we are experiencing provides a sobering reminder of what happens when innovation fails to drive economic growth. For over a decade, money from around the world has poured into the United States. Despite massive investments, when adjusted for inflation, U.S. GDP grew slowly with much of the growth from professional and business services—including real estate, financial services, and outsourcing—and from government. What's more, inflation-adjusted wages stalled for many, even as consumer spending increased. Where did the money for all this spending come from? Companies borrowed, governments borrowed, and families borrowed. Savings rates approached zero. Commercial lenders sold their loans to investment banks where they were converted into securities and sold again and again. We can't fix our current economic problems by simply spending more money to buy bad debt. Rather, we need real innovation that creates jobs and drives productive economic growth. Companies that survive the financial crisis by identifying and exploiting innovation will serve as economic growth engines in the future—and will be the industry leaders of tomorrow.

Q: Which industries offer the most opportunity?

Over the long run, opportunity exists in every sector. In the short term, I recommend that companies do what we always advise when searching for opportunity—look to the marketplace. Think of the economic crisis as a disruptor to the status quo and look for areas of “pain.” For example, the financial services industry is in shambles, yet pockets

of opportunity exist for specialists who provide leasing, payment, and foreclosure services. In healthcare, nursing services, community social services, mental health services, and home healthcare services are on the rise. One executive recently told me that his firm's business training services were up over 400 percent since fall 2008. Government funding programs also present opportunities. And, while oil prices continue to rise and fall, energy services firms are seeing rapid growth—especially those firms that provide services to both traditional and emerging “clean tech” energy sectors. In the IT industry, opportunities are arising to replace high-cost data centers and incompatible networks with lower-cost web services platforms. For example, Amazon.com and Google recently stepped up their efforts to deliver state-of-the-art, customizable web and information services that support small-to-midsize businesses. While many of these are short-term opportunities, they can build important foundations for longer-term productive economic growth.

Q: Can shrinking companies position themselves for a better future?

Opportunities are at an all-time high, but the question is how companies will pursue those opportunities. Cutting back and hunkering down may get you through the short-term crisis, but will not position you to be a leader in the future. That's why you need a mindset that says: “I'm not just going to survive—I'm going to thrive.” Obviously, you must be realistic about what you need to do to survive in the short term, but the trick is to do those things in a way that moves your strategy forward.

BUILDING BUSINESSES IN THE NEW ECONOMY

Q&A WITH PROFESSOR LYNDA M. APPLIGATE



HARVARD
BUSINESS
SCHOOL

EXECUTIVE EDUCATION

Even leaders who need to make very deep cuts can think strategically about where the business will be and how they might build for the future. A great example is Lou Gerstner at IBM. When he took the helm, he had to take \$7 billion out of the company's cost structure in less than two years—not an easy task. He listened to customers who told him that their key area of pain was the difficulty of integrating the “islands of automation” throughout their global companies. Gerstner, himself a former IBM customer, immediately recognized the opportunity. He reversed the previous CEO's decision to break up IBM and announced a new strategy, which he called “One IBM.” Having planted that stake in the ground, the company carefully chose what businesses to divest—its energy was then pointed toward the One IBM theme. Processes were streamlined and layoffs were targeted to enable the company to go to market as One IBM. Not only is IBM surviving, it is thriving once again.

In times of crisis, owner-managed businesses also are responding to the need for “disciplined innovation.” Business owners, for example, report that the crisis has helped them make changes in mature businesses, which they've been trying to make for a long time. These changes not only are being made inside the company, but also involve customers, suppliers, and business partners. “We find that our customers and suppliers are much more willing to partner with us to streamline operations,” noted one business owner. “We're taking out costs and simplifying how we do business. In the process, we're creating tremendous long-term potential.” Another owner explained that: “Our strong cash flow and lack of debt have positioned us as a survivor. Now we're in an excellent position to renegotiate with larger suppliers.”

Once operations are stabilized, business owners are pursuing opportunities while carefully managing risk. As one owner reported: “We're actively looking to buy up undervalued businesses in growth areas that we've been actively evaluating for sometime.” Still another owner related that: “The upheaval of the branded investment houses has created disruption that is the biggest opportunity of my lifetime. Because we're

a 30-year-old, independent and privately held financial services advisory firm that is debt free, we're leveraging current capabilities to dramatically expand market share, enter new markets, and deliver new services.” A Latin American business owner noted that: “We're using the crisis to expand throughout the region.”

Q: Is a recession really the time for a company to make major changes?

Change is coming anyway, so leaders need to take control. At HBS, our motto is: “Never let a crisis go to waste.” The major dislocations happening in industries around the world give companies a great opportunity to lay the foundation for the future. Because everyone acknowledges the current crisis, they often readily accept restructuring and changes that were not possible in the past—even if change has been needed for some time.

When approaching change in these turbulent times, don't go searching for a change specialist. What you need are leaders with a strong plan for how the company is going to survive today and succeed in the future—leaders who can communicate the first few steps on the path forward and rally employees, customers, and partners to work together in making the tough decisions and taking the steps needed. Success will depend on leaders who are able to stabilize the company as they identify and exploit opportunities, find new market niches, create innovative new offerings, and restructure and reposition the company. Given that we don't know how long these economic problems will last, it's important to carefully manage risk when pursuing opportunities. Staging commitments to reduce uncertainty and risk, while paving the way for new business growth in the future, is critical. Indeed, innovation has always been about managing uncertainty and risk. The only difference today is that uncertainty and risk are not just tied to the business opportunity you are pursuing—you also must identify and manage risk that is tied to the global economy.

BUILDING BUSINESSES IN THE NEW ECONOMY

Q&A WITH PROFESSOR LYNDA M. APPLIGATE



HARVARD
BUSINESS
SCHOOL

EXECUTIVE EDUCATION

Q: How should today's economy change our view of innovation?

Some people think about innovation and new ventures as a side business to running the real business, but the economic downturn takes the need for innovation to a new level. In this environment, "business as usual" is not the answer. Companies must work aggressively to innovate and make the kinds of changes that are critical to success today and in the years to come. They must consider cost cutting as one step on the journey to future success. In a sense, every business, large or small, needs to think of itself as a "new venture" right now. This is a time of unprecedented opportunity to rethink offerings, markets, business processes, and organizational structure—and to improve them to achieve growth.

Q: What kinds of companies are better positioned to make such changes?

Owner-managed companies are typically more nimble and can often make change happen more quickly, but they also may be more dependent on large firms for major sources of revenue. Interestingly, this can mean that owner-managed businesses may be the first ones to feel the economic squeeze, which increases their motivation to find new opportunities. We see an interesting pattern at HBS Executive Education. Many small business owners who come to our programs tell us they are finding today's market to be the most fertile ground for innovation that they've ever seen, and they are impatient to build the skills needed to take advantage of the current opportunities. The rallying cry for turbulent times is: "Let's not just survive—let's thrive."

.....

Lynda M. Applegate, Martin Marshall Professor of Business Administration. Head of the Entrepreneurial Management Unit, member of the General Management Unit; faculty chair of the "Owner/President Management program," "Building Businesses in Turbulent Times," "Building Ventures in Established Companies," and "Launching New Ventures: Jump-Starting Innovation for Entrepreneurs and Business Owners."

.....



For further information, please contact our client service specialists at:
Executive Education Programs
Harvard Business School
Soldiers Field
Boston, MA 02163-9986 U.S.
Email: executive_education@hbs.edu
Telephone: 1-800-HBS-5577
(outside the U.S., dial +1-617-495-6555)
Or visit: www.exed.hbs.edu