The focused company

Unnecessary complexity cripples companies. But some have learned to root it out wherever it crops up.

By Mark Gottfredson

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When my colleagues and I assess a company, we often begin by asking executives to answer five questions. It's a quick test that helps us identify possible trouble spots. You can try it yourself: How would you respond to each of the following?

- Do you strive to invest enough to win in all of your product markets, all the regions you compete in and every division of the company?
- Does your product portfolio offer enough options to appeal to all types of customers?
- Is your organization designed to provide support for all of your company's processes and functions?
- Do you expect every function in the company to redesign its processes to maximize internal efficiency?
- Are your IT systems and applications built to enable all of your existing business processes?

At first glance, the questions seem to define objectives that every company should be pursuing. Many executives nod their heads enthusiastically as they read through the list.

But here's the twist: If you answer or strive to answer "yes" to *any* of them, it's a red flag—a sign of too much complexity and a resulting loss of focus. And that can be a company killer.

Look again at the questions. A truly focused company—one that has cut complexity to the minimum—does *not* invest to win in every element of its business. It invests primarily in its core, the business in which it can outperform everybody else. A focused company does not try to appeal to every potential customer. It concentrates on the most profitable customers, those whom it can serve better than any competitor can. And so on down the line. When respondents answer "yes" to the questions, it usually indicates that their core business, the capabilities and assets that really distinguish their company from competitors, has been swamped by complexity. Executives no longer have a clear sense of priorities. They spend their days putting out fires. They wonder why the latest change initiative has once again failed to achieve the hoped-for goals.

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Where complexity comes from. Complexity is a natural trait of any large organization—"natural" because it is a by-product of business decisions that are sound and rational. Every day, your customer service people are creating new processes to better address customers' problems. One new process a month means 60 new processes in just five years. Can the organization handle that? Every day, your engineers and marketers are trying to get a little more shelf space or share of wallet, so they add a feature or a product or three new options. Let that go on for a while and before long you have 10,000 SKUs, with only a small percentage in any one outlet. Growth itself begets complexity. You move into one new market and then another; soon your organization is a tangled web of reporting relationships. You acquire one new business and then another—and you wind up with a portfolio of unrelated companies requiring large amounts of management attention.

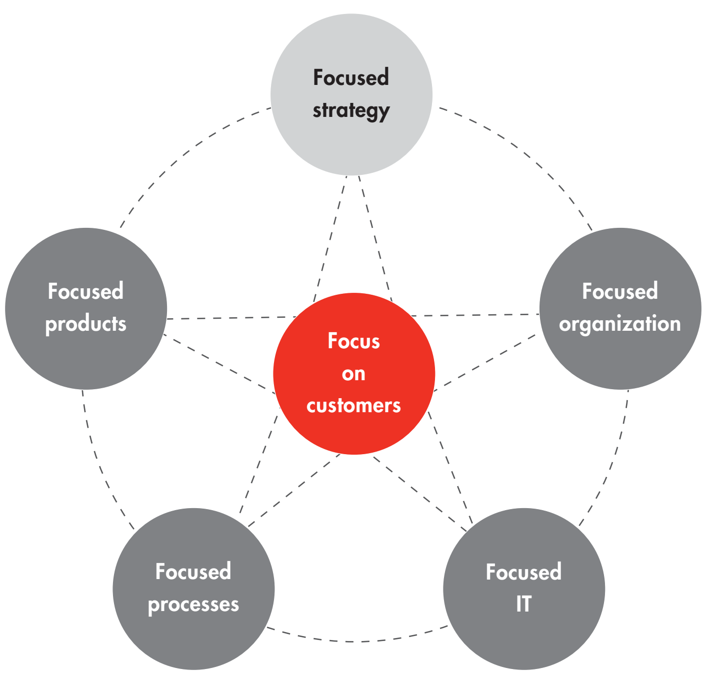
Is it any wonder that CEOs in a recent survey identified complexity as the primary challenge they face? Nearly 80% said they expected high levels of complexity over the next five years. Far fewer felt prepared to cope with it.

Faced with such concerns, most companies try to take action. Teams attack product-line complexity, organizational complexity and complexity in IT systems. They create new structures. They reengineer processes. They put in more stage gates and ROI hurdles for new products, and they pursue functional excellence. Unfortunately, what they usually find is that fixing complexity in one area is like squeezing a balloon: It just pops up somewhere else. Though one element of the organization may seem to work more smoothly, costs continue to rise and decisions continue to be bogged down in bureaucracy. One executive we talked to was ready to throw his hands up in dismay. His company—a major energy producer—had spent close to $100 million on a series of process reengineering initiatives, every one reportedly a complete success. Yet somehow general and administrative (G&A) costs kept rising faster than revenues. "If you add up all the savings we're supposed to get from the reengineering," he said, shaking his head, "we should have negative G&A right now. Instead, it keeps on going up."

Stop squeezing the balloon. There's a better way to fight complexity—a better way to create a focused company. The key, we have found, is to *follow the connections* where they lead. As anyone who has tried to squeeze the balloon can attest, the different kinds of complexity really are interrelated. It's hard to get results by attacking just one aspect of the business, such as processes. But that interrelationship also creates a web of opportunity: Simplification in one area opens up possibilities for simplification in others. Instead of leading to frustration, an attack on complexity in one part of the business can establish a beachhead for rooting it out elsewhere *(see Figure 1)*. The result of such a multipronged approach, ultimately, is a truly focused company—and results that last.

There may be no better example of creating focus in this way than the Ford Motor Company under Alan Mulally. Mulally became Ford's chief executive in 2006. When he arrived, he found a company drowning in complexity. It had eight major brands and more than 40 vehicle platforms. It relied on too many suppliers, offered consumers too many option configurations

Figure 1: Tackling complexity in one area creates opportunities for simplification throughout the company



Source: Bain & Company

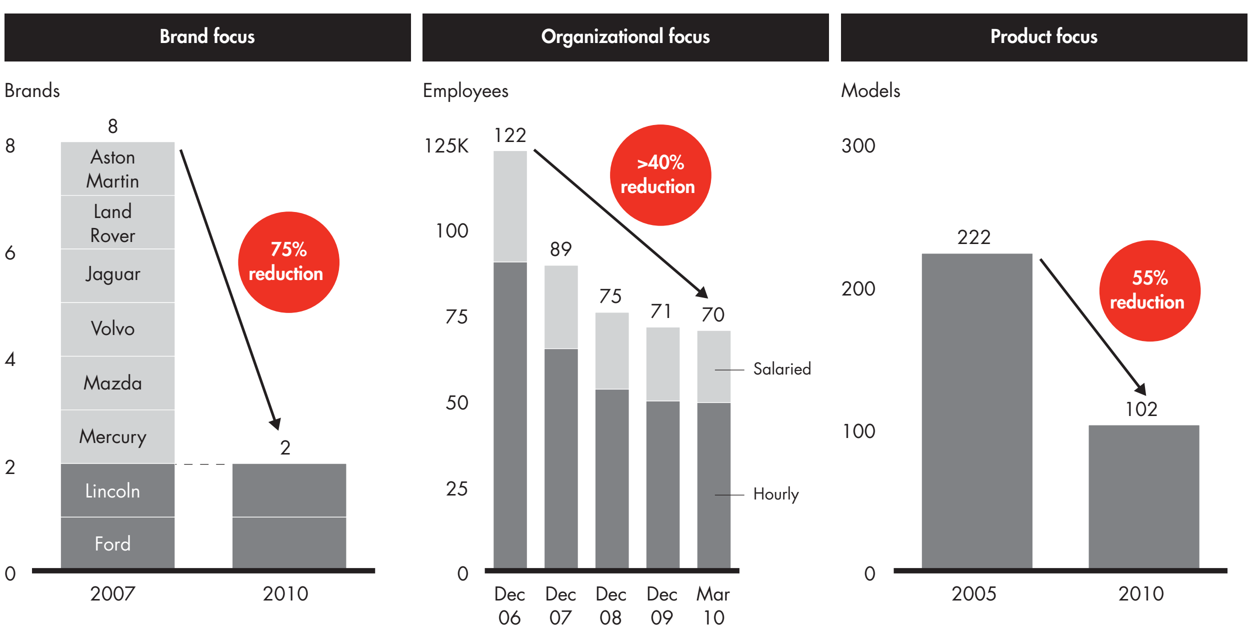
and utilized fewer than 10% of its parts in more than one vehicle.

Mulally's task was to refocus the company, and he moved aggressively from one locus of complexity to the next. He and his team reversed Ford's strategy of competing in every major segment of the automotive market, selling off or eliminating six of the eight brands. From then on, Ford and Lincoln buyers would be the company's sole focus. The team also reduced the number of platforms and models, increasing the proportion of common parts to more than 50% *(see Figure 2)*. These actions allowed Mulally to cut the number of suppliers in half, lower the company's headcount and radically simplify the organization, moving from a convoluted regional structure to a simpler global matrix. When Mulally arrived, the company was already rolling out a new cross-functional product design process. That complemented his renewed brand and organizational focus, enabling Ford to streamline its engineering and get new products to market faster.

Simplification on this scale generates impressive results. Ford, which lost more than $2 billion in 2007, earned more than $20 billion in 2011. "If you roll the clock back two to three years ago," a Ford executive named John Felice told the *Detroit Free Press* in 2010, "one of the things we realized is we just had too much complexity."

Examine a focused company closely, and you find that it differs from the typical company on five important dimensions: strategy, customers, products, organization and processes, including IT. Subsequent articles in this series will look in detail at how to improve focus in each dimension. In this introduction we want to concentrate on their interconnections. It's tough, and usually fruitless, to simplify any one dimension alone. But when you move from one to the next, as Mulally did at Ford, you get a powerful multiplier effect. Each step toward simplification reveals opportunities for more, and the results you create are both dramatic and durable.

Figure 2: Ford implemented brand, organizational and product focus



Sources: Ford Motor Company; *Detroit Free Press*; Bain analysis

1. Focused strategy

Average company: Invests to win in every element of its business.

Focused company: Invests to identify and strengthen core capabilities.

A company's *core business* comprises its most profitable customers, its unique and most differentiated assets and capabilities, and its most important products and channels. These elements are the crown jewels of the business. A company with a focused strategy adds new businesses or enters new markets only when doing so reinforces the core. Its growth model is tried, tested and repeatable. Its strategic objectives can be articulated as clearly by frontline employees as by senior executives. Look at the difference between NIKE and Reebok. In 1989, the two companies were comparable in size and profitability. Then Reebok diversified into fashion footwear, boats and other businesses while NIKE maintained a laserlike focus on athletic shoes and apparel. Reebok ran into trouble and was acquired by Adidas. NIKE posted a record-setting performance, redefined the rules of the game of its industry, and reshaped and enlarged the global profit pool that supports it.

A focused strategy immediately creates opportunities for simplification in virtually every area of the business. Since it is based on understanding the core, it helps you recognize precisely who your core customers are. It allows you to determine which products will most appeal to those customers and which are unnecessary. Strategic focus has implications for organization and processes as well. It enables a company to create an organizational structure that supports the right set of businesses and markets, as Ford did. It encourages the development of a culture focused on quick, effective decision making and execution. It provides a lens that helps you align processes with business objectives.

These links emerge clearly in the story of LEGO. In the 1990s, LEGO had diversified into a variety of businesses, including clothes, watches, publications, TV, learning labs and theme parks, all while its core business of building blocks was under attack by low-cost competitors. "We had moved far, far away from what we did well," said a company official, "absorbing vital management capacity." The company struggled mightily, and by 2003 found itself with a sales decline of 29% and a drop in earnings before interest and taxes (EBIT) of 21%.

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In 2004, however, LEGO got a new CEO, Jørgen Vig Knudstorp, who believed in the value of a focused strategy. He and his team sold off most of the non-core businesses. That immediately simplified the organization and eliminated a wide variety of product lines. The team refocused everyone's attention on LEGO blocks, and on the children and adult hobbyists who loved them. Now they could introduce new product kits, negotiate new licensing arrangements (Harry Potter, among others) and create innovations such as LEGO Digital Designer. Meanwhile, new systems for gathering regular, detailed feedback from core customers ensured that the company didn't stray too far from what those customers most wanted.

The result of this simplification? Sales rose 22% in 2009, 37% in 2010 and 17% in 2011. In 2011, EBIT was at 30%—and the company was able to eliminate an entire layer of management, even though the workforce had grown by 12%. That's what a focused strategy will do for you.

2. Focus on customers

Average company: Has plenty of data about its customers but struggles to find insights it can act on.

Focused company: Knows its core customers' sweet spots and designs its business around those customers' needs.

At a focused company, executives and frontline employees understand which customers are at the center of their business. They create systems of continuous feedback, so that they can constantly adapt their offerings and processes to meet the needs of these core customers. That kind of deep customer knowledge informs every other aspect of the business. Companies that know their customers well can create a focused value proposition, tailoring product decisions, pricing, channels and so on to the most valuable segments. They can also take the next step, which is to eliminate whatever portions of the offering do not address the needs of these groups. They can simplify processes to make customer interactions easier and faster, create IT systems that facilitate those interactions and organize their front line in a way that best meets customer needs.

A major insurance company operating in the Asia-Pacific region illustrates this potential. The insurer, realizing it was not on track to hit its 2013 goals, had tried redesigning processes and installing new IT systems, with disappointing results. So it began focusing first on its brokers, intermediaries and end customers, exploring their needs through research, workshops and analysis. It identified the segments that were most important to the business and then designed winning propositions for each segment. This customer-based approach helped the insurer to simplify on several dimensions. It created a sales and distribution unit aligned to each customer segment, with representatives having responsibility for whole accounts rather than single product lines. It developed functional centers of excellence for underwriting, claims, operations and support, each with simplified processes and clear decision roles. It accelerated selected IT process enhancements to support the new operating model and propositions. Thanks to these broad initiatives to simplify the business, executives expected the organization to grow significantly. Customer needs were being better met, the organization was leaner and the company was on track to realize about a 30% gain in efficiency.

3. Focused products

Average company: Provides options (and carries sufficient inventory) to appeal to everyone. Pushes supply-driven innovations on the market.

Focused company: Gives its core customers exactly what matters most to them. Is equally disciplined in releasing new products and in trimming those that customers no longer value. Market demand pulls innovation.

Companies regularly add new products, options, features and line extensions for reasons that usually seem good at the time. But the resulting proliferation of SKUs often has unanticipated effects. It adds hidden costs. It increases cycle time and hinders accurate forecasting. It makes buying more difficult and thus complicates the customer experience. Ironically, it may even put a dent in revenues, because customers confronted with too many choices often walk away.

A focused portfolio of products is different. A company with a focused portfolio understands exactly what its core customers want, and it can accurately assess the additional costs of each product line and SKU. Organizations that develop these capabilities often find that they can trim their offerings radically—sometimes by 50% or more—with no negative effects on profitability or competitive position.

A truck manufacturer, for example, originally offered customers individually configured trucks, with millions of different option combinations and more than 40,000 unique vehicles produced. When the company switched to a modular-product system, it not only cut cost to order by 71% and was able to consolidate its suppliers; it also learned that it could cover 80% of historical demand with only about 250 product/option modules, compared with the million-plus it had the capacity to build. A computer manufacturer, similarly, found that many consumers were happy to buy preconfigured machines rather than the individually customized products offered in the past. The move to preconfiguration helped the company reduce its product line in some segments by more than two orders of magnitude.

Companies that focus their product portfolio typically find big simplification opportunities in other areas of the business. Among the potential effects of significant SKU reduction are these:

- **Clarification and reinforcement of customer and strategic focus.** Simplifying a complicated product portfolio requires item-by-item analysis of costs, profitability and value to the core customer. An industrial distribution company learned from this analysis that it had five distinct customer segments, each with different needs. The data was invaluable to the senior team as it decided on strategic priorities.

- **Streamlined operational processes.** A company's purchasing function can concentrate on effective supply chain management for a far narrower range of products. Its marketing function can more easily focus on core products. At the computer maker, simplification of the sales process led to 40% more time available per call for added-value activities such as selling software and services.

- **Simplified data and applications requirements for a company's IT systems and website.** Fewer SKUs can unburden legacy systems that are bogged down in complexity and create opportunities for more effective use of IT. At the computer company, designers simplified the website and realized a 30% improvement in up-sell consideration from visitors.

4. Focused organization

Average company: Designs its organizational structure to support existing processes.

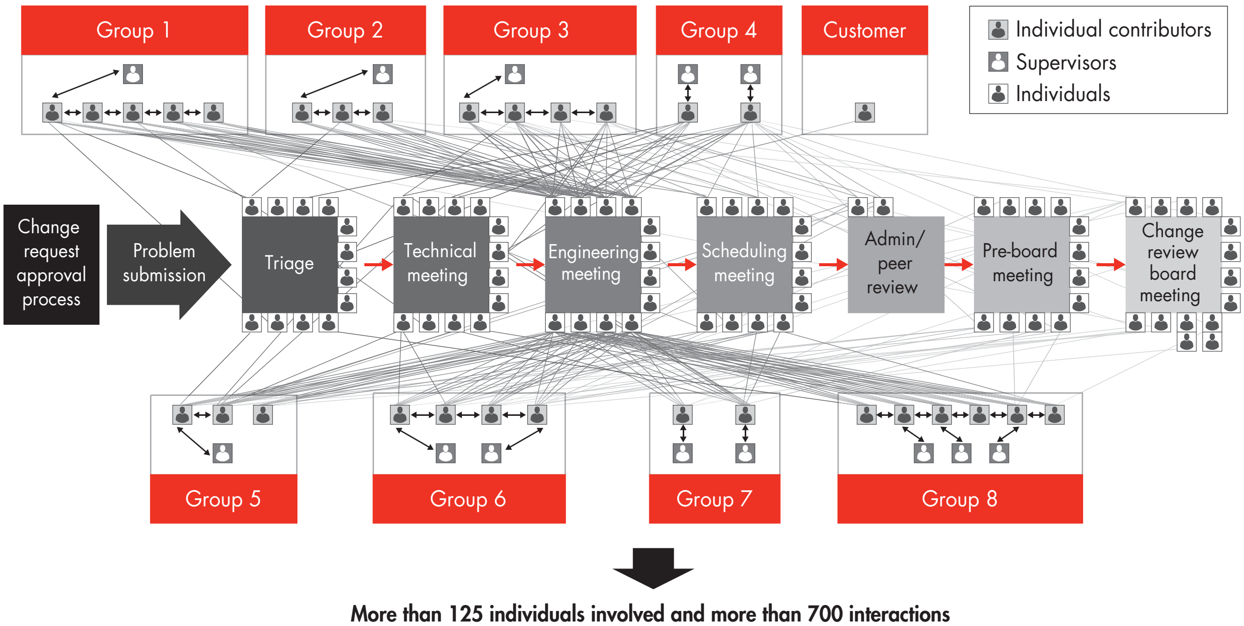
Focused company: Designs its organizational structure to support critical decisions.

The defining characteristic of a focused organization is that it makes and executes its most important decisions well, quickly and without undue effort. That requires a high degree of simplicity at three different levels. First, the overall organization needs a clear structure tied to the company's strategy, without too many "nodes" or points of interaction among functions and units. Second, each unit needs a minimum number of layers and appropriate managerial spans, and the organization needs a simple way of ensuring that the right people are in the right jobs. Third, the organizational culture—the way it handles meetings and other interactions—has to facilitate good decision making and execution.

Too often, the exact opposite is the case: Nodes proliferate, bureaucracy grows and what we call *swirl* takes over. Units in a company begin to add staff. Each unit's analysts develop their own view of the "truth" regarding the organization. When a cross-functional process kicks in, all these analysts have to vet and validate one another's data—and then, typically, they trade requests for still more data. Suddenly people feel like they can never keep up with all the work and can never get anything done. Costs spiral upward. Decision speed slows. At one aerospace company we studied, the process for approving a contract change request involved 125 individuals and more than 700 interactions (see Figure 3). Little wonder that the company was perpetually behind schedule.

Organizational simplicity facilitates other kinds of simplicity primarily because it clarifies decision roles and procedures. A company loses strategic focus because members of the management team go in separate directions. It loses product focus because no one is accountable for regularly reviewing the portfolio. It loses process focus because people keep adding new processes (or steps to existing processes) without coordination. A focused organization with clear decision roles casts a bright light on all these failings. And it identifies the individual or group responsible for fixing each one.

Figure 3: Organizational complexity at an aerospace company



Source: Bain & Company

This multiplier effect was clearly visible at the aerospace company just mentioned. Originally the company was concerned mainly with complexity in its supply chain. But analysis revealed that the problem lay deeper. Decision rights were unclear, decisions took longer than they should and nearly 70% of employees in upper layers were in staff jobs with no direct reports. That's why processes such as the engineering-change procedure had bogged down: Each one entailed seemingly endless rounds of meetings and sign-offs across the organization's nodes. Though the company was implementing 13 different IT systems to improve its supply chain, none of these systems addressed the underlying complexity and the problems associated with it. Assigning rights and accountabilities for the decisions involved allowed the company to simplify this and many other processes.

5. Focused processes and IT

Average company: Redesigns processes to maximize functional efficiency. Aligns its IT systems to support existing processes.

Focused company: Redesigns to maximize integrated process efficiency. Aligns IT systems with business objectives.

Business processes and IT systems link a company's strategy to its everyday operations. If the strategy, product line or organization is unduly complex, processes will be unduly complex—and vice versa. The symptoms are usually easy to spot. People report that they waste a lot of time. Products are late to market. IT systems cement process complexity in place, and so the two are closely linked. Companies trying to fix their processes often run up against that time-honored response from IT: "That's a great idea, but our systems won't support it."

An effort to create either focused processes or IT nearly always leads to simplification in other areas. As an example of how that is true for processes, a chemical company found that it was suffering from too much downtime, late deliveries to customers and low overall utilization of machinery. The company immediately began working on the processes in the plant by implementing a Lean Six Sigma effort. Team members correctly diagnosed one cause of the low utilization: excessive changeover time from one product to another. They then worked to address that inefficiency by speeding up the process of cleaning the plant and equipment between batches, as well as improving housekeeping and making other process improvements within the plant. These efforts were considered successful, improving utilization by about 20%.

But the real cause of the trouble lay upstream—in product development, in engineering and in decision roles. Many of the company's products were functionally similar but still required a full cleanout. Reducing product complexity helped lower the number of required changeovers. Scheduling issues were a source of trouble as well. The engineering department created a production plan designed to minimize time lost to cleaning. Operators in the plant, however, often changed the plan based on issues such as materials delays and machine breakdowns. When the company looked at the cross-functional changes that could be made and specified decision roles, giving responsibility for optimizing operations to the people who could see the issues most clearly, the number of required changeovers was greatly reduced and its overall equipment effectiveness improved nearly 100%. That effectively doubled the capacity of the plant with almost no capital investment.

The link goes in the opposite direction as well: Simplification in other areas rarely takes root unless a company also addresses its processes and IT systems. A credit card company, for example, reorganized around customer segments, reduced product offerings by more than 50% and ended more than 50% of its retail partnerships—all steps in the direction of greater focus. But the company did not reorganize its back-end functions, instead assuming that its functional silos would adjust to the new reality. Its cost savings, consequently, were nowhere near as great as expected. So a team attacked the company's processes, beginning with marketing. Detailed process maps revealed significant opportunities for savings—for instance, 80% of the time spent developing marketing campaigns was wait time. Front-to-back process redesign enabled the company to capture those savings. Not only did operating expenses drop; cycle time declined as well.

Conclusion

When companies attack complexity, they nearly always begin with a specific pain point, an element of the business that seems to be costing too much or causing some kind of delay. What they find, often, is that they don't want to stop there. Bringing focus to one dimension of the company typically reveals sizable opportunities for simplification elsewhere. Most companies find that this kind of multidimensional approach is far more effective than tackling one element at a time.

For an executive team, building a focused company is the great challenge of our era. Complexity is like a weed, insinuating itself into every nook and cranny of an organization. Rooting it out requires a serious commitment of time and resources. But it can be done, and the payoffs are significant. Costs decline. Sales rise because customers are less confused and find it easier to buy, the salesforce is more focused and marketing can invest more effort in each remaining product line. People in the organization can make better decisions, make them faster and implement them more effectively. The performance of Ford and the many other companies that build focus into their everyday operations shows the power of simplicity. It's almost always a hallmark of great companies.

So rather than trying to answer "yes" to the questions we posed at the beginning of this article, good managers will take a more fruitful approach. They will wake up every day and ask themselves, "What can I do today to simplify and focus my company?"

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