Burkhard Schwenker
Mario Müller-Dofel

On Good Management

The Corporate Lifecycle

Roland Berger
School of Strategy and Economics

Springer Gabler

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An essay and interviews with
Franz Fehrenbach, Jürgen Hambrecht,
Wolfgang Reitzle and Alexander Rittweger

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MARIO MÜLLER-DOFEL
Journalist and Communication Trainer
Dialektik for Business

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"FOR THAT MAN WHO,
WHEN TIMES ARE UNCERTAIN,
IS FALTERING IN SPIRIT,
ONLY INCREASES THE EVIL."

JOHANN WOLFGANG VON GOETHE

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PREFACE: DEDICATION TO AN ENTREPRENEUR

The idea for this book grew out of a challenge: the challenge of finding a suitable present to mark Roland Berger's 75th birthday. One thought immediately sprang to mind: maybe a book about lifecycles. Why? Because few people can lay claim to a life as successful as Roland Berger's. He is the successful founder of a successful consulting firm that has remained successful to this day, 45 years after its inception. It is also the only consulting firm of German origin that competes with the world's biggest and best.

Stories such as that of Roland Berger are inextricably interwoven with a series of skills and factors that, as we will see, can determine whether a company (or an entrepreneur) succeeds or fails in the course of its (or his or her) lifecycle:

- The first is having the right idea at the right time. When Roland Berger founded the company that bears his name in 1967, few people in Germany had heard of management consulting. Where it existed at all, it was American consulting firms that were getting the ball rolling.
- The second is sufficient creativity to communicate new solutions or strategies convincingly. Roland Berger himself points to the build-up of tourism group TUI in the 1970s as his breakthrough project. To this day, the same success factors – marketing, a systematic approach, networking, collaboration and size – have lost none of their validity.
- The third is the courage to take risks in order to occupy a position. The word "entrepreneur" means someone who wants to be enterprising, who wants to do something. That is one of the core attitudes I learned from Roland Berger right from the outset.

◆ The fourth is the ability to convince people – initially to convince them of your ideas ("the German alternative to the American style of consulting") and later to convince them of the need to continue growing rapidly – and then of the need to get involved.
◆ The fifth – another vital skill in the course of a company's lifecycle – is the ability to delegate and let go of things. In the history of the Roland Berger company, this capability is reflected in the transition from what was once a startup with one owner and one decision-maker to a partnership with many owners governed by a philosophy of meritocracy. In my personal relationship with Roland Berger, this was shown in his handing the reins over to me, initially when I succeeded him as CEO and later when I became chairman of the company. I did not realize how difficult and challenging handing things over can be until, two years ago, I too stood down from my role as CEO and in turn passed on the baton to my successor, Martin Wittig.[1]

These experiences alone would be enough to fill a book. To describe the history and lifecycle of our company merely in terms of anecdotes and recollections would, however, do a grave injustice to the intellectual capabilities of Roland Berger. That is why I took the idea a step further: The book was to be about "good corporate management", with the concept of lifecycles both befitting the occasion and setting the framework.

The idea of a company's lifecycle also lends itself to the task in hand because, to my mind at least, the very concept is a contradiction in terms. On the one hand, it is intuitive. Companies are founded or products are developed. They are successful and grow until the market becomes saturated and then they "die". Because there are distinct phases and because these phases are predictable, it is possible to think in advance about what success factors are critical to which phase – and about what forms of management (or which leaders) are the most suitable in each case. As I see it, this is precisely the reason why management literature has for decades been packed with discussions about lifecycle concepts, despite the fact that these concepts are often little more than common sense.

On the other hand – and hence the fascination for me personally – lifecycle models make an implicit basic assumption that I believe is incorrect: that of a fixed, predetermined lifespan. Companies are not biological entities. Their death is not predestined by fate. Rather than looking for the style of management that is best suited to this or that phase, we should actually be looking for leaders and strategies that can help a firm break out of the regular pattern of phases. Precisely this search leads us to the questions that are most relevant for "good management": How do we grow quickly without spinning out of control? How do we escape the saturation that appears inevitable and, instead, continue to grow? Or if that doesn't work in the long run, how do we know whether the much-vaunted relaunch, the "reinvention" of a company, is at all feasible? And if it isn't, where do we find the courage to prepare the ground for a rich harvest before decline sets in? For me, the question of whether to reboot or head for the exit is one of the most exciting in a company's lifecycle. My answer is that genuine entrepreneurship and good management can also show themselves for what they are by soberly deciding to beat the retreat and sell.

The inherent contradictions in the lifecycle concept also reflect the diametric opposites which good management must deal with:

- As managers we know that the future is complex and, above all, uncertain. Yet precisely because this is so, the people in our companies feel a need for security that we must factor into our considerations.
- We know from painful experience that trends and numbers can no longer be relied upon. Yet we still have to plan, do our sums and decide about investments.
- We know that an interdisciplinary mindset is the only way to stay abreast of the complex world we live in. Yet at the same time, expert knowledge and practical experience are necessary if we are to properly steer our companies' day-to-day business.

In my opinion, this circle can be squared with a piece of good news: Corporate management is once again becoming more direct, more personal, more entrepreneurial. It can no longer hide behind models, concepts and techniques. On the contrary, it demands personality, courage, the ability to think and reflect, and a system of proven values. Managers need to have convictions: They must nail their colors to the mast. That is why we prefixed this book with a quote from Goethe: "For that man who, when times are uncertain, is faltering in spirit, only increases the evil."

This book represents a personal opinion. It is not an academic treatise. It is an essay, an at times very personal meditation, if you like, on what makes good management today. Its purpose is to take stock of where we are at and, ideally, provide orientation for the way forward. Thinking about the idea of lifecycles – the conceptual framework for this book – has also shown me how little existing concepts reflect the conditions that are faced by company managers today. For this reason, the book also attempts to stake out a new, contemporary lifecycle concept.

We don't want these considerations to remain purely conceptual, of course. The second part of the book brings together a series of in-depth interviews with outstanding company founders and business leaders: Franz Fehrenbach, Dr. Jürgen Hambrecht, Professor Wolfgang Reitzle and Alexander Rittweger. These individuals have become synonymous with excellent corporate management, farsighted vision and sociopolitical commitment. In the course of their careers, they have mastered a whole battery of challenges in the lifecycle of the companies they represent. They willingly agreed to share their experience and insights, and to corroborate – or, on occasion, contradict – my own musings. For this I am sincerely grateful. Incidentally, they are all also long-standing associates and close friends of Roland Berger himself, a fact that neatly rounds off the fundamental motivation for writing this book.

The interviews were prepared by Mario Müller-Dofel and conducted by an experienced business journalist whose professionalism and unerring sensitivity have translated deep insights into an exciting read, and to whom I owe a debt of gratitude. Thanks are also due to my colleagues Klaus Fuest, Professor Torsten Oltmanns and Dr. Tobias Raffel. As in my other publications, their creative ideas, first-class research and stimulating discussions played a very substantial part in bringing this project to fruition. Last, but by no means least, my thanks go to Dr. Katherine Nölling, whose exceptional skill, tenacity and powers of persuasion ensured that the book was finished on time. Birthdays always come around faster than you thought.

This book is dedicated – as a birthday present – to my mentor and guide Roland Berger, who, over the years, has also become my friend.

Dear Roland, congratulations on your 75th birthday!

HAMBURG, NOVEMBER 2012,
PROFESSOR BURKHARD SCHWENKER

1.
THE CHALLENGES OF GOOD MANAGEMENT

1.1 WHAT SHOULD INFLUENCE HOW WE THINK ABOUT GOOD MANAGEMENT

Why yet another book about corporate management? Scarcely any aspect of management doctrine has triggered such an avalanche of writings. Over the past ten years alone, no fewer than 23,943 new books on the subject have appeared in German or English. That's 2,394 books a year, or more than ten on every working day.[2] One would think that everything worth thinking has already been thought.

Yet the world is changing at an ever more rapid pace. "Truths" that had become flesh and blood are suddenly unmasked as error. As recently as a decade ago, who would have thought that the Internet would revolutionize the retail industry or that green technology would shape our growth trajectory? Or that Germany would, once and for all, pull the plug on nuclear power? Or that China would emerge as the world's biggest net exporter, prompting the US to herald the advent of the "Pacific Age"? And who would have thought that the financial markets would spiral completely out of control, plunging us into one of the most profound global economic crises since the 1930s?

In a lead story entitled "The Nightmare of the Alpha Dogs", Manager Magazin, a respected German-language business periodical, asserts that "Risks are growing more dramatic, markets more volatile, technological leaps more gigantic and global entanglements more complex by the day."[3] While that may be stretching the point a little too far, brain researcher Gerald Hüther is nonetheless right, in the same context, to make the following observation: "Everyone in politics and business knows that we stand on the verge of a transformation process, that something is going to have to change completely."[4]

The fact that our notion of corporate strategy must change completely has already been underscored by my brief list of the fundamental changes that have taken place over the past ten years. And the list is not even exhaustive. If it is no longer possible to paint a realistic picture of future developments, then it also makes little sense to calculate a detailed strategic plan for the next ten years, or to base

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investment decisions primarily on quantitative computations. No, we need to find other ways. I see three points that should influence how we think about good management – and that show why thinking about good management from time to time is always a valuable exercise.

FIRST: CORPORATE MANAGEMENT IS GROWING MORE COMPLEX

People often contradict me when I make this argument. The world, they say, has always been complex, the demands placed on management always exacting. Nor are upheavals a new phenomenon. There is also the view that the absence of "always-on communication" used to lead to much greater information asymmetries. While there is nothing wrong with all these assertions, there is a very definite scientific distinction between the terms "complicated" and "complex".[5] Many of the above factors do indeed make a system more complicated. Only one thing, however, leads to genuine complexity, and that is uncertainty.

In the context of corporate planning, uncertainty has become virtually ubiquitous these days. We will later examine why national economic forecasts no longer constitute a valid planning framework. For now, suffice it to say that, when research institutes constantly have to adjust their growth forecasts – which they did six times in 2011 alone – the outcomes can never serve as a reliable basis for corporate planning. When the DAX share index fluctuates between 7,000 and 5,000 points in a short space of time, it is only fair to speak of pronounced volatility. When the scheduled lifespan of nuclear power plants is first extended and then suddenly curtailed due to a political volte-face, conditions can no longer be said to be stable. To put it bluntly: The pace of change is picking up, it is becoming ever more difficult to maintain a clear overview of events and, as people are no longer sure what is going on, uncertainty is increasing.

This has several implications for good management: It means that business acumen is once again coming to the fore as predictability is on the wane. It means that it is important for leaders to know where they stand, to be able to make up their own mind about the future and not to go running after every trend that crosses their path. It means that the ability to reflect on things and the willingness to think in interdisciplinary terms is at a premium. After all, if we as entrepreneurs want to successfully overcome uncertainty, we need to look beyond our own backyard and build bridges. Bridges, for example, between the following:

- Business management concepts (What is the right way to organize the company? How do you gain lasting competitive advantages?)
- Economic concepts (How does growth work? What models is it based upon? How is economic policy changing?)
- Sociopolitical concepts (What values are important? What attitudes will shape future societies?)
- Geopolitical concepts (Where do security risks exist? How will countries and regions develop? What significance will regional alliances have?)

Careful reflection and interdisciplinary thinking don't just materialize out of thin air, however. We must point the training of our managers in this direction, and we must do the same with our day-to-day work: Where do we look for new ideas? How do we find room for the creative freedom to sketch pictures of the future? How do we populate a management team in a way that maximizes interdisciplinary influences? At the same time, we must reassess the tools of the management trade. Which brings me to my second point.

SECOND: THE VALIDITY OF OUR TRADITIONAL STRATEGY AND PLANNING CONCEPTS IS ERODING

This is happening not for lack of concepts. Until the early 1990s, diversification drove corporate strategic thinking. This period was followed by a concentration on "core competencies", combined with every conceivable variation on the theme of reengineering and/or corporate transformation. The New Economy ushered in the "deconstruction" of the value chain, later giving way once again to a concentration on core business. And diversification too is back on the menu today – at least as a side dish. Somewhere along the line, we have also seen trends toward the centralization and then the decentralization or distribution of corporate management.

Right now, centralization seems to be on the rebound – although I hope not, as I will discuss later on.

This constant stream of alternative strategy concepts leads many to conclude that corporate management is vulnerable to fashion fads, masterminded not least by consulting firms eager for new business. I may not be objective on this point, but I do not believe this is so. Why? Because almost every one of the concepts listed above had its rightful place at the time and given the prevailing conditions. Today, the problem is rather that such stable conditions no longer exist. This being the case, good management also involves recognizing when a concept no longer applies – and having the courage to go against the flow of both public and expert opinion and switch to a new concept. Or switch to an old one that might be just the right thing for the current situation.

What is true of strategy concepts is equally true of our planning tools. The experience curve is a good example of what I mean. We have all learned that the unit cost of a product can be reduced by 20% to 30% every time the cumulative production volume is doubled. That is a very useful thing to know when investing in expansion, setting prices and projecting cashflow. At least, it is useful at times when growth rates are high and your business environment is stable. If sales of a product are growing at a rate of 15% per annum, doubling the volume takes just five years. Even at a rate of 10%, it still only takes seven years. Both are manageable periods for planning purposes. But what do you do when your rate of growth shrinks to just 3%, meaning it will take 20 years to double your sales, or when new technology suddenly paves the way for completely new production methods? Or when growth of any sort is so volatile that reliable growth forecasts are simply no longer possible? In such circumstances, what used to be useful cost information is worse than obsolete: It can actually be dangerous.

The same goes for many modern methods of corporate finance. I know from my own experience how tempting it can be to adapt the analytical elegance of the capital asset pricing model in order to calculate the cost of capital. But what use is greater elegance and precision to me if the development of future cashflows – which this concept is supposed to analyze – is becoming increasingly uncertain? An incorrect estimate of cashflow development has worse consequences than a calculation of capital costs that was off the mark. Albert Einstein's famous saying is more valid today than ever before: "Not everything that can be counted counts, and not everything that counts can be counted."[6]

Of course, as far as good management is concerned, that doesn't mean that we should do without modern quantitative models and concepts entirely. Correctly applied, they can still help us reduce complexity and prepare decisions. What it does mean, however, is that we must think long and hard about when the analytical effort involved in these models is justified, and whether we have set our priorities correctly. Above all, it means that we must be more keenly aware of the assumptions and limitations that underpin such models. I do not believe that the financial crisis was driven by the complex algorithms that are used to design and put a value on derivatives. But I do believe that it was driven by users who did not know (or want to know) the assumptions and limitations inherent in these models.

We could say the same also applies to the shareholder value concepts that have substantially influenced our understanding of management since the 1980s. Again, there is nothing wrong in seeking to increase value and boost cashflow. But there is something wrong when we concentrate exclusively on finance and the capital markets. At the peak of the latest financial crisis, Jack Welch, former CEO of General Electric and perhaps the best-known proponent of the American-born shareholder value philosophy, acknowledged that: "On the face of it, shareholder value is the dumbest idea in the world. Shareholder value is a result, not a strategy (...). The main pillars are your employees, your customers and your products."[7]

Seen from this angle, my first two arguments about what should influence how we think about good management can be mapped onto an (admittedly oversimplified) "if-then" sequence:

- ◆ If trends are no longer reliable, then numbers will be of limited use as a basis for planning and decision making.
- ◆ If numbers cannot help us, then we must wave goodbye to the idea of wanting to quantify every entrepreneurial decision. What is useful, however, is a feel for technology, for what customers need and for underlying economic and sociopolitical developments.

- If the business environment is changing so fast, then short-termism will appear to be right. Only a long-term picture of the future can give orientation to the people in our companies.
- If the people in our companies are unsettled by complexity, then trust in the capabilities of management plays a pivotal role.

Underpinning this almost aphoristic summary is my third argument as to why we should rethink what good management means.

THIRD: WE NEED A NEW UNDERSTANDING OF WHAT MANAGEMENT MEANS

In the past – in the days before the Soviet Union imploded, before globalization and before the Internet – the world was content to work with the fiction of at least something like medium-term certainty. Today, however, we are confronted by fundamental doubts about the predictability of the future. In the past, clear, unambiguous statements – "this is our strategy", "that is our goal" – allowed us to reduce complexity and communicate a sense of security. In their place, uncertainty is now driving complexity and making clear statements impossible.

For me, communicating a sense of security is very important to good management. I believe every one of us has a deep longing for security – for a secure income, a safe job, solid career prospects, a future that we can visualize and look forward to. I see "org charts", for example, as symbolic of how we strive for this security and of the contradictions that are inherent in this striving today. On the one hand, we have known for years that we must be process-oriented in the way we run our companies, assigning tasks flexibly and avoiding structures that are cast in stone. Yet virtually every company still has an organization chart. Look, there's the little box with my name on it. That's my home. That's where I belong.

The challenge today is that no truly responsible manager is in a position to say how long any such org chart will remain valid. The same is true of supposedly reliable planning figures, which are likewise intended to convey a sense of security.

So we find ourselves in need of something new to replace the security we have lost. To my mind, this can only be anchored in the personality of managers and leaders. These days, no one can hide behind a number or a plan. Every manager must be able to explain their convictions and how they see the future. To paraphrase Joseph Schumpeter: Those who talk about their visions reveal the limits of their horizons. This is precisely the issue at stake: having a broad horizon – and having the courage to make it known. Managers communicate a sense of security and nurture trust by making it clear that they are willing and able to deal with complex situations, and by showing that they have sufficient integrity to tackle these situations in the best interests of the company and its people.

The good news is that this approach makes management more direct and personal. It becomes less technocratic, more accessible to people and closer to the business, clients and technology used. In other words, management becomes more entrepreneurial – more enterprising. The challenging news is that, on its own, this is not enough. Managers also need to cultivate an interdisciplinary mindset if political and social developments are to be factored into their business decisions. That is why analytical skills remain at a premium: For all the complexity that surrounds us, identifying patterns will be as necessary as ever in the future.

1.2 A SURVEY: WHY MANAGEMENT OFTEN FAILS

Are these challenging demands too much for top executives? In light of such complexity, is it possible for anyone to lead a company to success? What is certainly true – and we shall look at this more closely in the next chapter – is that not all companies are managed successfully. Failure is by no means uncommon. But what exactly goes wrong when companies fail? What management mistakes or behaviors lie at the root of the strategic errors and operational difficulties that can threaten the very survival of the modern enterprise? I posed the same questions to my fellow Partners at Roland Berger, asking them to list what they see as the seven most important reasons for failure and then prioritize them (7 being the most important, 1 the least