THE BREAKTHROUGH COMPANY

How Everyday Companies Become Extraordinary Performers

Keith R. McFarland

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CONTENTS

To my parents,
who taught me to seek the things most worthwhile,
And to Kelli, Will, and Cole,
who remind me every day what those things are

ACKNOWLEDGMENTS

THE TALMUD SAYS that learning is achieved only in company, so it only makes sense to first mentio the people whose company made this intellectual journey possible.

It was Peter Drucker who first launched my search for answers on how companies break through th entrepreneurial stage of development, and it is to him that I owe the greatest debt of gratitude. Nearly a decade later, at a chance dinner meeting, Jim Collins provided the encouragement and the template of a research model that helped me to turn my quest for answers into a book.

I could not have asked for a better collaborator on this project than Darren Dahl, who helped me make the results of our five-year study come alive on the page. He was by my side on every visit I made to the nine breakthrough companies. His skill as a reporter and writer was indispensable in telling the stories of these remarkable firms.

Thanks to Michael Fife of Dun & Bradstreet for his tireless support of this project for more than a year. His tenacity and creativity enabled us to accumulate an enormous amount of information about the more than 7,000 growth companies that made up our population. Thanks also to Noyan Garemani for his help in analyzing the public companies in our study.

I am deeply indebted to my colleagues at McFarland Strategy Partners, whose indulgence allowed me to spend so much time working on this book, and who actively participated in its creation. I owe a special debt of gratitude to Brett Pinegar, who helped create the research analysis model and who managed all facets of our empirical study, while at the same time continuing to provide exceedingly important and imaginative advice to our clients. Brett's work with clients demonstrates every day ho the ideas contained in this book can be used to help companies map their own trajectory to breakthrough. Another key contributor was Luther Nussbaum, our executive-in-residence, who upon retiring as CEO of First Consulting Group, the nation's premier healthcare consulting group, threw himself into the task of supporting the book project with all his energy. He served as the intellectual *consigliere* of the project these past two years.

My literary agent Esmond Harmsworth, of Zachary, Schuster, Harmsworth, is truly one in a millio (I know this because when I tell my author friends what he has done to make this book a success, the jaws drop and they reach for a pen to write down his number). Rick Horgan at Crown saw the potenti of this project early on and pushed our team to produce a book that was not only interesting, but that would really help people transform their companies.

The research team we assembled was wonderfully committed and resourceful, and without each of them, this book would not have been possible. I owe a special thanks to Mark Campbell, who took th job of project research leader five years ago and whose belief in what we were trying to accomplish never flagged. Thanks also to Rachel Strate, Brian Waterhouse, and Dan Creer, whose tireless energy and great questions pushed us to create and implement a rigorous research model.

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To recognize everyone from the breakthrough companies and comparison companies who assisted us in our data collection, structured interviews, and historical market analysis would require a listing of several hundred people. We want each of these people to know how much we appreciated their tim and instrumental help, and regret we cannot mention each by name here. A few who were particularl important were Beverly Brown, Allison Green, Linda Haneborg, Betty Johnson, Marlys Knutsen, Charlene Little, Laura Saxby Lynch, Molly Nelder, and Sherry Terzian.

We also owe a special debt of gratitude to the nearly 1,500 managers we met with during our fieldwork with fifty-two companies over a period of six years. Our experience working side by side with you made the results of our analytical work come alive.

Jim Wilburn has been a friend and mentor for twenty-five years, and it was he, more than anyone else, who set me on the path of writing. Joel Kotkin, Ichak Adizes, Paul Albrecht, Ruth Atteberry, Dick Ellsworth, Bob Fraley, Don Griesinger, Larry Hall, Dick Kaehler, Alan and Peggy Ludington, Chuck Morrisey, John Nicks, Doug Plank, Gabriella Soroldoni, and James Thomas all encouraged m to see myself as a writer, and their encouragement has finally borne fruit—though probably not in th same decade that any of them might have anticipated. Tom Turney, Steve Carpenter, Don Clark, Jose Collazo, Steve Hauck, and Steve Olson were all instrumental people in my early years as a technolog CEO, and their influence in these pages will be obvious to them.

Finally, a special thanks to Jennifer McMichael, whose fingerprints are all over this book—from assisting in the data analysis, manuscript review and revision, and supporting me in the myriad of other ways she supports me each day.

If you want to build a ship, don't drum up the men to gather wood, divide the work and give orders. Instead, teach them to yearn for the vast and endless sea.

ANTOINE DE SAINT-EXUPÉRY

1

INTRODUCTION

The beginning of knowledge is the discovery of something we do not understand.
FRANK HERBERT

I BUMPED INTO *Überguru* Peter Drucker one afternoon in 1994, on a tree-lined sidewalk at Claremont University. Over a Diet Coke, we had a short conversation that would change the course of my life, and would result—almost fifteen years later—in the writing of this book.

I was in my mid-thirties at the time, and had just been named chairman of Collectech Systems—a two-time *Inc.* 500 technology company based in Los Angeles. I believed Collectech had the potential for exponential growth—perhaps even to revolutionize the industry—but I also sensed that we were a a crucial transition point that would require wrenching changes if we were going to reach our full potential. Making those changes, I feared, might also run the company aground. At the time I ran into Drucker that fateful afternoon, I was making the three-hour, round-trip drive to Claremont University's Drucker Center three times a week to take PhD classes from Drucker and his colleagues hoping they could help me make sense of the difficult issues we faced as a company. My frustration, however, was growing and I decided to ask the master for some help. "Why can't I find the book that helps people like me solve the real problems of moving beyond the entrepreneurial stage of development?" I asked Drucker. After a moment of thought, he looked up and flashed his famous toothy, Zen master grin. "Because," he grunted in his thick Austrian accent, "you haven't written it yet."

Shortly after our conversation, the wheels came off of our business, and I didn't have time to think about books, neither reading nor writing them. I dropped out of the doctoral program with only my dissertation left to complete and spent the next several years fighting for our firm's survival. Collectech emerged from the crisis stronger than ever, with a new business model that propelled the company from revenues of $10 million to $100 million in just over three years. As the company transitioned out of that difficult time, my mind returned again to that conversation with Drucker. Where, I wondered, was the book that could help a leader steer a firm through the difficult terrain my firm had just navigated, the terrain that lies just beyond the entrepreneurial stage of development? Drucker's words echoed in my mind: "…you haven't written it yet."

Then, in 2002, I agreed to be a keynote speaker at a CEO conference in Detroit. At dinner the night before the event, I found myself seated next to the event's other keynote, *Good to Great* author Jim Collins. We discussed his book over dinner and I shared with him my frustration about the lack of books on how to help companies break through the entrepreneurial stage. I pointed out that all the *Good to Great* companies were big companies (in his book the average company has sales of $32 billion),[1] years or even decades away from their entrepreneurial roots. I wondered aloud whether we would learn different things if we studied companies closer to the time of their entrepreneurial breakthrough. "What a great research question," he replied, and then went on to encourage me to do my own study using research methods similar to those he used in *Good to Great*.

SOMEONE NEEDED TO WRITE THIS BOOK

On the plane ride home from Detroit, I decided that if the universe delivers signs, mine could not be any clearer. Two of the world's most respected observers of the business world had told me that I needed to write this book. I reached into the seat pocket and pulled out an airsickness bag and wrote out a list of three questions that would become the basis for *The Breakthrough Company:*

1. Why do most companies start small and stay that way?
2. What is special about the handful of companies that successfully "break through" the entrepreneurial stage of development?
3. What can a leader do to ensure that his company maximizes its chances for breakthrough?

You might think that there would be hundreds of books on the subject, but a quick review of the bookshelves of any bookstore proves otherwise. Business books tend to fall into two broad categories (1) How-to books for the small business owner on subjects like basic management, sales, et cetera; and (2) books on leadership and management that focus primarily on the very largest businesses.

> Only about a tenth of 1 percent (0.10%) of U.S. firms ever achieve revenues of more than $250 million in sales. A tiny 0.036 percent will grow to reach $1 billion in sales.

In fact, 99 percent of the business advice churned out by the publishing and consulting industries i written for people working at giant firms. Think I am exaggerating? Consider this: In America, only about 0.10 percent of businesses ever achieve annual sales of $250 million[2]—a tiny size relative to th companies in *Good to Great*. And yet the majority of business books written clearly focus on that top tenth of a percent. Does it seem like every magazine article or book you pick up mentions the same companies? That is because they do. We went to the Harvard Business Review Web site (*HBR*) and typed in the names of five companies that seem to pop up most often in magazine articles and business books. Here's what we found:

- 502 articles mentioned IBM
- 438 articles mentioned General Electric
- 122 articles mentioned Dell Computer
- 169 articles mentioned Wal-Mart
- 73 articles mentioned Southwest Airlines

The five big companies produced a total of 1,304 search hits from the roughly 2,000 articles that have been published since the *HBR* was founded in 1922. Even after adjusting for the fact that many articles refer to more than one of the "big five" in the same article, nearly 50 percent of all of the articles ever published by the *HBR* mention at least one of the five companies (nearly 25 percent of the articles mention IBM alone). These are all truly great companies, and I am sure they have much t teach us about running a business. Does it stand to reason, however, that just five firms account for 5 percent of the business knowledge created over the past eighty-five years? And what really can the leader of a small or mid-sized firm learn by studying the ways of IBM? Wouldn't it be better if a person studied the success factors of firms more like his or her own?

If you are like most businesspeople, you live a very different life from the ones lived by business celebrities described in the headlines of *BusinessWeek* and *The Wall Street Journal*. You don't relax company-owned New York apartments, travel about in teak-paneled private jets, or enjoy severance packages that guarantee you riches whether or not you succeed at your job. Instead, chances are you live your life on the ground, shoulder to shoulder with your troops, fighting for beachheads in tough markets. And you are probably also genuinely and deeply interested in what your company makes or creates—whether it be equipping the world's largest telecommunications companies with the latest technology or distributing construction materials. To you, a business is far more than boxes on an organization chart or a collection of assets to be exploited. Your company is probably a place where people band together to do what humans have been doing since they left the caves: working together build something important—something bigger than themselves.

> A search of the Harvard Business Review Web site revealed that nearly 50 percent of the article published by the *Harvard Business Review* mention at least one of the following companies: IBM, GE, Dell, Wal-Mart, and Southwest Airlines.

Most of us will never run an IBM or a GE, but millions of us around the world run mid-sized entrepreneurial companies, some of which have the potential to become significant, lasting, and difference-making organizations. But which ones? What are the characteristics that will separate thos that break through from those that don't? And what can we do as leaders to help our organizations maximize their potential for breakthrough?

My research team and I, along with a panel of thought leaders, have spent the past five years searching for answers to these questions. We set out to discover what enables little firms to become big. Our search led us to create and analyze what we believe is the most comprehensive database of more than 7,000 of America's fastest growing private and public companies. In addition, we have talked to more than 1,500 key executives, and reviewed and cataloged more than 5,600 articles. And make sure we understood the issues from the inside out, we conducted intensive ninety-day studies with fifty-two firms ranging in size from $9 million to $3 billion in annual sales.

> We studied more than 7,000 companies, talked to more than 1,500 key executives, and reviewed and cataloged more than 5,600 articles, annual reports, and studies.

My goal was to conduct the most exhaustive research ever undertaken on the subject, and to write the book that I had always wanted to read—the one that fills in some of the details of the territory tha lies just beyond the entrepreneurial stage of development. I wanted to identify the secrets of breakthrough.

THIS IS NOT INTENDED TO BE A RECIPE BOOK

We do not suggest that our reflections here on the dynamics of breakthrough are the be-all and end-a on the subject. As Boris Pasternak once said, “What is laid down, ordered, and factual is never enough to ~~embrace the whole truth: Life always spills over the rim of every cup.” Our hope is that the~~ ideas contained within this book make some small contribution to the conceptual blueprint of how businesses grow and that what is laid down in these pages spills into other “cups” of inquiry in the future.

As hard as it is to grow a company, wouldn’t it be nice if there was a “recipe” for creating a company with sustained high performance? It is tempting to dream that if we could just find the right combination of ingredients—a cup of customer loyalty, two tablespoons of *Blue Ocean Strategy*, a dash of reengineering, and a pinch of Six Sigma—we could unlock the secrets of building the breakthrough company. But believing in that dream would be like believing that one could, after a lifetime of “painting by numbers,” suddenly produce a masterpiece. That just doesn’t happen. However, if someone with a stroke of talent studies the work of great masters and comes to understand the interplay of light, color, structure, and composition, and then spends hours and hours playing with these aspects on his own canvas, he might create a great painting one day. In cooking, the goal of a person looking for a recipe is to cook an edible meal. The goal of aspiring chefs is to gain such a deep and visceral understanding of tastes and textures that they can create something wholly new and distinct—a breakthrough, so to speak. Breakthrough performance, whether in cooking, painting, and/or growing a business, is hard. In our study we were struck by how the people at all levels of the breakthrough companies seemed to get that. We are honored that they allowed us into their kitchens and studios—they reminded us of chefs in their aprons, drizzling on the olive oil, and painters bent over colorful canvases. We hope we do their stories justice in these pages.

2

THROWING THE DYNO

The important thing is this: to be able at any moment to sacrifice what we are for what we could become.
CHARLES DU BOIS

A SHORT HIKE from my home stands a 1,000-foot face of sheer granite that the locals call the Thumb I recently found myself balanced well up that precipitous wall on a too-small foothold looking across at a too-distant handhold leading up to the next pitch. As I mentally planned my retreat back down th face, my climbing partner let me know she wasn't having it: "Keith, time to throw the dyno!" she shouted from below.

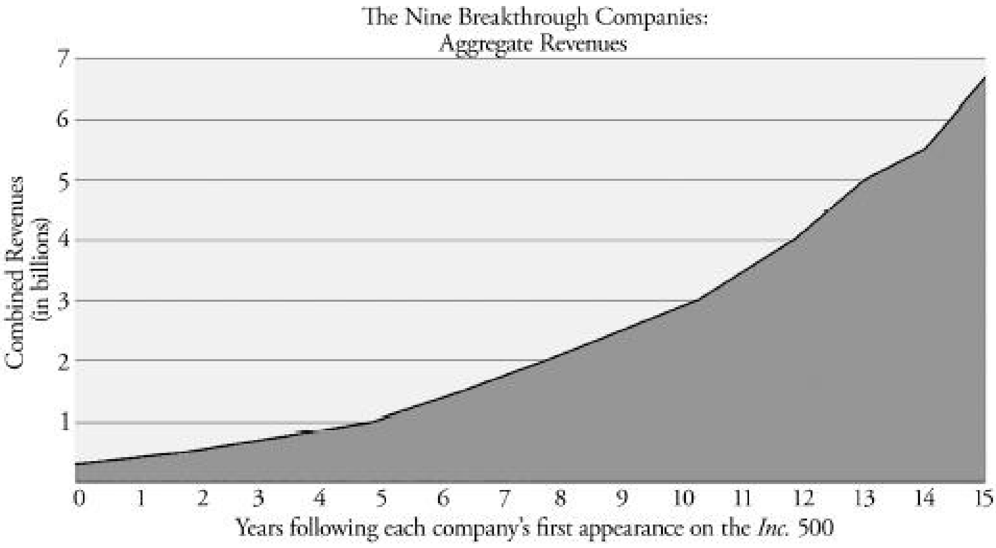
In climbing parlance, a "dyno" (short for dynamic) is a quick, gymnastic leap to a distant hold. If you miss, you can get pretty banged up. I pressed my face against the warm rock face, drew a deep breath, and closed my eyes—then opened them and lunged upward for the hold. Leaving the safety of my position, I stretched for what I hoped was the safety of another, higher position—just beyond my grasp.

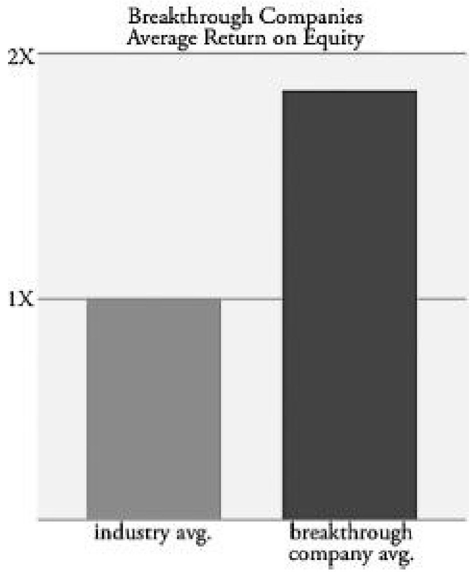
Growing a business can be a lot like rock climbing. Most businesses start out carving small but secure footholds at the lower elevations of some industry—usually by spotting some overlooked nich in the market they can defend. Some are satisfied to stay in the lower elevations and eke out a living. But for many, as time passes their aspirations rise, and their eyes turn upward toward footholds and handholds just out of reach. These are the breakthrough companies, the ones always focused on the next challenge up ahead, the ones ready to "risk what they are for what they can become." Breakthrough companies are distinguished by their willingness to throw the dyno.

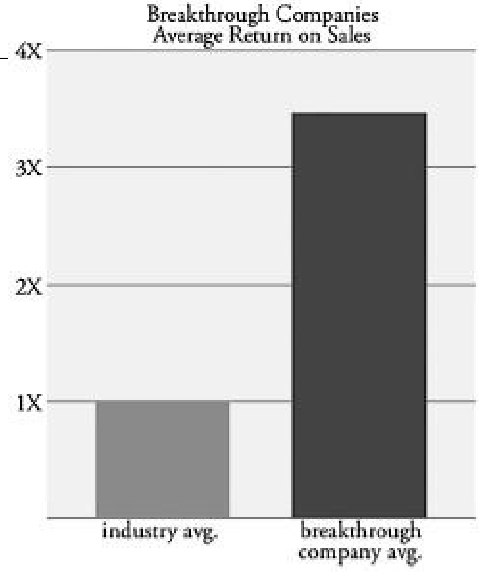
What does it take to build a breakthrough company, to move from chasing markets to actually influencing them? Five years ago we launched what we believe is the most exhaustive research effort in history to answer this question. We created a database of 7,000-plus companies—every company that was listed on *Inc.* magazine's annual list of the 500 fastest growing since it first published the lis in 1982. Using a broad range of public and private resources, we gathered information on each company's growth rate, profitability, and size, and rank ordered them according to their long-term financial performance (for a detailed description of our research, see Research Note B, The Breakthrough Study).

The tables that follow show the revenue and profit performance of the nine breakthrough companie identified by our study.[1] In the fifteen years following their appearance on *Inc.*'s list of the 500 fastes growing companies, the median revenue of these nine companies grew from $14.4 million to more than $700 million.[2] Cumulative revenues of the nine companies grew from $298 million to $6.6 billion over fifteen years, and at the end of 2006 these nine companies had combined revenues of $7. billion. And these companies are distinguished not just by their revenue growth—they are profit machines. They outperformed their competitors on profit by a factor of 3 to 1. A person looking for a blueprint for long-term profitable growth would be hard pressed to find nine better examples.

~~Six of the nine companies we studied went public during the period 1993–2004. A dollar invested~~ i each of these companies at their initial public offerings (a $6 total investment) would have been wort $250 if each stock were held for thirteen years following its IPO. That same $6 invested in the S&P 500 over that same time period would have yielded just $25—meaning that an investment in six public breakthrough companies at the time of IPO grew ten times faster than the S&P.[3] If an investor held those same six stocks until December 31, 2006, the value of the initial $6.00 investment would b $482.36, generating a staggering 7,939 percent return.







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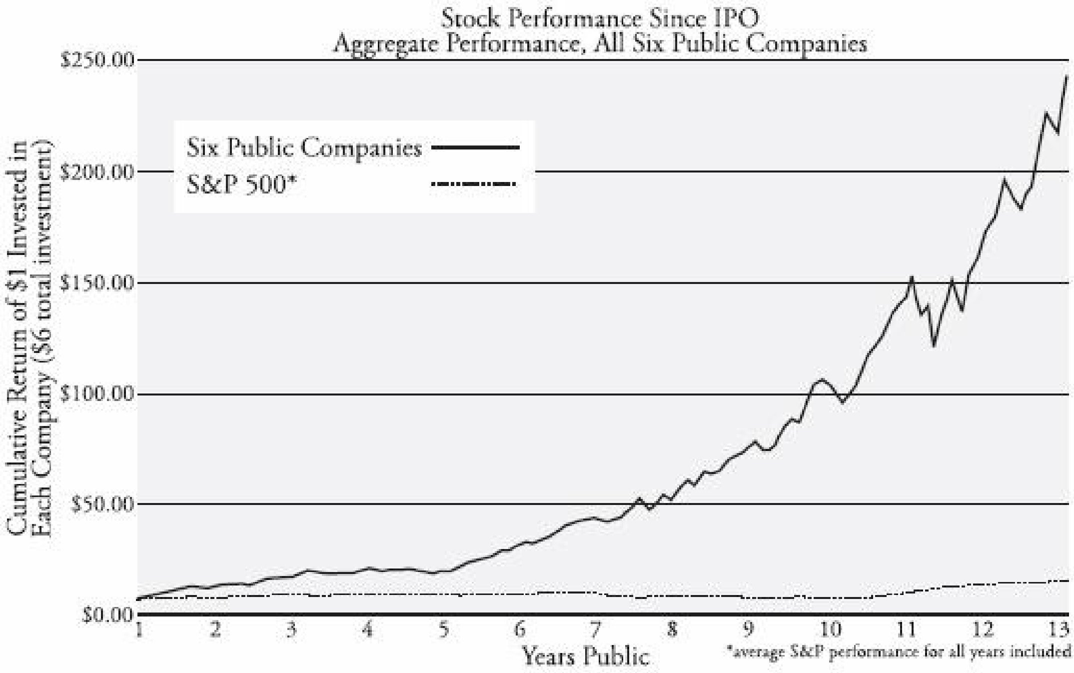


What impressed us most about these nine breakthrough companies was not their similarities, but their differences. They were founded in places as diverse as the "American Siberia" of northern Minnesota, sunny Florida, innovation-centric Silicon Valley, and glass-skyscrapered Dallas. The breakthrough companies come in a wide variety of shapes and styles: high-tech, low-tech, no-tech, ar everything in between. ADTRAN, which manufactures networking equipment in Huntsville, Alabama employs some of the most sophisticated microprocessor design and manufacturing technology in the world and generates phenomenal financial results. When the world's major banks began tracking financial transactions for links to terrorist activity, they didn't turn to the U.S. government for help; they visited the SAS Institute, the business intelligence and analytical software and services company in Cary, North Carolina. Chico's FAS in Fort Myers, Florida, shook up the fashion industry by becoming the anti–runway-model company by designing flattering apparel for middle-aged women, while Express Personnel in Oklahoma City created a network of staffing franchises with profit levels that would make any fast-food franchisee drool.

The Breakthrough Companies

Company	First Year on the Inc. 500	Revenues That Year	Current Status	Location
ADTRAN	1992	$42.6 million	Public	Huntsville, AL
Chico's FAS	1989	$6.2 million	Public	Fort Myers, FL
Express Personnel	1988	$50.0 million	Private	Oklahoma City, OK
Fastenal	1982	$3.7 million	Public	Winona, MN
Intuit	1990	$18.7 million	Public	Mountainview, CA
Paychex	1982	$14.4 million	Public	Rochester, NY
Polaris	1986	$90 million	Public	Medina, MN
SAS	1982	$10.1 million	Private	Cary, NC
The Staubach Company	1985	$2.8 million	Private	Addison, TX

Our study makes one thing clear: Building a breakthrough company is less about choosing the righ industry and more about acting on the opportunities already available in your existing business. All nine companies evolved from humble beginnings. Chico's didn't start as a fashion house; its founder Marvin and Helene Gralnick, began by buying folk art items in Mexico and selling them to tourists back in Florida. Then, they started experimenting with sweaters and clothing. Today, more than twenty-four years later, Chico's boasts the *highest profit per square selling foot of any clothing retailer*. At about $780 sales per foot, Chico's easily trumps the figures posted by the Gap ($409), An Taylor ($482), and even the Limited ($543).[4]

When Tom Golisano started Paychex, the payroll processing company in Rochester, New York, he spent his mornings drumming up new business selling door-to-door, and then used his afternoons and evenings to input payroll information by hand for his small business clients. Paychex, which was founded in 1971, went on to achieve ten straight years of more than 30 percent profit growth and, at the time of this writing, its stock was trading at ten-times revenue. That's ten-times *revenue*, not profit.[5]

GROWTH MATTERS

"What if I don't want to build a big company?" you might ask. There are thousands of profitable sma and medium-sized businesses out there that support comfortable lifestyles for thousands of entrepreneurs and business owners, right? True enough, but the harsh reality is that over the long terr companies either grow or die.[6] Getting your business to grow profitably frees up resources that you can invest in new products or in expanding the value you provide to customers. One thing you can count on: If you are not investing in making life better for your customers, your competitors will be. Growth is also important if you hope to attract and keep the best employees. For employees, growth means opportunity for advancement and new and more exciting challenges. If employees can't get those expanded opportunities at your firm, they are likely to move to another firm where they can.

And growth isn't just important for the company itself, it is important to the nation. One study suggests that just 4 percent of companies generate 60 percent of all new jobs in the U.S. economy.[7]

Figuring out how to turn everyday companies into breakthrough performers should be a national priority.

But growth by itself isn't the answer. Our study of twenty-five years of *Inc*. 500 data suggests that just as many *Inc*. 500 firms fail to reach their true potential because they grew *too fast* as because the grew too slow. In rock climbing, "throwing the dyno" is a quick, momentary move; in business it is a state of mind. Breakthrough is less a matter of bold strategic leaps than it is one of willful and diligen ascent from one foothold to the next. The difficult task of leadership is to make sure the organization raises its ability to handle growth as rapidly as it does its revenue line. Only then will it be able to achieve sustained profitable growth.

LETTING THE NUMBERS DECIDE

So where is the best place to discover the characteristics that enable breakthrough? We immediately ruled out just cherry-picking from the same lists of big-name companies most people write about. W wanted to be more scientific, to let hard analysis of performance numbers guide us.

We also ruled out the sort of ivory-tower research that is disconnected from the real issues faced b real business. We spent five years in intensive fieldwork with fifty-two different U.S. firms ranging i size from $6 million to $3 billion. Each field study lasted a minimum of ninety days. We spoke with from twenty to sixty people per company (1,441 in all) to learn their individual perspectives regardin where their firm stood, including the firm's potential for growth, its most promising products or services, its most difficult competitors, its relationships with customers, and its most important internal and external problems. Then for periods ranging from ninety days to three years, we worked with those companies as they created initiatives to boost their performance. The field studies, more than any other aspect of our research, gave us real-world insights into how breakthrough capabilities are actually built. (For a detailed description of our fieldwork, see Research Note A: Exploratory Fieldwork.)

We finished our third year of field studies armed with a list of questions that would drive our broader empirical research. We settled on *Inc*.'s list of the 500 fastest growing U.S. firms as a data source because it is the most widely recognized list of U.S. growth companies available (see Researc Note C, *Inc.* 500). We built a database containing performance information on every *Inc.* 500 compar listed between 1982 and 2004 (more than 7,000 companies in all). We then combined this informatio with data from public and proprietary data sources like Hoover's and Dun & Bradstreet to see what had become of these companies in the years since their *Inc.* 500 appearance.

While many of the companies were still in business either as private or public entities, a high percentage had been acquired by larger companies or had gone out of business altogether. Our research team went to work on the survivors, matching up their revenue and profit growth numbers with industry figures to identify nine companies that posted the top performance. To narrow our focu we set a filter to exclude any companies with annual revenues of less than $250 million and more tha $2 billion. We eliminated those with revenues of less than $250 million to make sure that the companies were big enough to have faced the full range of obstacles on the path to breakthrough. We eliminated those above $2 billion because we believed that former *Inc.* companies with revenues in excess of $2 billion (like Microsoft and Oracle) may now be so large that the characteristics of breakthrough may be too hard to locate and isolate in them.

We then added additional information on historical financial performance and conducted intensive research on these remaining companies using sources such as Reuters on-Demand, LexisNexus, and Thompson. We divided our list between public and private companies and rank ordered each list base on cumulative revenue growth rate, profitability, and size as compared with the industry average. We ~~then reviewed annual reports going back as far as twenty-four years and gained access to industry~~ reports from third-party analytical firms such as Gartner and IDC, as well as industry reports from th investment community. We tapped every news and data source we could find for background—more than 5,600 reports, white papers, and articles from the national, local, business, and specialized trade press in all. We also conducted longitudinal analysis of the financial performance of each breakthrough company and compared that performance with the general stock market and industry segment benchmarks. Since all of the breakthrough companies and their comparison companies were private for some portion of the 1982–2004 comparison period, we sought, and in most cases received access to private historical information that aided us significantly in our research. This information included: company histories, copies of presentations at company events, annual strategic plans and budgets, project summaries, videotaped interviews, and, in many cases, unpublished and detailed product, market, competitive, and financial information.

But only so much research can be done from a computer screen or in a library. In our most important phase, my research team and I bought plane tickets, made car reservations, and set out to d some old-fashioned shoe-leather reporting—logging hundreds of hours of interviews with people at a levels at the nine breakthrough companies.

COMPARISON COMPANIES

We wanted not only to study companies that most successfully navigated the route to breakthrough, we wanted to compare them with similar companies that failed to achieve the same sustained levels o performance.

Our comparison studies were able to shed considerable light on the key factors that enable breakthrough performance. Consider for example Fastenal, an industrial distributor in Winona, Minnesota, and one of its key early competitors, Endries International, located in Brillion, Wisconsi Not only were both companies founded around the same time (Fastenal in 1967, Endries in 1970), there was only a four-hour drive between them. Despite competition from the likes of established veterans like W.W. Grainger in nearby Lake Forest, Illinois, both companies had early success sellin nuts and bolts to area manufacturers, and by 1983, when Fastenal earned its spot on the *Inc.* 500, both companies had revenues of several million dollars a year. But something changed soon afterward. While Endries continued to grow modestly over the next twenty years, even topping $150 million in revenue in 2004, Fastenal hitched a ride on a rocket ship. By 1993, Fastenal earned $100 million in annual revenues and by 2004, it crossed the billion-dollar threshold, outpacing its would-be rival tenfold. In 2006, just two years later, as Fastenal opened its two-thousandth store and cracked the top 10 of trade magazine *Industrial Distribution*'s list of the country's largest distributors, Endries quiet sold its 30 locations to another rival, Ferguson in Newport News, Virginia.[8]

Comparison Companies

Breakthrough Company	Comparison Company	Comparison Company Current Status
ADTRAN	PairGain	Acquired
Chico's FAS	J. Jill Group	Acquired
Express Personnel	Westaff	Public
Fastenal	Endries International	Acquired

Intuit	Meca Software	Acquired
Paychex	InterPay	Acquired
Polaris	Arctic Cat	Public
SAS	SPSS	Public
The Staubach Company	Studley Inc.	Private

Why were Fastenal and the other eight companies able to break through while Endries and the othe comparison companies were not? Were they really that different? Was there something more than jus luck at play? You bet.

A FEW SQUIRTS FROM THE GRAPEFRUIT

Anyone who has ever made a study of anything knows one thing for certain: The best part is when yo come face-to-face with the unexpected. Surprising findings are, as star detective Charlie Chan once said, "like squirt from aggressive grapefruit." Our study produced "grapefruit squirts" at every turn, s many that we concluded that much of what is believed about what it takes to build a breakthrough company is just plain wrong. Here are just a few of the surprises we uncovered:

(1) The most interesting companies may not operate in the markets that Wall Street and the business press consider interesting or "cool."

When we launched our study, we worried that perhaps the best-performing companies would all come from a single sector of the economy like tech, leaving us with findings that wouldn't be applicable to the broader market. But our concerns were unfounded. Many of the breakthrough companies began in market segments experts considered unattractive at the time. We weren't surprised to identify several high-tech firms like Intuit, SAS, and ADTRAN among the breakthrough companies—but we certainly didn't expect to find a nuts-and-bolts distributor, a snowmobile maker, payroll processor, or even a niche real estate business. At its start, Tom Golisano's strategy to proces payroll for companies with an average of seventeen employees seemed downright quaint,[9] as did Roger Staubach's idea for a commercial real estate business that primarily represented tenants. Whe W. Hall Wendell Jr. led a managed buyout of Polaris in 1981, the snowmobile business was on its back.[10] As the research opened our minds, we learned that breakthrough companies actually fall into three categories: (1) those in hot markets that figure out how to dominate those hot markets; (2) thos in dud markets that figure out a way to ignite the excitement in their sector; and (3) those in stalled o dead markets that figure out a way to transition into more attractive markets.

(2) Sticking to the knitting won't always get you there.

Just as the breakthrough companies ignored the so-called experts when it came to the prospects fo their industry, they also kept redefining their businesses. While the textbooks—and the consultants— might have suggested that Polaris should remain focused on its core snowmobile business, the company hopped the fence into the far more competitive and profitable ATV market, facing off against some of Japan’s most powerful *keiretsu* at a time when most believed Japanese industry woul take over the world.[11] ADTRAN recently left the relative safety of its telecom niche to do battle over corporate clients with Cisco, the multibillion-dollar tech company in San Jose, California.[12] When Intuit squared off against Microsoft in the small-business accounting market, after having just bestec Bill Gates to gain control of the market for personal financial management software, there were man who questioned Scott Cook’s sanity. Cook’s decision, however, like the ones made by the other breakthrough company leaders, was critical to creating the kind of performance that put these companies on our distinctive list.

(3) Don’t look for extraordinary people; build a place where ordinary people can do extraordinary things.

While they certainly obsessed about each individual hiring decision, breakthrough companies also focused on creating systems that helped their people grow along with the business. “We built this company hiring who we could afford to hire,” said Lee Hein, a regional vice president at Fastenal. “What we found was that the average company today doesn’t have a clue what people are capable of you believe in them.”[13] Consider also Express Personnel, a company that earns its way by helping people find jobs: more than 350,000 billed hours’ worth in 2006 through its 588 franchise locations i the United States and Canada.[14] While the staff at headquarters in Oklahoma City is involved in the awarding of franchises, do you think they are involved in each of the decisions made on the front line at Express? Think again.

(4) It’s not about where (or whether) you went to school.

The diversity of the people who established and/or are running the nine breakthrough companies is simply astounding. The group includes: a former college professor and PhD in mathematics (Jim Goodnight at SAS); two Harvard MBAs (Intuit’s Scott Cook, who is also a Bain Consulting alum, an Tom Tiller, once one of General Electric’s rising stars); a guy who finished his associate degree (Tor Golisano at Paychex); and Scott Edmonds, who hit the bricks right out of high school in Virginia and rose to become CEO of Wall Street darling, Chico’s. Not only is Bob Funk, the CEO of Express, an ordained minister and cattle rancher, he’s also the elected chairman of the Federal Reserve’s Conference of Chairmen, which advises the Board of Governors of the Federal Reserve System.[15] Th success of these individual leaders, however, seems less related to their background, training, and expertise than how they see the world, and what they do with those insights. More on this in chapter Building Company Character.

(5) You don’t always need other people’s money.

We’ve all heard the professional investor’s elevator pitch, “Sure, you can grow your business, but you can grow it faster with our money.” We were shocked by the fact that not one of nine breakthrough companies was funded by venture capital in their start-up years. Scott Cook tried to rai venture money for Intuit and was turned down by more than twenty firms (he accepted a small amou of private money just before Intuit went public in 1993, mainly to tap the genius of Silicon Valley legendary VCs John Doerr and Burt McMurtry).[16] Of course, bringing in outside money at the right time can be a good thing. We saw considerable evidence in our fieldwork, in fact, that the right financial partner at the right time can greatly increase a company's prospects for sustained growth (f more on the potential benefits of outside money, see our discussion in chapter 7, Erecting Scaffolding).

(6) How employees feel about working in a place is a significant driver of success.

The first company we visited on our tour of the breakthrough companies was Intuit. As we waited the lobby before our meeting with cofounder Scott Cook, we noticed an award from *Fortune* magazine, naming Intuit one of *Fortune* magazine's best places to work, hanging prominently on the wall.[17] As we moved around the country visiting the other breakthrough companies, we experienced déjà vu as that same award kept popping up. When we returned home from our travels, we weren't really surprised to learn that the three companies that applied for *Fortune*'s Best Places to Work award made the list a combined twenty years.[18] A key discovery, driven home in our visits to one breakthrough company after another, was that the task of building a great place to work wasn't delegated to the human resources department alone. The top people in the company thought about it every day.

UNRAVELING THE BREAKTHROUGH DILEMMA

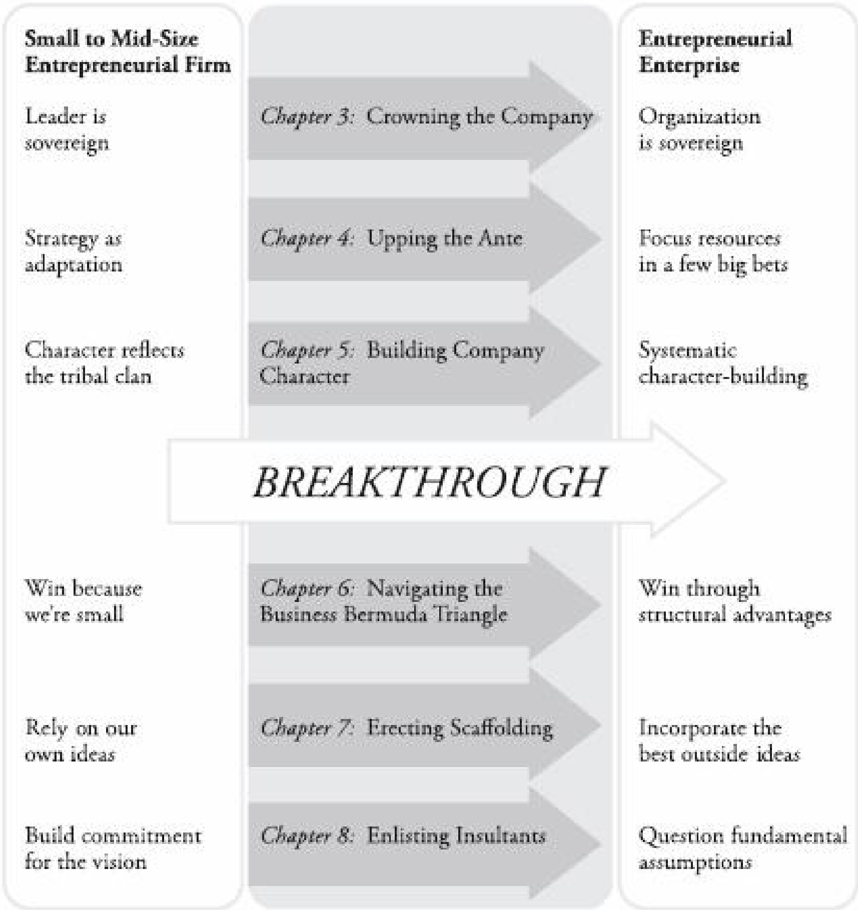
One key point we noted from our field studies was how different the average $2 million firm is from the average $250 million firm, and how different it still is from the average $2 billion firm. As a firm grows, it undergoes subtle changes in how it makes decisions and sets priorities; it often even develops a different language for identifying and communicating what is important. This realization highlighted a key challenge involved in achieving long-term growth: the need for a company to learn to operate differently as it grows larger, while at the same time retaining all the best qualities that allowed it to thrive as a smaller business. Breakthrough companies seek to integrate new tools, processes, and ideas to help them better manage the growing complexity of their worlds without, at the same time, losing the firm's unique aspects that inspire people to give their best efforts.

Writers often lump companies into two general categories, "entrepreneurial firms" and "professionally managed firms,"[19] a categorization that both oversimplifies and distorts how firms really work. We spent time in nearly seventy firms, many that clearly fit the classic definition of "entrepreneurial firm," and yet it would be unfair and inaccurate to characterize all of them as "unprofessionally managed" as some experts would. Many of these companies were, in fact, managed in a very professional way—though perhaps not in the way a manager in a large bureaucratic organization would recognize. Conversely, we spent time in several large organizations in which the "professional management" tail had clearly begun to wag the company dog. What these firms needed most, it seemed to us, was a healthy dose of entrepreneurship.

We began to see the story of the breakthrough company not as a journey from an entrepreneurial firm to a professionally managed firm, but from small or mid-sized entrepreneurial firm to *entrepreneurial enterprise.*

The next six chapters of the book describe the path to building an entrepreneurial enterprise.

Chapter 9, Graduating from Tough Times U, considers how firms react differently to setbacks and cris~~es and looks at how breakthrough companies turn lessons learned during periods of hardship~~ to their long-term advantage. Chapter 10 gives some of the highlights of what we learned in the more than five years we spent actually working with companies, how firms at all stages of development ca build breakthrough capabilities. This was perhaps the most important insight our study produced: There is really no such thing as a breakthrough company, rather there are principles of breakthrough that any firm can adopt to create breakthrough performance. Provided below is a summary of those breakthrough principles, which make up the remaining chapters of this book:



CHAPTER 3: CROWNING THE COMPANY

Is an organization built to meet the needs of its leader or founding family, or does it strive to be something that is bigger than any one of its members? Breakthrough companies, our research found, go to great lengths to create organizations built around the belief that the good of the organization, ar not the whims of leadership, should drive the firm.

CHAPTER 4: UPPING THE ANTE

Think entrepreneurial leaders are, by definition, big risk takers? Think again. Often when they get ahead in the game, they tend to begin to play tight, at the very time their firms are positioned to rake in the big pots. Intuit and Polaris would not be the household names they are today if it were not for their willingness to place increasingly bigger bets as the stakes of the game grew bigger.

CHAPTER 5: BUILDING COMPANY CHARACTER

It turns out that how the people in a company treat each other and their customers is vital to breakthrough. But we discovered that most breakthrough companies don’t spend a lot of time draftin values statements and fretting about corporate culture. They focus instead on aligning what they say with what they actually do. Anyone can write a values statement. It is quite another thing to imbue an organization with character.

CHAPTER 6: NAVIGATING THE BUSINESS BERMUDA TRIANGLE

When small firms succeed, it’s usually because they get good at leveraging the advantages of smallness: giving customers what they want, reacting quickly, and keeping costs low. But it’s hard to continue to act small as you get bigger. If companies learn this lesson too late, they risk being lost in the Business Bermuda Triangle.

CHAPTER 7: ERECTING SCAFFOLDING

Scaffolding is a temporary structure built outside a building to enable construction workers to wor on increasingly higher levels of a building. In the same way, we found that breakthrough firms build “scaffolding” for their organizations: outside resources and ideas that enable them to take their businesses to the next level.

CHAPTER 8: ENLISTING INSULTANTS

Walter Lippmann once said, “The best servants of the people, like the best valets, must whisper unpleasant truths in the master’s ear. It is the court fool, not the foolish courtier, whom the king can least afford to lose.”[20] Breakthrough company leaders realize that what is true for a business today might not be true tomorrow—and that it is vital that they build an atmosphere in which people are encouraged to question the fundamental assumptions of the business.

CHAPTER 9: GRADUATING FROM TOUGH TIMES U

Nothing tests an organization like a crisis and, without exception, each of our breakthrough companies faced a pivotal moment that could have radically altered the firm’s future. Breakthrough leaders, as compared to most CEOs, see difficult times as opportunities for the organization to develop a crystal-clear focus on its most important initiatives and even to tap into energies in people that tend to go dormant during the good times.

CHAPTER 10: BUILDING BREAKTHROUGH CAPABILITIES

Parallel with our empirical and field studies, we worked with a number of firms to help them develop the capabilities that would help them become successful entrepreneurial enterprises. This chapter ~~describes some of the most important things we have learned about moving companies~~ towar breakthrough performance and beyond.

AFTERWORD: POST-BREAKTHROUGH—AVOIDING BREAKDOWN

Does a company need one set of characteristics to reach breakthrough and another to continue a trajectory of growth as a big company? In this chapter, we reflect on the future fate of the breakthrough companies.

CASE STUDY IN THROWING THE DYNO

The Olson Company

Through our fieldwork with companies, we had the opportunity to watch first-hand companies successfully throwing the dyno. I had been tracking the Olson Company since Steve Olson founded it in 1988 in a small office he shared with Mark Buckland and an administrative assistant. Today Olson has grown into one of the nation’s leading providers of in-town affordabl living—winning the titles of Fastest Growing Builder in America and U.S. Homebuilder of the Year.

Steve contacted us in 2002, when his company’s revenues were about $200 million. “Our challenge,” Olson told us at the time, “is to get people at all levels of the organization involved building the strategy for the future of the company.” We worked with him and a group of twenty key managers for several years to develop and implement a dynamic approach to strategy that gave the company the ability to rapidly adapt on the fly and to tap the knowledge of people working in the regions to effect change.

Since then, revenues at the Olson Company have more than doubled to $500 million and the company has a several-billion-dollar construction backlog. More important, the Olson Company has grown from a mid-sized business to an *entrepreneurial enterprise,* capable of focusing its resources on a few big bets, building tangible structural advantages in its market space, incorporating the best ideas from outside the company while still staying true to its own unique company character.

3

CROWNING THE COMPANY

The bottleneck is always at the top of the bottle.
PETER DRUCKER

SCHOOLCHILDREN AROUND THE world learn that George Washington was the founding president of the United States, but not everyone knows that he nearly became the founding *king*. This turning point at the dawn of America's democracy, one that could have given Washington the honor he so craved as a young man, also helps illustrate the primary reason why so many entrepreneurial companies fail to crack the breakthrough barrier: Their founders fail to "crown the company."

At the end of the American Revolution, the fledgling nation was deeply troubled; bankrupt, exhausted by eight years of war, and torn with internal dissention. Some in the military believed that unless they crowned a king, the nation's chances of achieving unity—and survival—were slim. General George Washington was their natural choice. The nation's other founding fathers were a brilliant bunch—Thomas Jefferson, Alexander Hamilton, John Adams, and James Madison—but as a leader, Washington towered above them all. And as the Revolutionary War came to an end, his status was at its apex. As commander-in-chief, he had single-handedly held the revolution together and led ragtag militia to triumph over the world's greatest military power. But when Washington learned of the plan to crown him king, he flatly refused the offer. Rather than accepting the crown for himself, Washington insisted on crowning the country. Americans were building a nation that would be far bigger than any one person, he believed, and in large part because of his decision, the world's greatest democracy took root.[1]

Is your company building something that is far bigger than its leader? Without Washington's crucial decision to crown the country, it is unlikely that America would have come to occupy its current position on the world stage. And similarly, our research suggests that in order to achieve breakthrough, a company's leaders must be willing to "crown the company." In other words, they must put the interests of the firm above their own, harnessing the power of people at all levels in building the firm's future. Too many leaders, after they achieve some level of success, tend to make their organizations all about them. The investment community and business press share the blame; all too often, they are the ones bestowing the royal treatment on these individuals when perhaps, if they dug a bit deeper, they would discover that an organization's success is always the result of the efforts of many people.

If anyone in business today would have the right to make a business all about himself, it would be Roger Staubach, founder of The Staubach Company. After winning the Heisman Trophy as a junior at the Naval Academy in 1963, he delayed his NFL debut to complete a tour in Vietnam. He was considered past his prime in 1969 when, at the age of twenty-seven, he signed on as a tenth-round draft pick of the Dallas Cowboys. It was at the ripe old age of twenty-nine, after sitting on Coach Tom Landry's bench for two years, that Staubach burst into the sports world's consciousness, earning Mos sample content of The Breakthrough Company: How Everyday Companies Become Extraordinary Performers

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