A typology of growth

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The type of growth that a firm is producing should also be evaluated against impact on employees, customers and other stakeholders . — P.V. SIVAKUMAR

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Two fundamental motivational drivers in a capitalist economy, at least on the financial front, are profit and growth. Profit leads to sustainability, and ensures survival. Growth leads to a fast rate of capital accumulation for the owners of a firm. Market forces help to keep the profit motive in balance by ensuring that the forces of supply, demand and competition neutralise any attempt to achieve a disproportionate profit margin. The growth motive, on the other hand, seems to be far more subjective, and is often linked to the ambition of the owners of a firm. Of course market forces limit the ability to grow as well, but the greed of owners and investors often comes in the way and demands 'perpetual' growth.

In this article an attempt is made to look at a possible typology of growth. Firms need to actively question which type of growth they are currently pursuing, and whether they have the capacity to pursue it, and if not, they must either build capacity or decide to focus less on growth and more on maintenance of their existing position. The typology of growth outlined below does not necessarily represent sequential stages, but rather represents possible states that a firm could occupy at a given point in time.

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MARKET PENETRATION-LED GROWTH

This type of growth is seen when the addressable market for a product or service remains largely untapped, and there is a lot of headroom for rapid growth. One feature of this type of growth, unfortunately, is low focus on the customer, since the marginal cost of acquiring a new customer is negligibly low. Even if competition is intense, there would be enough for each player to survive on. In the absence of significant differences between competitor offerings, intangibles like brand equity play an important role in this type of growth phase. Another feature of this stage of growth is the entry of a lot of existing, diversified firms into the market aiming to deploy their surplus capital in a new growth area.

EFFICIENCY-LED GROWTH

As the market for a product or service nears saturation levels, achieving higher efficiency in existing processes may drive some amount of additional growth over the medium term. This efficiency may also manifest in the ability to retain existing customers. One feature of this stage of growth is that customers assume a far more central position in the firm's strategy. However, efficiency improvements are not a perpetual or long-term source of growth. Firms operating in saturated markets with limited efficiency-led growth prospects must seriously evaluate the growth question.

INNOVATION-LED GROWTH

Innovation can become a driver of growth particularly in conditions of near market saturation. Provided that the firm has a capacity to innovate, there is a possibility of delivering higher order variants of existing products and services to the same set of customers. This type of growth is far riskier than the above two kinds because the acceptance or rejection of innovation by customers may lead to a wide spectrum of payoffs.

DISRUPTION-LED GROWTH

Disruptive breakthroughs also offer the possibility to drive growth. However, typically disruptions are brought about by start-up firms that start from scratch to address new ways of looking at existing problems. As soon as a disruptive product or service offering is accepted and attains some critical size, competition steps in and drives market penetration, and sets in motion a new cycle of growth of the first kind enumerated above. The early stages of any disruption usually offer the highest scope for profit margins, and the later stages offer scope for sustained growth till saturation is achieved.

During each state described above, there is of course opportunity to merge with or acquire other firms to create a fresh growth cycle. Additionally, each type of growth outlined above requires a certain kind of capacity. While some firms may be good at penetrating markets, others may be good at developing the intellectual capital required to create disruptions. Thus, when constant demands for growth are made from a firm, it is important to assess which type of growth the firm is currently pursuing, and whether it has the capacity for that type of growth (or any other kind for that matter). If it doesn't have the capacity, then it is best to drop the idea of growth, and serve owners and investors by redistributing profits as dividends and achieving a steady return on capital. As a corollary, a firm attempting a type of growth for which it does not have the capacity can be considered to be delivering a lower quality, unsustainable type of growth.

Finally, the type of growth that a firm is producing must also be evaluated against a larger framework consisting not just of financial growth, but also impact on customers, society at large, employees and other stakeholders. In an ideal world, capital must chase "growth with quality," that is, firms that are delivering the right kind of growth in line with their competence, and, while doing so, create a greater good for all stakeholders across the spectrum.

(The author is a corporate strategy professional.)

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