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An Abdul Latif Jameel Company

CUTTING THROUGH THE COMPLEXITY: LEAN THINKING FOR HOLDING COMPANIES

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HOLDING COMPANIES ARE FREQUENTLY CHARACTERIZED BY THEIR COMPLEX GLOBAL OPERATIONS. TAKE BERKSHIRE HATHAWAY, FOR EXAMPLE, A HOLDING COMPANY WITH POSITIONS IN MULTIPLE, DISPARATE INDUSTRIES — STRETCHING FROM UTILITIES TO RAILROADS AND INSURANCE— AND OPERATIONS AROUND WORLDWIDE.

This multifaceted structure comes with a unique set of challenges. Senior managers must tackle difficult decisions about resource and cost allocations across multiple, fundamentally different business units and product lines. How can holding companies navigate the complexity and diversity inherent to their businesses while ensuring a widespread focus on value creation?

There's no magic pill, but Lean Management principles — synonymous with effective, zero-waste processes — can make a meaningful impact. *"Lean techniques are recognized as the single most effective business improvement strategy to achieve long-term, profitable growth, no matter how complicated or large the holding company,"* said Patrick Wiebusch, Co-Founder and Managing Partner of Four Principles. *"With the right implementation tools and processes, holding companies can harness the measurable, tangible benefits of Lean thinking."*

GETTING STARTED: KEY CONSIDERATIONS FOR IMPLEMENTING LEAN IN HOLDING COMPANIES

When implementing Lean in a holding company, the first major steps are anchored in establishing an understanding of the big picture and setting the overall direction. The following four considerations often serve as the starting point:

1. What is the role of the holding company?

Objective: Determine and optimize the core functions and tasks the holding company is performing; clarify the operational role of the holding company.

Ultimately, Lean thinking posits that supervisory and service-oriented responsibilities should be separated and streamlined. The holding company is best suited to focus on tasks that are necessary for achievement of corporate goals and governance, or required from a regulatory or monitoring perspective. These tasks include defining objectives, standardizing and harmonizing various interests and monitoring the operational businesses. As a result, expertise-driven, transaction-driven and business-specific tasks are funneled downward to the proper business divisions. The holding company serves as the corporate center, providing leadership and creating the context for efficient growth.

2. How should the business units operate?

Objective: Define and analyze the internal value streams to empower business units to act flexibly and with appropriate autonomy, while generating sustainable growth. This involves detailed mapping of processes and agreement upon key business metrics and goals.

A large Latin American conglomerate, for example, used Lean principles to divide its units into three groups: new businesses, "cash cows" (reliable cash generators) and "tiger businesses" (smaller money-losing businesses).

Working with Lean experts, the company then defined clear, sustainable strategies for each group. As a result, the holding company's return on invested capital increased from 13% to 25% over two years.

3. Where can expertise be aggregated and services shared?

Objective: Identify synergies and areas of functional excellence to eliminate inefficiencies and waste.

To increase productivity and effectiveness, holding companies can consolidate expert knowledge in designated hubs or centers of excellence. Companies can also benefit by identifying opportunities to realize and improve shared services programs. Together, these initiatives are important tools for improving service quality and reducing costs across the entire organization.

Consider the holding company Russian Railways JSC, which owns shares in more than 160 subsidiaries, including foreign companies. The company transformed its shared accounting system, which resulted in substantial improvements in managerial efficiency. Under the reorganized accounting system, the number of days required to consolidate financial reporting decreased by 19% (from 27 to 22 days), and the number of available accounting details increased by 230%.

4. Where does it make sense to outsource?

Objective: Weigh the costs and benefits of outsourcing–what will be done internally and what will be done externally?

Outsourcing has obvious potential benefits, including lower costs. Professional services, such as IT, software development, technical support, and accounting are typical targets for outsourcing. When contemplating the "make or buy" decision, companies should consider long-term productivity and cost projections, physical and data security, long-term business and employment stability and business continuity capability.

Complex holding companies can reap gains in efficiency and improve the focus of their core businesses by strategically outsourcing secondary activities. For example, a large electronics, media and entertainment conglomerate with interests in over 100 countries chose to outsource some of its treasury operations, which provide various services to its affiliate companies, including foreign currency hedging and financial reporting. As a result, the company reduced operational costs by more than 40% year-over-year and improved its regulatory audit results.

In some scenarios, outsourcing comes with increased risk. The Royal Bank of Scotland, a banking and insurance holding company, faced an outsourcing disaster in 2012 when its IT vendor botched a software update, leaving millions of customers unable to access their accounts. The debacle resulted in a £56 million fine by regulators.

WHEN IS IT BETTER TO INVEST VS. DIVEST?

After assessing their business units and product lines, holding companies often wrestle with a tough debate: For certain assets with sub-par performance, is it better to invest or divest? When is it best to dispose of a business that no longer fits into the longer-term model? Perhaps the given business would benefit from a capital injection — or, alternatively, it may be wise to channel divestment proceeds to a different, top-performing business to further bolster its position.

Consider this: A record 87% of companies plan to divest within the next two years, but maybe they should think twice: Almost half of all divestitures fail to realize value for their shareholders.

Lean principles are designed to help holding companies navigate these tricky waters by providing a systematic philosophy and process for reviewing a portfolio of business units. Companies can't properly answer the "invest vs. divest" question unless they are able to establish alignment around strategic priorities and identify ways to improve asset performance and overall portfolio performance — all key deliverables of Lean thinking.

COMMON IMPLEMENTATION PITFALLS

Any company that sets out to implement Lean principles may fall victim to multiple hazards that can steer the initiative toward failure. For holding companies in particular, here are the three most dangerous pitfalls — and how they can be avoided to ensure Lean success.

1. Not fully understanding the principles of Lean: Lean is not just about buzzwords like Six Sigma and Kaizen — it is a philosophy and mindset and, as such, can be challenging for complex businesses to fully undertake without guidance. The key is to identify and engage the right partners who can assess problems and deliver the palpable, quantifiable results of a full Lean transformation.

For diverse multi-national holding companies, it can be particularly challenging to map various value streams without an expert understanding of Lean. For example, a European conglomerate successfully analyzed the value-adding capacity of its manufacturing process—a relatively straightforward endeavor that follows the flow of the product design. In the company's vast research and development (R&D) division, however, value mapping proved more difficult. Testing and modeling consumes most of the R&D project cycle, making it difficult to parse apart value-adding versus non-value adding operations.

The company was able to resolve the uncertainty regarding the wasteful versus value-adding R&D activities by performing complex mapping multiple times under the guidance of an expert team. To overcome the implementation obstacle, the company needed a deep, thorough understanding of value mapping—a surface-level knowledge proved inadequate. As a result, the R&D process was transformed to an efficient, innovative hub of creative excellence (center of excellence) positioned to drive the overall business forward.

2. Seeking a "one and done" solution: One of the biggest mistakes holding companies can make is looking at Lean implementation as a fixed state or goal — making the objective "becoming lean." In reality, the path is never-ending: Lean is a journey, not a short-term target. As such, complacency becomes a major challenge for many organizations.

Consider GlaxoSmithKline (GSK), a massive pharmaceutical and biotechnology company that operates on a global basis, primarily through subsidiary companies. Following the 2001 merger of Glaxo-Wellcome and SmithKline Beecham, GSK's approach to improvement was fragmented and inconsistent across the business units. While elements of Lean principles were present in various parts of the company (and were delivering some results), the principles weren't applied consistently or continually.

In 2009, a newly installed CEO approved an initiative to essentially change how the company approached change. A key tenant of the effort, known as the Accelerated Delivery Program, was a commitment to maintaining standard approaches. The company focused on scaling up from "one-and-done" project-based thinking to embracing a long-term, sustainable and unified framework for continual improvement and business transformation.

Consider also multi-national corporation Whirlpool, which recently applied Lean principles to multiple sites in North American under two distinctly different approaches. In half of the sites, the company adopted a highly focused "blitz" approach that yielded rapid results. The other half adopted a longer-term path focused on continuous improvement. Where the "blitz" sites made short-term gains but lost them as improvement leveled off and eventually stopped, the sites with a longer-term view fostered greater awareness and education that led to superior, sustained results.

As GSK and Whirlpool learned, a structured commitment to continuous improvement is imperative, but this can be hard to achieve: The success rate for continuous improvement endeavors is less than 60%. To keep the Lean transformation moving forward, organizational leaders must align behind a long-term vision — and make sure the vision stays consistently top-of-mind across all levels of the company. While top-down leadership is important, companies with strong continuous improvement success are also able to coordinate and prioritize value stream initiatives that bubble up from front-line employees.

Finally, keeping in close touch with Lean experts and consultants can help carry the momentum forward. In fact, process improvement authority Satya S. Chakravorty said, *"The extended involvement of an improvement expert is required if teams are to remain motivated, continue learning and maintain gains."*

3. Ignoring the importance of cultural change: Lean Management is far more than a toolkit. *"It is a profound change of corporate culture, from the bottom of your organization to the top, that perceives value from the customer's perspective and gears everything you do towards optimizing that value. This cultural change can be an especially tricky for diverse holding companies with numerous business units,"* noted Seif Shieshakly, Co-Founder and Managing Partner of Four Principles. *"Truly implementing Lean introduces a seismic shift in the way work is done and managed."*

All aspects of corporate culture must be considered, including how people are incentivized to behave and the way they think, talk, work and act every day. Academic studies of organizational management have shown that effective implementation hinges on educated leadership that demonstrates a commitment to enthusiastically embrace and sustain Lean change processes. Cultures must be aligned with Lean ideology and driven by a compelling, shared vision, purpose and goals, embraced and made consistently visible throughout the organization.

Take, for example, multi-national conglomerate and diversified holding company General Electric. Former CEO Jack Welch strongly and visibly supported cultural implementation of Lean principles by linking opportunities for promotion and bonuses with quality improvement initiatives, aligning employee incentives with Lean goals. Without this lead-from-the-top cultural commitment, General Electric would likely have generated far less than the $12 billion in savings it realized.

Lean transformations take time and commitment to achieve, especially for compound holding companies — but the results can generate sustainable competitive advantages and substantial benefits in today's increasingly challenging business environment.

When your holding company is ready to apply transformational Lean thinking, Four Principles is here to deliver actionable expertise, not idle talk. We develop sustainable Lean Solutions for companies of all types, including holding companies. We implement. We are passionate about what we do. We are Lean experts. Learn more at https://fourprinciples.com.

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