SPEED TRAPS

MANAGING FAST GROWTH
PART ONE

Every fast-growth company eventually runs into at least one of these all-too-common obstacles. How you handle them can make the difference between success and a high-speed smashup

BY KIMBERLY WEISUL /// ILLUSTRATIONS BY ZOHAR LAZAR

SOME ENTREPRENEURS just don't know how to operate in first gear. That's certainly true of the company builders featured in this issue of *Inc.* The median growth rate of Inc. 500 companies from 2008 to 2011 was 1,435.9 percent. And when you're traveling at that kind of velocity, encountering an obstacle can be downright painful—and, in some cases, even fatal.

What kinds of obstacles do fast-growth companies encounter? Gary Kunkle, an economist and research fellow at the Edward

Lowe Foundation's Institute for Exceptional Growth Companies, has long wondered the same thing. To get deeper inside what makes successful (and unsuccessful) businesses tick, Kunkle has constructed a vast database of some 45 million workplaces. He has collected more than 250 data points on each of those companies and can sort them by more than 400 factors, such as industry, size, and location.

Kunkle recently completed a study of 4,000 fast-growing companies in Pennsylvania. (The survey was sponsored by the Team Pennsylvania Foundation, a nonprofit economic development agency.) He then surveyed 600 of them. He visited their headquarters and held focus groups with their CEOs. It soon became clear that these companies had more in common with one another than they did with industry peers or businesses of the same size. In fact, these growth companies shared the same struggles, regardless of those factors. "These challenges transcend the industry you're in, the location you're in, or the size you are," says Kunkle.

We asked Kunkle to help us identify the challenges that all fast-growing businesses face. They're listed below, along with case studies showing how current Inc. 500 entrepreneurs managed to overcome them. If you plan to join the Inc. 500, you can expect to encounter these traps, too. The secret is not to let them slow you down.

1 YOUR BUSINESS OUTGROWS ITS STAFF

The people who got you to $5 million aren't the ones to get you to $50 million

In 2008, Black Elk Energy closed its first deal, to develop a single gas field in the Gulf of Mexico. And the company's logistics manager did a bang-up job of getting workers out to the drilling platform and back.

About a year later, Black Elk signed its second deal, this time to develop 30 oil and gas fields. Suddenly, the logistics manager had a very different job. Moving people and equipment was the easy part. Now, she had to figure out how to get the most efficient use of the company's helicopters, boats, and other resources.

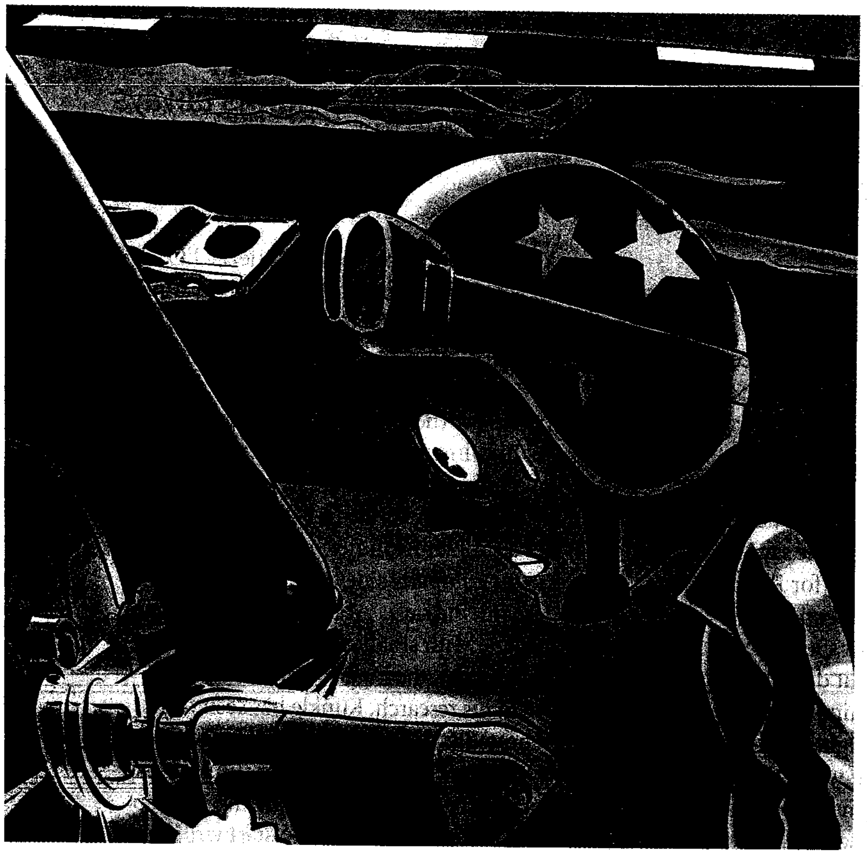
And so it was that Black Elk CEO John Hoffman found what many entrepreneurs have learned: As a business grows and its challenges become more complex, you may need a whole new staff to deal with them.

Black Elk's early staff members were excellent tactically, Hoffman says. But some lacked strong strategic skills. They were doing their jobs, but they weren't measuring what they were doing; as a result, managers lacked the metrics they needed to boost the company's efficiency and productivity.

Yet Hoffman was reluctant to part with his original employees. "It's very easy to say, 'You no longer fit, so you have to go,'" he says. "But that's counter to our culture." Early employees took a big risk in leaving their corporate jobs to come work for a start-up, he says. What's more, there's a major talent war afoot in the oil and gas industry. If Hoffman has good people, he wants to keep them.

So when he has to tell someone that his or her job has outgrown him or her, Hoffman tries to make it a positive experience for both parties. That's not always easy. In most cases, Hoffman says, the employee does not understand the gap in competency. To make his point, Hoffman assigns employees a difficult but not unrealistic assignment. For instance, he asked his logistics manager to figure out how many passenger miles the company's helicopters flew every day. Then he asked how Black Elk might increase its passenger seats per mile.

The logistics manager couldn't answer these questions, which Hoffman says is what made the light bulb go on: "Then you can have a real, honest conversation that isn't personal." In such situations, he takes pains to explain why the company



needs a different type, or level, of expertise. "If you allow them to understand your needs and why it's important, nine times out of 10, they want the company to be successful," he says. He doesn't cut anyone's pay, but he does not hesitate to recruit the talent the company needs. The original employees get someone to learn from and can keep doing the things at which they are best. As Black Elk has grown, he has hired senior people in nearly every department.

Black Elk manages 98 fields and has $340 million in revenue. There are six people in its logistics department, including a senior executive recruited from the giant JX Nippon Oil & Gas Exploration. The original logistics manager is still with the company. Hoffman has had conversations similar to those he had with his logistics manager with about a dozen people in all departments. "We have zero attrition," he says. "So I think we're managing the right way."

NUMBER TWO

YOU WAIT TOO LONG TO HIRE

Demand is surging. Where are the employees to handle it?

It's only natural for new hires to feel some pressure. But at FM Facility Maintenance, which runs facilities for companies with multiple locations, new account managers seemed to be having an extra-tough time adjusting. And the customer experience, CEO Jim Reavey thought, was beginning to suffer.

The problem, Reavey decided, was that he was hiring reactively. The solution: He now brings on account managers about 120 days before he truly needs them. That way, the new employees have plenty of time to absorb FM's culture and shadow an existing account manager before they get started.

According to Kunkle's research, most high-growth companies would benefit from a similar strategy. Still, it isn't easy. Reavey, for instance, tries to coordinate hiring with the deals he has in the sales pipeline, but if sales slow down or a big deal fails to materialize, those people do represent an added investment.

Entrepreneurs often have to hire before they know when the new person will be needed.

One way of addressing this problem, says Kunkle, is to follow what he calls the Chuck Noll approach, named for the acclaimed Pittsburgh Steelers coach. Noll always sought the best overall athletes rather than the best candidates for particular positions, reasoning that a great athlete can be trained to play a variety of positions. This works for entrepreneurs, says Kunkle, because they often have to hire before they know exactly what the new person will be doing or when he or she will be needed. By the time entrepreneurs realize exactly what they need, then start searching for someone to do it, it's often too late.

For Reavey, the best performers come from the military. He uses recruiters who specialize in veterans returning from Iraq and Afghanistan. They are trained in leadership and mentoring. And stress is never much of a problem. "They're great when things don't go their way," Reavey says. "When things get really busy, they don't panic. They keep their teams calm and focused on the customer."

Since 2008, revenue has grown to $350 million from $37 million. Reavey says FM's customers do not appear to have noticed the common backgrounds of many of his recruits. But he gives the new staff members the bulk of the credit for FM's success. After all, he says, "When you're in a pressure situation, it's never as much pressure as bullets getting shot at you."

YOUR BUSINESS LACKS THE RIGHT SYSTEMS

Eventually, gut instincts won't cut it

For OtterBox, a manufacturer of protective cases for hand-held devices, the launch of a new device is a huge opportunity. But in May, when Samsung released its long-awaited Galaxy S III smartphone, OtterBox blew its chance. Though it had long been planning for the Samsung launch, OtterBox had fallen behind and didn't get its cases to retailers until two weeks after the product debuted. Founder Curt Richardson says he forfeited as much as $10 million as a result. "We totally blew it," he says.

OtterBox is on time about 90 percent of the time. But for Richardson, that's not enough, and he has been struggling to upgrade his company's systems for years. That's a big change for OtterBox, where processes often have involved no more than a gut decision by Richardson himself. "I've realized I can't fight this thing the way I fought when the company was small," he says. "If I expect to scale, I need to look at this totally differently."

> ***"When you're growing this fast, the processes you have today will not be working in six months."***

OtterBox's predicament is complicated. It's not just that it needs a more systematic way of designing, manufacturing, and shipping products. It also needs systems it will not outgrow—a problem, given that OtterBox has been growing at a ridiculously fast pace. Four years ago, it had revenue of $10 million; in 2011, sales hit $348 million. "When you're growing this fast, the processes you have today will not be working in six months," says Richardson. "You have to somehow get ahead of it."

In 2009, OtterBox began installing a technology to help automate its distribution and add some clarity to decisions about what needed to be moved where and when. "I've got to be able to determine where my volume is and how full my factories are, so I can determine if I need to put more factories in different spots," says Richardson.

Unfortunately, the new system "was a giant disaster," he says. For one thing, the company that was implementing it was acquired before the project was completed. And once it was finally installed, OtterBox promptly started to outgrow it.

After months of trying to patch things together, Richardson decided to start over. The company's new platform is scheduled to launch in January. And Richardson is confident that sometime in 2013, he will have a much better handle on how busy his factories are, how much product he has, where it is, and where it needs to go. And gaffes such as those that led to the botched Samsung Galaxy S III launch will be a thing of the past.

YOU RUN OUT OF MONEY

Cash flow is always a concern—no matter how much cash you have

You wouldn't think Tony Jimenez, CEO of the IT-services provider MicroTech, would have had to worry about cash flow. Within several months of founding his company in 2004, he had a $500,000 line of credit and a pair of partners with money in the bank.

But Jimenez learned that even the best-prepared businesses are never free from cash-flow concerns. In fact, Jimenez says, it's a problem you never truly outgrow. "Your company's never big enough to buffer you," he says. "At the beginning, you're playing with smaller balls of fire. The bigger you get, the bigger the balls of fire."

In his research, Kunkle has seen this repeatedly. As companies land bigger contracts, they need to put larger sums of cash on the line to buy equipment and staff up long before they are able to start writing invoices. "Companies often actually become less liquid as they grow," says Kunkle. "They grow themselves right into bankruptcy."

That's nearly what happened to Jimenez and MicroTech. Shortly after launching, the company scored a major coup when it landed a gig as a subcontractor to General Dynamics, which had been hired by the Department of Defense to perform a major data migration. Jimenez quickly hired 40 people.

And then the funding was pulled.

Jimenez was faced with firing 30 of his newly hired staff members. Plenty of business owners would have wielded the ax immediately. Instead, Jimenez called everyone he could think of, trying to find jobs for his new people. But in the meantime, he was still paying them, which was killing his cash flow. Says Jimenez, "I was convinced I was going to lose my company. It was a very emotional time for me."

Jimenez has no regrets. But he has learned his lesson. Now, even with a $30 million credit line and $100 million in credit from Dell, Jimenez never stops keeping a watchful eye on his cash.

NUMBER 5 — YOU CAN'T KEEP UP WITH DEMAND

When people want what you're selling, you had better be able to provide it

Chobani, the $634 million yogurt maker, has had capacity issues from the very start. At first, the problem was overcapacity. In 2005, Chobani's founder, Hamdi Ulukaya, bought a 90-year-old yogurt factory in New Berlin, New York, on a vague conviction that, he says, "something is going to happen with yogurt."

The company got its first order, for 300 cases, in 2007. Since then, it has been a constant scramble to keep up. "You get your sales started, and you're very excited," says Ulukaya. "Then you look at your actual capacity, and it's very little." By 2009, Chobani was selling 200,000 cases of yogurt a week. It had the capacity to make 400,000. Ulukaya wanted to expand his facilities to make 1.4 million cases a week. Price tag: $100 million.

This, says Kunkle, "is the most dangerous point for hypergrowth companies. They need to expand and often need to go into debt to do it. If the demand doesn't show up, they end up highly leveraged and at risk of bankruptcy." The best strategy, says Kunkle, is to manage growth so it can be dealt with in small chunks rather than in big ones.

For Ulukaya, that wasn't an option. It would be a year before a new facility would be up and running. "You have to see the demand long before it's coming," says Ulukaya. "You have to invest in time, and hopefully, when you finish it, the orders will come."

Ulukaya started building out his new production lines. He figured that as his business grew, he could use the profits to finance some of the expansion and that the growth would coax the banks to come on board. By 2010, he had enough capacity to produce 1.4 million cases a week. But by then, orders were up to 1.6 million. Ulukaya plans to spend $300 million this year on yet another expansion.

NO. 6 — THE PROBLEM IS YOU

As your company grows, you need to grow with it

Jessica Herrin co-founded her first company, WeddingChannel, at the height of the dot-com boom. She recruited talented, highly motivated people willing to work around the clock. Then, one by one, she watched them burn out.

In 2004, Herrin started the jewelry and accessories designer Stella & Dot. This time, she was determined to build a lasting, global company, and she was pretty sure the frenzied approach of the dot-com era wasn't the way to do it. She knew she would have to take her leadership abilities to another level. So she sought some help. Her first move: to establish a board. She recruited pros from the world of finance and from other beauty and lifestyle companies. They have provided crucial advice about the kinds of people Stella & Dot should hire and have worked their contact lists to help Herrin find them. She has also sought help from peer-mentoring organizations, such as the Young Presidents' Organization.

Smart moves, says Kunkle. Most high-growth entrepreneurs, he has found, lack the experience needed to guide their organizations. He recommends they create advisory boards and meet with them regularly. Peer-networking groups, he adds, can be helpful. But he cautions that peers often are unable to address the deep questions that many entrepreneurs face, such as "Who am I? Who should I be?" Indeed, one of Herrin's advisers helped her understand that her intense drive may have exhausted the people around her. "I didn't have a lot of patience for anyone who couldn't give 110 percent, 110 percent of the time," she says.

Herrin still has a vision, and she is as intense as ever. But she wants a company in which employees can grow into their positions and remain productive for the long haul. She has high expectations for performance but none for face time. Herrin says she finally understands that her way is not right for everyone.

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