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Three corporate tales: Ground rules for growth

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Three Corporate Tales

Ground Rules for Growth

The White House waits for it; Congress wants to stimulate it; the media keep looking for it—and when we get home at night, our kids seem overdosed on it. What’s so great about growth?

Nowhere is growth more sought after than in America’s boardrooms, where progress is measured by “substantially higher revenues” or “significantly improved earnings.” The corporation as compared to a ship is a well-worn metaphor, but according to three CEOs it has some validity. To them a corporation without growth is a ship becalmed. We asked these captains of industry to share with us their views of growth, the problems of achieving it, and the challenges of maintaining it.

The CEOs represent companies in very different stages of growth—from the emerging Metheus Corporation (with virtually no sales), to Visual Technology (with sales now at $50 million), to Automatic Data Processing (with annual revenues of $700 million). These companies are guided by remarkably dissimilar growth philosophies.

One CEO theorizes that “Growth occurs when you’re in the right place at the right time.” Another asserts that “You’ve got to create a good place for growth to happen.” And the third insists that growth is a careful orchestration of concepts combined with a constant fine-tuning of details.

Can growth be controlled or encouraged, or does it just happen? The experiences of the three growth-oriented companies suggest that there is value in the process of growth, as well as in the growth itself.

Visual

A Home for Growth

To hear Tom Foley describe it, starting a $25 million company is a cinch—you just convince some brilliant, well-paid corporate managers to risk their livelihoods, rustle up a half million dollars, and tell the world you’re in business. “It’s the easiest thing I’ve ever done,” says the gregarious president of Visual Technology Incorporated.

Visual epitomizes the high-tech, high-growth entrepreneurial success story of our era: a well-defined market niche, a small but impressive team of managers and technical people, and the conviction that you can do something better that anyone else.

The marketplace seems to agree. From $700,000 in revenues just three years ago to $26 million in 1982, Visual ranks among the leaders in its industry in return on equity and profitability. Adding icing to the cake, the stock market has afforded Visual a generous price/earnings multiple.

Visual designs, manufactures, and markets a broad line of both standard and custom-designed video display terminals. A popular feature of the Visual terminal is its ability to emulate (at a significantly lower price) the characteristics and compatibility
requirements of expensive brand-name terminals.

Visual appears to be in the right place at the right time. But if a 340 percent annual growth rate appears effortless for Visual, it hasn’t come without its challenges, the biggest of which was the decision to start the company in the first place. The major impetus, according to Foley, was a philosophical conviction that a successful company in the high-tech realm could be built based on employee incentives and informal management rather than on bureaucracy and fear.

“We started this company with a nucleus of top people and a formal, well-defined business plan,” says Foley. “It contained the usual stuff—market segmentation, competitive analysis, growth plans. From day one we had an unbeatable management team offering new ideas and technologies. We’ve always had more management than company.” Thus, Foley had a vice-president—finance, vice-president—operations, vice-president—marketing, controller, product manager, and vice-president—quality assurance in place by the end of the first year.

Yet, having good people was no guarantee of success, and Foley knew it. Motivating them was crucial in the early months before sales could begin.

According to those who work with Foley, there’s a lot more back-patting than lecturing at Visual; and Foley agrees: “Camaraderie breeds honesty,” he says, “allowing us to fix problems before they become headaches.” In Foley’s mind, that’s an important way to be sure nothing gets in the way of growth.

Many venture capitalists look at growth differently, seeing it as a function of three key elements: a sound concept, the availability of funds, and the availability of more funds. Foley’s start-up experience contradicts this tenet. “Maybe we were just lucky,” he says, “but we made it work with very little funding. Our initial capitalization was $600,000, which lasted through the introduction of our first product. Once we had the prototype and a solid order backlog, getting venture capital for production was easy.”

In 1979, with a blanket order agreement amounting to $7 million, the year-old company received about $400,000 more from venture capitalists. In late 1980 a consortium of Massachusetts-based insurance companies provided an additional $1 million for working capital and inventory; and in 1981 the company took advantage of its brief but impressive track record and issued its initial public offering at $5.5 million. More recently, in May of 1983, a secondary public offering of stock was issued that raised $11.5 million.

“It’s a good thing we were an instant overnight success,” Foley says good-naturedly, “because in the beginning we didn’t have much money to play with.”

He muses about the good old days when employees devoted equal time to designing products and renovating an old mill (rent: $1.25 per square foot) which served as Visual’s base of operations. Though $50 million in revenues have filled the corporate coffers since then, amenities seem to remain a low priority. Foley describes the current Tewksbury, Massachusetts headquarters gruffly: “We’re not exactly laden with overhead.”

If Visual’s success doesn’t reflect a tested formula, it does suggest several guidelines. First, make sure you have experienced management, and enough of it. Second, find a way to differentiate your product from your competitors. Third, make sure you have enough money, but don’t take more than you need unless you’re willing to surrender control of the company. And most important, according to Foley, make sure people are enjoying themselves.

Foley warns prospective entrepreneurs that a different mind-set is required after leaving the corporate womb. “You don’t have to impress anyone with how hard you work. What matters is how smart you work. You don’t need the memos, the letters, the meetings anymore. We’re doing it our way and having the time of our lives.”

Visual has a double-edged strategy in place for future growth. First, just by broadening the definition of its existing business, the company has targeted five distinct market segments in which its existing skills and talents can be applied: smart terminals, personal computers, intelligent terminals, graphic terminals, and microcomputers. Visual’s strategy is to increase market share in each of these product categories, which, in the aggregate, are forecast to grow at the rate of nearly 40 percent per year for the next several years.

The second strategy is to grow through acquisition into market segments which are allied to but not directly in Visual’s field of expertise. Through the recent acquisition of an intelligent terminal/microcomputer producer, Visual effectively doubled its size, making a quantum jump to $50 million in annual revenues.

Most small, successful companies are reluctant to make that kind of commitment. Internal development of technical capabilities can take years, however, and in a rapidly expanding marketplace, development time can mean lost opportunities. Clearly, rapid growth is a high priority at Visual.

“The acquisition puts us into a new market a lot faster than our own internal development would,” asserts Foley. The fit between Visual’s terminals and the acquired product line appears to be perfect. Considering no cash was used for the transaction, the dramatic increase in revenues and working capital, plus immediate entry to new markets, should give an additional boost to Visual’s already impressive growth record.
A History of Growth

In striking contrast to the methodical formation and casual management style of Visual Technology is Automatic Data Processing, more commonly known as ADP.

Where Visual began with a formal business plan, international sales aspirations, ample capital, and astute professional management, ADP began with a vague notion of a business opportunity, applied within a small geographic area. Its only resources were a few thousand borrowed dollars in the hands of a 21-year-old accountant. And while Visual attributes much of its success to an informal management style, ADP credits its outstanding growth record to its consistent adherence to key management principles, which include decentralized management, intense concern for client service, and a focus on opportunities that lend themselves to mass marketing and mass production.

ADP is the world's largest independent computing services company. It processes about one out of every 20 American payroll checks, in addition to providing a broad range of other computing and data services to more than 100,000 clients.

ADP's initial success required a lot of hard work and salesmanship. No amount of capital poured into the business in 1949 could overcome the natural reluctance of potential clients to relinquish payroll and accounting data to a third party. After three years, the firm had only 12 clients, accounting for total revenues of just $35,000.

"In those early years, the growth of ADP was slow and methodical," says Josh Weston, president of the multinational corporation. "Punch card machines helped us to automate certain tasks in the 1950s, but we didn't begin to see the real potential of this business until we first began using computers in 1961."

Weston, a quiet but articulate CEO, views ADP's computerization as the genesis of its growth into a $700 million company. "The computerization, and standardization, of our business meant that we had the capability to serve thousands of clients with the same basic product while enjoying economies of scale." The big problem, according to Weston, was to reach a large enough market so that development and standard servicing costs could be spread among a client base sufficient in size to keep costs competitive.

ADP took its case to the public in 1961 and raised $270,000 in its first stock offering. Even though ADP was not itself a high-tech company, its association with computers was enough in those days to make ADP a hot stock, a speculative issue selling at 90 times earnings.

A highly valued stock seemed a perfect medium to pursue an aggressive expansion program: and, like Visual, ADP opted to supplement its growth through acquisition. The trend of the era, however, was toward the conglomerate—the highly diversified corporate behemoth. "Temptations were many," says Frank Lautenberg, ADP's former chairman, "to use our stock to buy non-data-processing companies with high returns on investment." In about its twelfth year, this issue forced an assessment of the company's strengths, which in turn led to a clear picture of ADP's future growth priorities.

"We were able to categorize our capabilities under two key strengths," says Weston, "our leadership position in computing services and our reputation for high quality and service in one of the fastest growing industries in the world."

Once this was recognized, ADP's challenge was clear: make the transition as rapidly as possible from a local to a national company—from single service in a single geographic area to multiple services in many areas. The stock's high price-earnings multiple helped the implementation. By using the generously valued ADP stock to purchase small service bureaus in major markets, the company's geographic growth was accelerated. Two dozen small firms were acquired in the late sixties and early seventies. Within two years after each acquisition, the acquired customized services were converted to ADP's packaged services. In the process, local management was trained in mass marketing techniques and an ongoing business which could contribute to ADP's growth was created.

"Nearly a hundred acquisitions have been consummated to date," Weston says. "Virtually every one of them was quite small in size, but directionally relevant. It was by far the fastest way for us to get into new markets and to pick up the managers we needed."

Once the nationwide infrastructure was in place, however, a shift in strategy was called for to help ADP maintain its superiority in service as well as size. Development of new products, systems, and technologies became a high priority. ADP's success with this effort can be seen in the range of new services for specific industries added in recent years—such as computerized car repair estimates for auto insurance companies and cash management services for corporate treasurers.

Like Visual, ADP favors a decentralized management structure. However, there is more structure to ADP's organization. While management stratification and bureaucratic procedures are kept to a minimum, responsibilities are clearly delineated, and there is a published set of management principles. This has helped to maintain ADP's business culture as the company grew too big for personal senior management communication to reach all 15,000 employees.

Corporate planning at ADP modifies the kind of opportunism which recently doubled Visual's
revenues. Each year, according to Weston, ADP creates two primary plans. “One is an annual operating plan for each profit center, which includes statements of key objectives, plans for organization, human resources, and capital investments. The other,” Weston continues, “is a three- to five-year plan for each strategic business unit, including situation analysis, statement of business mission, key objectives and strategies, and action programs for implementing the strategies. The strategic plan also includes resource requirements and general financial projections.”

Like Foley at Visual, Weston sees “niche marketing” as an important component of future success—as long as the niche is of sufficient size to provide adequate returns. “You’ll seldom see ADP as the first into a new market,” says Weston. “For risk/reward reasons and conservation of resources, we generally prefer to let someone else do the early spade work in a new market, waiting until the opportunity is further defined and its potential corroborated.”

A service business, ADP depends on people more than on products, a distinction which is not lost on senior management. As Weston observes: “The greatest stimulation we can give our employee is a set of intangibles comprised of challenges, freedom to innovate, recognition of accomplishment, positive feedback, and an environment in which he will find enjoyable associates to work with.”

**METHEUS**

*The Seeds of Growth*

You are not likely to hear talk about formal organizational principles or the necessity of positive reinforcement and back-patting from Gene Chao, the quiet, self-confident CEO of Metheus Corporation. Though clearly cognizant of the importance of employee motivation and managerial principles, Chao’s more immediate concern is to establish a viable operating history for his Hillsboro, Oregon company.

As Metheus approaches its second anniversary, its performance shows a fairly typical pattern for a technology-oriented company: substantial losses, little revenue, and, until recently, no products. Yet, behind this early history stands a forceful CEO with impressive technical credentials and a proven ability to convince investors of the merits of his ideas.

Through two financings, Dr. Chao has raised more than $10 million to develop, manufacture, and market computer-aided design equipment intended for use in the design of large-scale integrated circuit devices.

“In essence,” Dr. Chao says, “Metheus’ products will enable product designers to innovate custom-integrated circuits for perhaps $10,000 in one month’s time, instead of requiring $100,000 or more in a year’s time. Our first product, the Graphics Controller, will also improve the quality of customers’ products by adding high-performance computer graphics capabilities to their systems.”

But if Chao’s products sound complex, his management style is simple. “We talk a lot,” says the Shanghai-born CEO. “When we started this company, we only had a general concept in mind, no specifics.” Described by those who know him as both methodical and analytical, Chao sat down with his people to take a long, hard look at the pros and cons of various hardware/software decisions. “We considered entering the marketplace where several competitors already existed, but we decided it wouldn’t be an appropriate risk for our investors.”

Risk recognition is an important concept to Dr. Chao, who believes it is crucial for employees and investors to understand the risks of a venture of this type. “If people are willing to devote their talents and financial resources to you, they will fully recognize the risks, they’ll be more committed to you in the long run,” he says.

However, Chao cites finding, attracting, and developing good people as his biggest problem. To achieve the $14 million in revenues he’s targeted this year, he’ll need to increase Metheus’ staffing by about 150 percent. Like Foley of Visual and Weston of ADP, Chao recognizes the importance of providing a satisfying environment. But unlike Foley, Chao hopes his top people will be motivated by the potential challenge rather than by an environment laden with positive reinforcement. And unlike Weston, Chao theorizes that formal organizational guidelines will only hinder the flexibility and inhibit the creativity so crucial to a company dependent on state-of-the-art technology.

Chao talks in terms of evolutions and revolutions when viewing the future for Metheus: “A company like ours has two choices,” he says. “We can either evolve by developing products and technologies which are a step or two ahead of what came before, or we can introduce the revolutionary new concept or idea, far removed from anything currently available.”

Though there may be some questions as to which method Chao prefers, he leaves no doubt that, despite a management style which might seem improvisational to Foley or naive to Weston, he fully intends for Metheus to be as successful in its specialized field as ADP and Visual are in theirs. And it’s also safe to say that if Metheus—and Visual—are still around 30 years from now, both will look a lot different than they do today.

—Austin Mayer