



Detecting and Surviving Seven Silent Growth Killers

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Midsized firms are the foundation of the American economy.

Today, there are almost two hundred thousand companies with revenues between \$10 million and \$1 billion—midsized, as defined by Ohio State University’s Fisher College of Business.

These firms account for about a third of U.S. GDP and a third of all U.S. jobs, and yet they are often overlooked compared to their smaller and larger brethren. Like all businesses, midsized companies are grappling with the recovering economy, growing global competition and the incessant demands of technology, but they also face unique challenges that smaller and bigger firms do not experience.

Unlike dry spells in innovation, quality defects and mistakes made in entering new markets, many of the problems that midsized companies must deal with are not obvious. These problems grow out-of-sight in the dark recesses of the midsized organization, unrecognized by management in their daily routines until they emerge as full-blown crises that can threaten the present and future of the business. I refer to these special afflictions of midsized companies—seven in all—as silent growth killers.

These silent growth killers sneak up on leaders at midsized companies just as high blood pressure and high cholesterol can creep up on us, often unnoticed, and later cause massive complications. Just as those medical conditions, untreated, can lead to an early demise, executives who fail to prevent or address these silent growth killers may see their businesses collapse in a dysfunctional heap. But many midsized companies have dealt with them well, and by doing so have grown strongly, profitably, and in many cases spectacularly.

Why Midsized Firms Are Different

Apart from the somewhat arbitrary revenue differentiator, what makes midsized companies special? What makes their problems—and the solutions to those problems—unique? I have found six factors in the makeup of midsized companies that set them apart from both larger and smaller companies and cause the distinctive challenges they face:

- **A low tolerance for risk.** Midsized firms have much more to lose than startups. They have many more employees that depend upon them, and their owners have a larger portion of their personal wealth at stake. Midsized companies just aren't big enough to survive too many missteps. Their investors keep tight watch on profits and growth to fuel investment value. Startups, by contrast, are all about risk. If they fail, everybody goes out and gets a new job.

Their investors know the risks and, in the case of venture capital, have diversified portfolios to manage them. Deep-pocketed Fortune 500 companies, of course, have the resources to experiment with new products and even new business models. They can assume great risks because they can write off multimillion-dollar failures. But in bootstrapping their small firms into midsized companies, many midsized company executives have survived hard times by being frugal. Such frugality makes them risk-averse and often holds them back from getting to the next level. That often includes avoiding making risky but crucial investments in talent, infrastructure, R&D, and brand building.

- **High barriers to internal collaboration.** Midsized companies typically have more than a single office, and their dispersed teams must communicate in order to conduct business. Yet they aren't so large as to be able to afford taking their managers away from their daily tasks to attend the off-sites or all-hands meetings like larger companies. Nor are they rich enough to pay for in-house organizational development teams or the other tools that big businesses use to keep top management in sync. Startups, on the other hand, typically have all their people in one place, focused on the same or closely related tasks at the same time, brewing their coffee in the same kitchen. Collaboration is easy when you're gathered around one water cooler. Midsized firms are caught between critical mass and unencumbered nimbleness.

- **Few ways to develop talent.** Midsized firms (especially those growing quickly) typically don't have large HR functions to develop leaders, or the cash to invest in successor positions or training the way large corporations do. In slower-growing midsized firms, top managers can't (or won't) create adequate opportunities for advancement for younger talent, their future leaders. Midsized companies without multiple business units can't give aspiring leaders P&L responsibilities. In just about all midsized companies, it is rare to find executives who can spend time mentoring. Everyone is too busy doing his or her own job, making the business run.
- **Less investor patience for leaders learning on the job.** When venture capital or a private equity firm backs a business, there's a hard horizon for an expected return. Investors typically believe that the leaders of the businesses they put their money behind should have the skills they need to succeed. They're not interested in waiting for them to develop. If the leaders don't produce within the investors' timeline, they will be replaced. This can lead to a turnover rate at the top levels not experienced by smaller businesses (often run by their owners) or larger companies (in which leadership training is a core activity).
- **Less strategic thinking.** Big firms have chief strategy officers and teams dedicated to strategy, M&A, and corporate development. Startups have a central belief in one opportunity they race to embrace. Midsized firms, however, busy working to make the business they already have run profitably, often have to do their strategic thinking on the fly, with the

part-time efforts of the CEO. Maybe, once or twice a year, they'll have an offsite at a nearby hotel. In general, midsized firms don't have the time, inclination, and skills to consistently think strategically.

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- **Less seasoned talent.** In midsized companies, a high percentage of owners, CEOs, and other leaders began at the bottom. They rose with the business, which means they may never have acquired or got the chance to polish the executive skills you see in Fortune 500 companies: disciplined planning, financial acumen, relationship building both inside and outside the business, talent development, mentoring, and leadership. Take any one of my law firm clients: great lawyers but no business training or experience. Or a retail client who started a business in college and grew it to over \$300 million revenues in 12 years, without ever holding more than a summer job as a teen.

Like the soil and climate that determine the evolution of the plants and animals in a specific region, these six limitations create the environment that affects the life and growth of the midsized firm. They also provide the ideal conditions for the emergence of the seven silent growth killers.

The Seven Silent Growth Killers at a Glance

Not every midsized business wants to grow, but in my experience, most need to show some growth to remain healthy. Many aspire to grow significantly. Only some succeed. The others fall victim to one of the seven silent growth killers. They can slip in and set up shop in your boardrooms, executive suites, lunch rooms, sales floors and factories before you even know they're there. Before you can begin to guard against them, you must learn to recognize all seven, then understand the critical moves you must make to avoid them altogether or to mitigate their effects. They are:

1. Letting Time Slip-Slide Away | This growth killer is silent almost by definition because it has to do with that most ephemeral and subjective thing, time. When an organization loses its sense that time is a limited resource, deadlines on critical projects get pushed back with few if any consequences to the individuals and teams responsible. It's very easy to overlook time that slip-slides away, especially if a CEO allows it. In order to overcome this killer, leaders must create

a sense of urgency around deadlines by tying projects to the calendar—combining time boxing, expectations, prioritization, and intermediate deadlines. This creates clarity and ongoing pressure, thereby leading to greater appreciation for time and better results.

For example, despite the best of intentions, Goddard Systems Inc., a fast growing \$530 million revenue Pennsylvania-based national franchisor of The Goddard School® preschool system, found itself in 2007 missing deadline after deadline as it tried to rewrite its franchisee training manual. New CEO Joe Schumacher recognized the fundamental problem: at Goddard Systems, Inc., time was not appreciated as a valuable resource.

Schumacher required his management team to develop strong business cases for each project. That helped everyone differentiate high-priority initiatives from low-priority ones. And it forced senior managers to identify precisely the resources their projects required. Schumacher also made rewriting the training manual a real priority because he knew that rapid expansion was just around the corner, and when that happened, if Goddard didn't have the new manual, training (and performance) would suffer. Responsibility for getting it done was assigned. And it got done.

2. Strategy Tinkering at the Top | Startup companies must always be ready to tinker with their strategy. Because they are trying to tap previously unrecognized or unmet needs, they must tweak, adjust and change course whenever they discover that those needs aren't exactly what

they expected. Big companies simply don't tinker. They study, analyze, plan and pilot. But for a midsized company, tinkering with the business's core strategy can be deadly, particularly when changes are made without proper research, planning, and testing. Any changes made should be necessary, well-planned, and in alignment with organizational goals. To ensure this is true, leaders should conduct strategic planning and operational planning as separate tracks and with a high level of discipline.

Consider Lori Bush, CEO of \$300 million Rodan + Fields, a San Francisco-based skin care company selling through the direct sales channel. She was facing inconsistent results in late 2009 from business development efforts across the country. Bush's sales leader wanted to continuously spike the company's commission plan with temporary short-term bonuses, but that had risks and big costs. Another option was to try a new behavioral training method that might help low performers improve and identify future high performers. Instead of diving into one or the other, or both, she devised measured trials for each strategy. The behavioral training program became a clear success, turning a stubbornly underdeveloped market into the top region in the U.S. Sales leapt 300 percent in that region in the fall of 2010. This strategy became a clear driver and was quickly expanded, and today the firm continues to grow rapidly.

3. Reckless Attempts at Growth | In the effort to scale, organizations face increased risk and expense. If the attempt at growth costs too much and the revenue doesn't match the expense, a nasty cash crunch will materialize. There are three ways to take the "reckless attempt" out of growth. They are: gaining a deep understanding of your market; developing well-founded forecasts, and making evidence-based assessments of your ability to execute.

BlueArc, a venture-backed data storage equipment manufacturer, made a prudent attempt at growth and succeeded. They built a cash reserve despite having to make large, risky investments to grow in turbulent times. In 2008 BlueArc's CFO, Rick Martig, and BlueArc's other executives had been getting out of their offices and into the company's fast-changing marketplace. They had a gut feeling that to grow they needed to add a mid-priced product to complement their high-end, high-performance product portfolio. This would require R&D investment even as cash from ongoing operations was dwindling.

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But a gut feeling, even backed by BlueArc's intelligence-gathering, wasn't quite enough. Fortunately, several of BlueArc's larger competitors had started down the path to IPO or had been acquired, so their financial and operating results suddenly became visible. Their financial data reinforced BlueArc's belief that it needed that mid-priced product. On the strength of all those inputs, BlueArc raised \$7 million in venture debt, which enabled it to complete the R&D work to design, produce and bring the product to market. At the same time, the company cut G&A expenses and even some of its sales staff. Still, the senior team knew it needed more cash to continue investing in the business, and it raised another \$21 million.

BlueArc's new product became a major success. That enabled it to hit its targets and get it to break-even in EBITDA eighteen months later. As it prepared for its own IPO in 2011 (by that time, BlueArc's revenue was \$86 million), it was acquired by Hitachi Data Systems at a very good revenue multiple.

4. Fumbling Strategic Acquisitions | Companies often pursue growth by buying it. Sometimes, that doesn't work out. When a corporate giant makes a bad acquisition, it usually has plenty of capital to absorb the loss. But when a midsized company makes a poor acquisition—even if the acquired firm is small—it can knock the company off course for years. Making a good acquisition is less about the deal and the closing, and more about what happens afterwards: the integration process and execution of the acquisition plan. To beat the odds against acquisition success,

leaders must carefully consider four critical factors: alignment with the buyer's core strategy; the M&A experience level of the buyer's executives; the fit between buyer and seller as to scale, culture, and operations; and lastly, the discipline and focus of the integration process.

Consider EORM, a San Jose-based environmental, health, safety (EHS), and sustainability consulting firm founded in 1990. Until 2010, the 75-person, \$13 million revenue company had shunned acquisitions. But in recent years, growth had stalled and top managers decided they needed to include acquisitions as a part of their growth strategy.

EORM created clear guidelines for acquisition targets. They had to be companies performing the same or related EHS and sustainability consulting services. They had to be small (with ten to twenty employees), and based either in Southern California or the East Coast (to support geographic expansion).

EORM launched a disciplined search following those criteria. In late 2010 the firm acquired a second target company in Southern California, Sigma Engineering, in August 2011. EORM now has a critical mass in a target geography, and penetration in two new sectors (corporate retail and public sector) and new skills in important service areas such as environmental site assessments and remediation. Since then, EORM has grown to 175 employees and \$27 million in revenues in 2013, and it is continuing to include acquisitions to grow with a second one targeted for 2015.

5. Operational Meltdowns | Small firms tend to notice problems in production, distribution, marketing, sales or other critical processes early on. They have to. If they don't, they'll wake up to find themselves out of business. Large companies typically have established written plans and performance metrics and people who are well-paid to monitor them. Midsized companies, however, usually lack both rigorous processes and dedicated operational troubleshooters. They are often surprised and overwhelmed by meltdowns in key processes, especially those that come from the always-difficult process of automating systems. Leaders must be able to recognize four early signs that an operational meltdown is looming. They are: an overbearing sales culture; an outdated IT or physical infrastructure; a skills shortage; and customer concentration.

For example, Dave's Killer Bread, based in Milwaukie, Oregon, avoided a meltdown despite an overwhelming, unexpected surge in demand for its products. The company was launched in late 2005 with revenues of \$3 million. Demand exploded, and by summer 2006, the company had maxed out capacity in its 15,000-square-foot bakery. What Dave's needed was a new facility, but it didn't have the capital.

The company could have gotten that capital by saying yes to several major national retailers that were lining up to sell its bread. But it said no again because it had done the math and knew its budget didn't provide for the investments that would allow it to honor those commitments. Too many firms in Dave's position might have said yes, figuring that they would have months to figure

out how to make it work. They might have taken the money, built a new facility and found out later that the market had evaporated or they didn't have the skills to run a larger operation.

After initially struggling to get financing, Dave's began planning for a new facility in late 2006 and borrowed \$2.1 million to build a new 50,000-square-foot bakery capable of producing 3,000 loaves per hour. By 2011 it grew to a \$50 million business. In March 2013, Dave's sold 50 percent of the company to a private equity firm at a very good multiple to help capitalize an ongoing national rollout.

6. Liquidity Crashes | Running out of money can happen to anyone. A dramatic economic downturn, the loss of a key customer and other unexpected events can catch even the most experienced CEOs unprepared. The keys to emerging from a liquidity crisis include building a strong balance sheet, monitoring cash flow, making smart and timely cost reductions (while avoiding harmful ones) and making sure you have the right investors in the business to begin with. You don't want impatient capital in times that require patience.

MBH Architects, a leading Northern California architecture firm best known for its design work for retail stores, had consistent growth and profits since its founding in 1989. It had had a banner year in 2007 (\$26 million revenues) and a staff of 205. To accommodate its growing business, the firm moved its headquarters and borrowed \$3 million to make tenant improvements. Then

the great downturn slammed the firm in 2008, and by the end of 2009 revenues had dropped 83 percent. The company had to lay off 74 percent of its staff. The bank froze MBH's line of credit in December 2008, tying management's hands and forcing a million dollar capital call. It couldn't pay the rent on its new headquarters; key clients stopped all work.

MBH's founders cut costs hard and fast, monitoring productivity carefully. The founders had planned for a downturn and had saved enough to loan \$1,000,000 back to the company to allow it to survive. Great financial management, cutting quickly, negotiating with landlords, banks, and others gave MBH the time to recover, and recover they did. By late 2010, MBH's revenues were on the rise. By 2012 its revenues were 84 percent of 2007's peak. The headcount stood at 177 and profits actually exceeded 2007's level.

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7. Tolerating Dysfunctional Leaders | When a business grows to midsize, it needs teams to handle projects and manage a larger workforce, and it needs leaders to manage the teams. Big companies can easily survive two or three weak links on a team of several dozen executives. But two or three weak links out of six or seven (the size of many midsized company management teams)? That's a recipe for disaster. Having a strong, high-performing leadership team in place is critical to growth and to overcoming the other silent killers—or avoiding them in the first place. Organizations must not tolerate high-maintenance leaders or those that are consistently underperformers—regardless of their popularity. Leaders must regularly assess the strength of the leadership team, and strive to reduce the range between the lowest and highest achieving performers.

Melanie Dulbecco has been CEO of 125-person R. Torre & Co., which makes the Torani brand syrup flavorings, for twenty years. In 2007, as growth flattened, she knew her long-standing executive team couldn't take the San Francisco-based company to the next level. In an orderly and respectful manner, she changed out the team, and R. Torre has since returned to double-digit annual growth.

Was Dulbecco disloyal to those executives who had worked with her for decades? No. Dulbecco was loyal to her company's mission. Tolerating poor performers out of a sense of loyalty is ultimately disloyal to the company, and firms with active boards will hold it against the CEO.

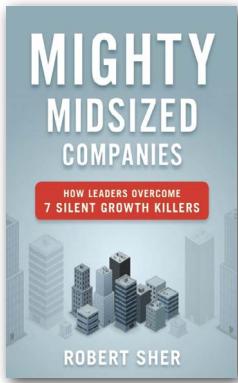
Becoming a Mighty Midsized Company

“Be prepared” is the Boy Scout’s solemn creed. It should be yours, too. Knowing about the seven growth killers is a good start to defending against them. However, there is one other important step all midsized businesses can take to reduce their vulnerability overall. That step is to strengthen their leadership infrastructure.

Leadership infrastructure is the sum total of all the management systems, processes, leadership teams, skill sets, and disciplines that enable companies to grow from small operations into midsized or large firms. Small firms don’t need a leadership infrastructure, since everyone takes direct orders from the CEO. Big firms have had their leadership infrastructure in place for years. But midsized firms must create it for the first time, in small steps, matching the growth of the company. Leadership infrastructure has four elements: quality leadership, planning and governance processes, information gathering and analytics acumen, and an effective internal communications rhythm.

Despite the world’s growing volatility and uncertainty, with the right level of leadership infrastructure, you can position your midsized firm for healthy growth, and then the growth killers, one through seven or all at once, won’t stand a chance against your firm. ☐

Info



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ABOUT THE AUTHOR | Robert Sher is the founder of CEO to CEO and the author of *Mighty Midsized Companies: How Leaders Overcome 7 Silent Growth Killers* (Bibliomotion; hardcover; Sept. 16, 2014). A regular columnist on [Forbes.com](#), Sher has worked with executive teams at more than 80 companies to improve the leadership infrastructure of midsized organizations.

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