



Expanding into adjacent markets is tougher than it looks; three-quarters of the time, the effort fails. Here's how to change those odds dramatically.

Growth Outside the Core

by Chris Zook and James Allen

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Growth Outside the Core

The Idea in Brief

Seventy-five percent of growth initiatives fail. So how do the few firms that generate sustained, profitable growth succeed? They expand their strong, core businesses—in predictable, repeatable ways—into related markets where they can excel.

For example, they may continue to focus on their core products, but sell them in new geographic regions, through new distribution channels, or to new customer segments. Such companies develop—and rigorously apply—a strict **repeatability formula** to these adjacency moves. This formula enables them to change just one variable at a time and execute moves faster.

The payoff? Companies that execute adjacency moves using a repeatable formula grow revenues three times faster than average firms in their industry. Take Nike. By systematically expanding product sales into a series of sports, Nike raced past rival Reebok—growing its profits from \$164 million to \$1.1 billion, while Reebok's shrank from \$309 million to \$247 million in the same timeframe.

The Idea in Practice

RULES FOR ADJACENCY MOVES

The particular adjacency moves you select matter less than how you choose and execute them. You generate the most growth by carrying out your moves according to well-defined rules:

- Never put your core business at risk.
- Make an adjacency move only if you expect to be among the top three players in the new space.
- Pursue one opportunity at a time.
- Change one variable at a time.

► Example:

Initially distributing one product (Nigerian cashews), Olam now handles 12 agricultural commodities and operates in 35 countries. It won a reputation for profitably bringing commodity products out of developing markets—by developing vehicles for hedging price and foreign-currency risks. These vehicles formed the kernel of its repeatability formula.

Impressed, customers asked Olam to handle cashew producers in other, nearby countries. It made this adjacency move first, changing only one variable (geographic area). Next Olam started selling coffee, cocoa, and sesame through its existing infrastructure—again changing one variable (commodity product). Soon it built businesses in hulling, sorting, and processing—and eventually marketing, distribution, and risk management.

BUILD YOUR REPEATABLE FORMULA

Develop your repeatable formula based on insights about customer behavior:

Segment customers.

Use insights about customers' behavior and purchasing decisions to identify potential adjacency moves.

► Example:

Dell's direct-to-customer business model lets it communicate regularly with end users. It uses this information to subdivide and service customers more efficiently. For example, it splits early education into primary and secondary schools, and higher education into colleges and universities. It locks onto high-priority segments and controls its margins with remarkable precision.

Grow share of wallet.

Sell related products to customers whose behavior you know intimately.

► Example:

American Express strengthened its core business by analyzing millions of daily transactions from customers. The data suggested patterns of opportunity; for example, expanding from individual consumers to corporate cardholders. AmEx used these insights to create a family of credit cards with varied interest rates, terms, services, and reward programs.

Mirror customer adjacencies.

Track customers' expansion plans and future needs.

► Example:

STMicroelectronics saw wireless phones take off. Its main customer, Nokia, wanted to load phones with new services without taxing batteries. ST adapted its microprocessor power-management technology to grow with wireless handsets' capabilities. It became Nokia's leading supplier of a one-chip system that drove the entire phone.

Expanding into adjacent markets is tougher than it looks; three-quarters of the time, the effort fails. Here's how to change those odds dramatically.

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Golf ranks as one of the most brutal and demanding markets in the sports business. So, despite its fabled swoosh, Nike was regarded as an amateur when it decided in 1995 to branch out from shoes to golf apparel, balls, and equipment. Four years later, however, Nike had scored priceless marketing victories—not once, but three times running. First, the British Open champ wore Nike's golf shoes in 1999. Next, Tiger Woods switched from Titleist golf balls, the leading brand, to Nike golf balls in 2000. And, finally, David Duval won his first major tournament just after switching to Nike golf clubs in 2001.

Nike's entry into the golf market appeared to be the business equivalent of sinking three successive holes in one. But those who had followed the company closely over the previous decade were not surprised. They recognized the formula that Nike has applied and adapted successfully in a series of entries into sports markets—from jogging to volleyball to tennis to basketball to soccer. Nike begins by establishing a leading position in athletic shoes in

the target market. Next, Nike launches a clothing line endorsed by the sport's top athletes—like Tiger Woods, whose \$100 million deal in 1996 gave Nike the visibility it needed to get traction in golf apparel and accessories. Expanding into new categories allows the company to forge new distribution channels and lock in suppliers. Then it starts to feed higher-margin equipment into the market—irons first, in the case of golf clubs, and subsequently drivers. In the final step, Nike moves beyond the U.S. market to global distribution.

This formula, we would argue, is the reason that Nike pulled away from Reebok as leader in the sporting goods industry. In 1987, Nike's operating profits were \$164 million to Reebok's \$309 million, and Nike's market valuation was half the size of Reebok's. By 2002, Nike had grown its profits to \$1.1 billion, while Reebok's had declined to \$247 million. Both companies had started out in the same business with the same manufacturing technology and comparable brand names. Yet Nike found a formula for growth that it used successfully again and

again, while Reebok seemed to pursue a different source of growth every year with uneven results.

To learn more about how to sustain profitable growth, we recently conducted a five-year study of corporate growth involving 1,850 companies. We tracked specific growth moves and linked them back to individual company performance. Our research yielded two major conclusions. One was that most sustained, profitable growth comes when a company pushes out the boundaries of its core business into an adjacent space. We identified six types of adjacencies, ranging from adjacent links in the value chain to adjacent customers to adjacent geographies. (For the complete list, see the exhibit “Six Ways to Grow into an Adjacent Space.”)

Our second finding was that companies like Nike consistently, profitably outgrow their rivals by developing a formula for expanding those boundaries in predictable, repeatable ways. The average company succeeds only 25% of the time in launching new initiatives. Companies that have hit upon a repeatable formula have success rates of twice that, and some drive their rates up to 80% or higher. That’s because growing a business is normally a complex, experimental, and somewhat chaotic process. Repeatability allows the company to systematize the growth and, by doing so, take advantage of learning-curve effects.

Companies that master repeatability work within any number of adjacencies. Some companies make repeated geographic moves, as Vodafone has done in expanding from one geographic market to another over the past 13 years, building revenues from \$1 billion in 1990 to \$48 billion in 2003. Others apply a superior business model to new segments. Dell, for example, has repeatedly adapted its direct-to-customer model to new customer segments and new product categories. In other cases, companies develop hybrid approaches. Nike, as noted above, executed a series of different types of adjacency moves. It expanded into adjacent customer segments, introduced new products, developed new distribution channels, and then moved into adjacent geographic markets. The first time Nike did this, it undoubtedly struggled with the inherent complexity of making so many moves, but as it repeated the process again and again, managers learned to execute consistently.

The successful repeaters in our study had two common characteristics. First, they were extraordinarily disciplined, applying rigorous screens before they made an adjacency move. This discipline paid off in the form of learning-curve benefits, increased speed, and lower complexity. And second, in almost all cases, they developed their repeatable formulas by studying their customers and their customers’ economics very, very carefully. These capabilities may seem basic and unglamorous, yet companies that excel at them set the stage for industry-leading growth.

The Discipline Needed

We focused our study on 25 companies that achieved sustainable growth performance far in excess of their peer groups. This diverse set of companies ranged from retailers like Pet-Smart to banks like Lloyds to consumer electronics companies like Legend. Typically, these companies grew revenues three times faster than did the average company in their respective industries. Collectively, their revenues rose from \$107 billion to \$276 billion in the last ten years, while earnings increased from \$7 billion to \$23 billion during that period. Together, they created more than half a trillion dollars of shareholder value that has largely persisted despite the market collapse of recent years. On average, they returned 22% annually to shareholders. The majority of these standouts have one or two powerful, repeatable formulas that generate successive waves of new growth, allowing them to push beyond the boundaries of their core businesses.

Typically these formulas are applied by CEOs who approach growth strategy with a strong sense of discipline and restraint. Many of them have well-defined rules about which opportunities to pursue. We heard over and over in interviews, “Never put the core business at risk.” These executives also wouldn’t make a move unless they had a good shot at being one of the top three players in a new space. And although they constantly scanned for opportunities, they pursued only one at a time. Says Peter Burt, the former deputy chairman of UK-based financial services leader HBOS, “The most important screen for new adjacencies is to limit the number of new variables we are managing to a small number: one.”

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James Allen is a Bain director in London and cohead of Bain’s global strategy practice. This article builds on ideas in Zook’s forthcoming book, *Beyond the Core* (Harvard Business School Press, 2004).

To get a sense of how effective this disciplined approach can be, consider the story of Olam, a Nigeria-based start-up that went from distributing one product in one country to building a \$1.9 billion multinational business in only 13 years. Today, Olam supplies cocoa, coffee, cashews, sesame, and other food commodities to global packaged food companies including Kraft, General Foods, Sara Lee, and Nestlé. The company's activities have expanded to the point where it now manages the complete supply chain for agricultural raw materials in some of the most challenging markets in the world, including Ivory Coast, Gabon, and Uzbekistan.

Olam was launched in 1989 as an intermediary between local Nigerian producers of cashews and shea nuts, an ingredient in chocolate, and big food processors like Mars and Planters. Large customers had previously been dealing with an array of poorly capitalized local exporters, who would sell forward contracts for commodities and simply default if the price

turned unfavorable at delivery time. Olam created its own vehicles for hedging commodity price risks and foreign currency risks in currencies where there are no forward-exchange markets, offering a better security proposition to customers. Solving this problem created a competitive advantage for Olam that became the kernel of its repeatable formula.

The young company quickly became a reliable source of Nigerian cashews, establishing a strong presence in its core market. Olam's CEO, Sunny Verghese, insisted that each of his executives spend a lengthy term living in the supply areas to absorb the details of bringing commodity products out of unruly, developing markets safely and profitably. Verghese himself lived in rural Nigeria for three and a half years.

Customers, recognizing Olam's growing expertise in distribution in developing markets, began asking the company to handle cashew producers in Burkina Faso, Ivory Coast, Ghana, and Cameroon. Olam was able to make this adjacency move with little risk: It was simply changing a single variable—geography—but continuing to sell the same product to the same customers using the same formula. Not long after the geographical expansion was under way, customers wanted Olam to move other commodities—coffee, cocoa, sesame, and shea nuts—through its infrastructure of buyers, quality laboratories, and warehouses. Again, these adjacency moves varied a single step—the commodity product—but did not change customers, supply chain, geography, or channels. Verghese is convinced that Olam's success in these moves stemmed from its ability to change a single variable at a time—a management feat that requires an exquisite degree of control.

As Olam repeated the process with new products and new markets, other growth opportunities emerged. The company, once a middleman, now controls most of the supply chain for existing products in the countries where it operates. From its core business of trading in raw cashews, for instance, the company moved into shelling and blanching cashews. Similarly, its strength as a trader of cocoa, coffee, cotton, and sesame enabled the company to build businesses in hulling, sorting, and processing those crops as well. From its strong position in sourcing and processing, Olam moved into even higher-value adjacencies, including marketing, distribution, and risk

Six Ways to Grow into an Adjacent Space

In our recent study of the drivers of profitable, sustainable corporate growth, we analyzed 181 adjacency moves that took place between 1995 and 1997 (recent enough to have data but before the Internet era of more reckless investing). We excluded growth through diversification, which leads a company far away from its core business. We also excluded inside-core growth moves, like accelerating innovation in R&D, investing in corporate ventures, and stepping up the company's metabolism by, say, speeding up operations or hiring more salespeople. What we found were six types of adjacencies that successful companies used to outperform their competitors.

Expand along the value chain. This is one of the most difficult adjacency moves.

De Beers extended its diamond business from wholesaling into retailing.

Grow new products and services.

IBM moved into global services, which now constitutes 50% of the company's revenue and pretax profits.

Use new distribution channels.

EAS, a leading sports supplement company, made minor changes in formulation, packaging, and celebrity sponsorship of its Myoplex sports bar and moved from a niche position in specialty nutrition stores to become the leader in its category, selling to Wal-Mart.

Enter new geographies.

Vodafone expanded from the UK to Europe, the United States, Germany, and Japan.

Address new customer segments, often by modifying a proven product or technology.

Charles Schwab expanded its advisory services for discount brokerage customers to target high-net-worth individuals.

Move into the "white space" with a new business built around a strong capability. This is the rarest and most difficult adjacency move to pull off.

American Airlines created the Sabre reservation system, a spin-off now worth more than the airline itself. Sabre, in turn, went on to create a new business adjacency of its own in the online travel agent Travelocity.

Olam's repeatable adjacency formula "makes it pretty clear where our next \$1 billion will come from."

management. Olam now operates in 35 countries and handles 12 agricultural commodities.

Not all of Olam's moves worked out. When the company entered the black pepper and rubber markets, for example, both commodities seemed promising. But Olam quickly realized that differences in industry regulations and trading norms across Africa and Asia would make it difficult and expensive for the company to expand beyond one key producing country—Nigeria in the case of rubber and India for black pepper. So Olam exited the markets. These experiences helped tighten Olam's investment criteria for making adjacency moves. When evaluating a new opportunity, the management team whittles each potential move down to its essence and ensures that it meet three defining criteria. First, the team asks, will the opportunity allow Olam to function as supply chain manager, not simply as intermediary? Second, will the company be dealing in agricultural raw materials—the products it knows best? Third, will it be operating on the ground in emerging markets—the terrain it understands well?

Even with those questions answered, Olam still isn't ready to move. The company applies additional screens to assess whether it should repeat its formula in an adjacent market. The company must have a good shot at being in the top three in terms of global market share in that product, and it must have a physical presence in all the key processing countries. The adjacency move must also provide clear opportunities to expand into higher-value processing. And each new product must have strong end-market customers—big players willing to enter long-term contracts.

These rules give Verghese and his team the game plan for repeating adjacency moves. But the discipline required to apply the formula successfully can't be overemphasized. Now based in Singapore, Olam is the leading global supplier of cashews and shea nuts, the original core business, and ranks among the top six suppliers worldwide in its other key products. Olam has relied on organic growth to expand at a pace that far outstrips the industry average of 2%. From 1997 to 2003, the company grew revenues at 84% and earnings at 28%, with a return on capital of 35%. While most producers of agricultural raw materials plod along, Verghese says Olam's repeatable adjacency formula "makes it pretty clear where our next \$1 billion

will come from."

The Benefits Gained

Olam and Nike have little in common. Yet both companies have been extremely disciplined at finding one formula for incremental growth and repeating it over and over again. That repetition appears to create real, interconnected strategic benefits, each of which contributes to competitive advantage.

Learning-Curve Effects. A repeatable model allows managers to refine skills and systematize processes that are developed mostly through guesswork the first time. GE Capital, for example, built expertise in evaluating and executing deals on its way to becoming a serial acquirer. A Bain study of 1,700 acquirers found that companies doing more than three relatively small deals per year achieved 25% higher returns than companies doing fewer, but larger, acquisitions. One reason: better organizational capability gained through experience.

Reduced Complexity. When we asked A.G. Lafley, the CEO of Procter & Gamble, how the consumer goods company had managed to consistently outperform its industry, he talked about the importance of managing complexity. "Complexity is the bane of a large organization," Lafley said. "It strangles growth." When P&G's legendary Crest brand was flagging in the late 1990s, the company sparked a growth revival by expanding into two large adjacencies—teeth whitening and brushing. Two innovative products led the charge—Crest Whitestrips and the SpinBrush. Using the same Crest brand, the same P&G marketing infrastructure, and the same channels to reach the same set of customers, P&G quickly launched the two adjacent products—adding more than \$200 million of new sales apiece in one year. By holding other variables constant and changing one thing at a time, P&G dramatically reduces complexity, which allows it, in turn, to make adjacency moves one after the other without straining the system.

Speed. When a company has mastered a repeatable formula for adjacency moves, it can successfully start—and finish—a number of moves faster than a competitor would. Vodafone, for example, is able to collect high-potential properties in wireless communications, thanks to a rigorous formula for evaluating and acquiring regional cellular phone service companies. A well-honed process for

rapidly teasing out key criteria, mapping market boundaries, and calculating the profit potential of future add-on services enabled Vodafone to snap up the number one or number two wireless players in quick succession in markets across Europe, North America, and parts of Asia, while competitors gave chase.

Strategic Clarity. A surprising number of chief executives fail to communicate a clear growth strategy to the investment community—and they pay a high price. Compaq failed to convince investors that its superscale growth rationale could work, whereas Dell's direct model resonated with investors. Employee loyalty also hinges on understanding and believing in the company's strategy for the future, according to a recent Bain survey. Companies savvy enough to identify and execute a repeatable formula for growth have the advantage of strategic clarity: Repeatable formulas are compelling, and they are easy to understand.

Even when competitors work in the same geographic markets, seek the same customers, and are affiliated with the same channels, the company with a repeatable formula will typically grow faster and more profitably than its rivals. To see this principle in action, let's return to Nike and compare its growth path with Reebok's. The handicap for Reebok was its undisciplined approach to growth. Reebok veered from one adjacency to the next without a clear plan. The company sought to position itself as a sports and performance company,

not a fashion and fitness company, for example—but undercut that approach with such brand additions as Ralph Lauren and Polo footwear. Unrelated investments like the acquisition of the Boston Whaler boat company also sapped Reebok at the same time that its core shoe business was under severe attack.

Nike, meanwhile, was refining its repeatable formula. The company had been selling shoes for 22 years when it broke into basketball with Michael Jordan's 1985 endorsement, followed by its entry into tennis in 1986 with John McEnroe as its brand star. Throughout the 1990s, the company picked up speed as it moved into baseball, football, cycling, volleyball, hiking, soccer, and then golf. Shoes drove the business, but increasingly Nike replicated its success with adjacency moves into apparel and hard goods. The star power of its endorsers made international expansion a logical next step. Having started out neck and neck with Reebok, Nike ended up increasing its global market share from 22% in 1990 to 38% in 2002, four times the share of its nearest competitor.

What's in this story for the typical company? First, repeatability doesn't happen overnight. Nike took a while to find its repeatable pattern. Second, a repeatable formula for adjacency expansion is practically imitation proof. Nike's formula helped it pull away from competitors that were watching its success but unable to match it. Indeed, Nike's ability to replicate success was a siren song that lured competitors to Nike's own game, where their

The New Math of Profitable Growth

A company that develops a method for repeatable adjacency moves has many advantages in terms of speed and transparency, organizational efficiency, mastery of hidden detail, and reduced complexity. The result is often a breakthrough in performance; executives make relatively modest adjustments and improvements that drive significant increases in growth and valuation. One might call it the new math of profitable growth.

Consider a simulated scenario of a company in a 3% growth market. Let's see what the company would be worth if it achieved just half of the average benefits captured by the most successful repeaters in our study.

Using its repeatability formula, the firm:

- cuts 30% off the time it takes to realize the growth benefits from its adjacency moves;
- handles three instead of two adjacency initiatives per year because of its superior organizational knowledge; and
- boosts its success rate from 30% to 55% because it reaps learning-curve benefits from its repeatable formula.

That firm can grow revenue much faster—by 6.4% per year as opposed to 3.9% (the average performance in a 3% growth market). Compounded over five years at a constant margin and price-to-earnings ratio, this

higher growth rate leads to a 50% improvement in value creation over competitors by the end of the period. If the higher growth rate leads also to a much higher P/E, as is likely, the increase in value creation could be much larger.

Companies that make such substantial improvements in the timing, quantity, and success rate of their adjacency moves see the benefits magnified by stock market valuations. Clearly, disproportionate advantage accrues from successful, repeatable growth versus moderately successful, "hunt and peck" growth, allowing companies to significantly distance themselves from their competitors.

efforts foundered. Reebok's efforts to duplicate Nike's "Air Jordan" halo, for instance, led to the "Shaq Attack" sneaker. But copying one move in Nike's pattern gave Reebok little traction, and by the time Reebok figured out Nike's game, Nike had pulled too far ahead to catch. Finally, repeatability is about strategic focus. Nike accomplished its expansion without displacing its core athletic shoe business. Indeed, the company increased the strength of the original business, then drove that market power into new adjacencies just a step or two away from the core.

By definition, however, there is always an adjacency too far removed for successful repeaters. As companies get better at rapid adjacency expansion, opportunities proliferate. Along with the confidence to follow customers aggressively into new adjacencies, companies need to develop the confidence to say no when the organization is stretched. Golf clubs, for instance, may turn out to be one step too far for Nike at this stage. Tiger Woods seems to think so. Woods's recent decision to swap Nike clubs for an older set as he tried to regain his winning form suggests that Nike still has work to do in expanding the business to include golf clubs.

Indeed, every successful repeater we examined in our study has entered adjacencies that didn't pan out—Lloyds pulled back from California's big financial services market, Staples withdrew from selling insurance products, Olam, as we've seen, exited from black pepper and rubber. In each instance, the companies have used their setbacks to become more closely acquainted with the tastes and habits of their customers and the companies' own limitations.

The Sources of Repeatability

Of course, failed experiments aren't the only way to figure out what works. In our interviews with CEOs, we heard strikingly similar observations about the process for developing a repeatable formula for adjacency expansion. Nearly 80% of the successful adjacency formulas we studied were built around insights about customer behavior. It's a logical connection for companies to make: The more attuned a company is to its customers' preferences the more readily it can spot untapped opportunities.

Segmenting Customers. For many companies, the foundation for a repeatable formula is

effective customer segmentation. This may come as a surprise, particularly among CEOs who have grown disillusioned with conventional techniques used to group customers into logical clusters. Over the last ten years, segmentation has come to be seen by some senior executives as the domain of marketers and ad agencies—useful for marketing campaigns but not as a lever of growth strategy. The rap against segmentation is that it's not practical enough to use for allocating resources, particularly when delineations among customers are based too heavily on lifestyles and psychological motivations.

Structured properly, however, with pragmatic segments that illuminate how customer behavior leads to purchasing decisions, customer segmentation becomes a seedbed of repeatable adjacency moves. Companies can develop a more thorough understanding of customer needs. Perhaps even more valuable is the framework such analysis provides for making very large-scale investment decisions to pursue new adjacencies. Identifying the lifetime value of each segment, and determining a company's market share within each, allows the management team to rank the attractiveness of new adjacency opportunities. The same tools help spot patterns of success, reinforcing repeatable formulas when they emerge.

Dell, for instance, has used this approach to enter one adjacency after another. With its direct-to-customer model, Dell communicates with end user customers regularly and feeds that information into deep and detailed segments. Dell then subdivides existing customer segments, making slight adjustments to its direct model to tap sources of new growth. Dell first split its public sector activities into education and government, for example; then it segmented education by primary and secondary schools; higher education was further divided into colleges and universities. For each segment, Dell changed its product focus, rewired its salesforce training, and—most important—modified its salesforce cost structure. This approach enables Dell to lock on to high priority segments and control its margins with remarkable precision. As a result, the company has developed a strategy where competitive advantage is based not on volume alone, but on knowledge of its customers and ability to serve them efficiently.

Growing Share of Wallet. Selling related

products to customers you know intimately—in other words, growing share of wallet—is another highly successful expansion strategy, according to our study. Yet plenty of firms get it wrong—Saatchi & Saatchi in consulting, Sears in financial services, and Allegis in travel, to name a few. Success depends on understanding your customers' behavior and following familiar pathways to build the new business.

Over the last 14 years, American Express has exemplified the power of a repeatable formula based on selling related products to customers it knows. In the 1970s, the switch from checks to “plastic” was in full swing, propelling the growth of AmEx's basic green and gold cards. As market momentum slowed in the 1980s, the management team decided to assemble a “financial supermarket” of products around the core credit card business. The strategy spawned a series of acquisitions—seven in six years—starting with brokerage firm Shearson Loeb Rhodes in 1981 and concluding with E.F. Hutton in 1987. The company grew dramatically in size, but profitability suffered and the stock price dropped by more than 50% from 1987 to 1991, when top management was replaced.

The new team quickly divested all but one of the acquired businesses and then set about strengthening the original core business of charge cards. They started by analyzing the detailed microeconomic buying behavior reflected in the millions of transactions that poured in each day. The data contained patterns of opportunity—expanding from individual consumers to corporate cardholders, for instance, or from a focus on business-travel to retail and everyday spending. From a couple of cards with no add-on services, AmEx managers created a family of cards with varied interest rates, terms, services, and reward programs. In the process, they uncovered four repeatable formulas: finding new customer segments; creating new, more precisely targeted charge- and credit-card products, including popular reward programs; expanding the types of merchants where cardholders can use their cards; and selling additional services to existing card customers.

Each time AmEx considers a new product, teams first scrutinize market data to see if existing buying behavior supports the move. “We're often serving the same customers,” says Alfred E. Kelly, Jr., group president of consumer and small business services. “They just might be in

different segments depending on whether they are at work, on vacation, or shopping on the weekend.”

Mirroring Customer Adjacencies. Other companies uncover opportunities by tracking their customers' expansion plans and anticipating their needs.

In the mid-1990s, for example, STMicroelectronics' search for new opportunities led the European microprocessor company to map out key customer segments where it could become number one in the world. Wireless phones were just beginning to take off, and handset manufacturers, including ST's customer Nokia, wanted to load their phones with new services and features without taxing the batteries. ST saw an adjacency opportunity: Its leading technology in power management for microprocessors could be adapted to grow with the capabilities of wireless handsets. Today, ST is Nokia's leading supplier of a one-chip system capable of driving the entire phone. Building on that success, ST has gone on to supply the system to wireless handset manufacturers in the United States and Asia. Similarly, when ST's customers in the computer industry began expanding into disk drives, printers, and monitors, the company saw an opportunity to grow with its customers in a market largely ignored by its rival, Intel. ST invested to adapt its logic chips, and today is the world's leading supplier to computer peripheral companies.

ST's growth pattern has been to adapt a core technology prompted by insights from its dozen largest customers, apply the technology to new segments, expand into new geographies, then start the cycle again. The formula has proven highly resilient in a volatile industry. CEO Pasquale Pistorio stays in close contact with key account managers at ST's largest customers, often joining them on visits to their own customers. More than 95% of ST's R&D budget goes to developing new capabilities for existing customers, rather than making bets on future technologies that look generally promising.

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The STMicroelectronics story illustrates the two key principles of repeatability. First, adjacency expansion succeeds only when built around strong core businesses that have potential for leadership economics. Second, the best place to look for adjacency opportunities is inside a company's strongest customers.

Nike's ability to replicate success was a siren song that lured competitors to Nike's own game, where their efforts foundered.

Repeatability is just one formula for profitably outstripping the average growth rate in your sector. There are others: Investing in faster product innovation or cornering market power, to name a couple. But focused companies with a strong core that hit upon a formula for repeatedly expanding their strengths to new arenas have it made for the long term. Such repeatability becomes a source of growth

and value year after year. The formula for repeatability is already lodged in your experience—you just need to look for it.

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Growth Outside the Core

Further Reading

ARTICLE

[Leveraged Growth: Expanding Sales Without Sacrificing Profits](#)

by John Hagel III
Harvard Business Review
October 2002
Product no. 2012

Hagel describes one type of repeatable formula for adjacency moves that he calls **leveraged growth**. Unlike traditional growth strategies requiring up-front investment in new assets, this formula entails leveraging *other* companies' assets at many levels of your industry's value chain. You orchestrate a network of firms possessing specialized capabilities and use whichever companies best suit the task at hand. As the network coordinator, you manage connections between participants, not daily activities within them. The payoff? You break into new markets quickly. And by using other companies' assets, you boost your own profits with much less risk.

For example, Hong Kong-based trading company Li & Fung expanded into value-chain and customer adjacencies to double its revenues to \$3.2 billion in five years—without owning any of the facilities that produce the finished goods it supplies to garment retailers and designers.

BOOKS

[Profit from the Core: Growth Strategy in an Era of Turbulence](#)

by Chris Zook and James Allen
Harvard Business School Press
February 2001
Product no. 2301

In this book, Zook and Allen establish the foundation for their thinking about adjacency moves. Sustained-growth companies, they maintain, are built on one or two strong or dominant cores—not on diversification. To sustain profitable growth, firms must correctly assess their core strengths and seek growth in the right places. Abandoning your

core in search of hot new growth not only erodes your once-strong business; it also incurs direct costs when growth initiatives fail.

Using a broad selection of real-world stories, the authors explain how to define your company's sources of competitive advantage, the economic boundaries of your core, and where you could or should compete effectively.

[Beyond the Core: Expand Your Market Without Abandoning Your Roots](#)

by Chris Zook
Harvard Business School Press
January 2004
Product no. 9519

Beyond the Core picks up where *Profit from the Core* leaves off. Zook focuses on how to expand your core business into adjacent areas in ways that generate profits and enable you to expand and defend your core business. If *Profit from the Core* asked "Who am I?" *Beyond the Core* raises the even more challenging questions of "Where should I go? What should I be? How do I get there?"

The author explains how to select and execute adjacency moves and describes the most lasting adjacency strategies. He offers observations on when adjacencies make the most sense and when they're a last resort. And he describes organizational enablers and inhibitors to the success of adjacency initiatives.

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