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PARAGON Perspective

From the President

PARAGON Perspective is sponsored by PARAGON Development, an international consulting organization specializing in new value creation for corporations. This is accomplished through new business development and optimized planning in addition to corporate venturing. The purpose of this newsletter is to update, educate, stimulate, and enlighten our friends and business colleagues on many topics involving new business development as well as the world at large as they may affect our businesses and/or our professional interests. We are not intending, and will not use this communication to promote our business.

We hope to inspire debate and pass along information that may enable all of us to better understand and succeed in our new business objectives in the future. We further hope you pass these along to colleagues who may have mutual interests.

We want to use this forum to do the following:

- Share information we have learned that we consider important concerning best practices, trends, successes and failures, conferences, and other elements that will enable all of you to grow your organizations with maximum top and bottom line results.
- Share information about select client initiatives that may be of interest based on technologies, markets, or business needs that you believe could fit within the scope of those client's interests.
- Share opinions.
- Share personal observations and even humorous items given to us by others.

We welcome your comments on any topic and we encourage you to contribute to future newsletters.

This month's newsletter will highlight our opinion on: "**The acquisition environment; changes in strategy".** Also in this edition is a piece about innovation contributed by Russ Koch, a Vice President of PARAGON and a key member of our management.

Jack Peregrim
Pres., PARAGON Development

Paragon Update

New client projects are starting to expand, with the nature of these assignments being very broad. These projects range from the identification of new, exploratory technologies with value in the distant future to very short term oriented projects designed to determine commercial value in assets that will add top line value before the end of the year. We sense that companies have finally committed to growth and are investing in their future with budgeted initiatives.

In March we took part in teaching a course in "The Basics of Commercial Development" in support of the CDMA-EF. (Commercial Development & Marketing Association; Educational Foundation.) This was a very valuable course for individuals and organizations committed to excellence in creating new value via internal development. The course will be offered at least once per year to the public but may also be offered to specific companies who could sponsor a critical mass of people as students. The course is 2 days and anyone interested can contact us for more information.

Perspectives on Innovation
Russ Koch

Two key aspects of innovation that we have found are summed up by quotes taken from the article "Customer Intimacy and Empathy are Keys to Innovation", by Jim Clemmer. The first key is that practical, implemented innovation is driven more by strategic fit than by creativity, and the second is that innovation results are to a large extent determined by the "people involved" over the process.

"Innovation is a hands-on issue. It calls for an intimate understanding of our current customers and markets, potential new customers or markets, team and organization competencies and improvement opportunities, vision, values, and mission. We can't develop that intimacy from a distance. Studies, reports, surveys, graphs and measurements wouldn't do it.

Effective innovation depends on disciplined management systems and processes. But it starts with people. People searching for creative ways to do things better, different, or more effectively. People trying to understand how other people use, or could use, the products or services their organization could produce. That makes innovation a leadership issue."

Acquisitions: A Change in Strategy

Case Example:

Our task was to help a client identify new platforms for investment, with a starting point of looking strictly at internal investment as the preferred implementation vehicle. Their reasons were:

- The Company had little success in making recent acquisitions because for the last 6 years they were involved in so many M&As that most candidates that would be attractive were no longer available and those left were either too expensive or had '"too many warts".
- The Company had exhausted acquisitions that represented obvious extension platforms that fit their past view of strategic intent.

We started our work by establishing new criteria that would allow a fresh look at potential opportunities and allow the organization to look at strategic fit in a new way. A comment on the first day by an Executive Vice President was very telling: "We have made the decision to stay within a very narrowly defined 'strategic box' because of the risk of failure and the lack of enthusiasm from investors and stakeholders. But, this has been our strategy for the past 3 years and an irony has become evident. We are always staying with this course but the world is changing around us." He agreed that it was somewhat analogous to having a core competency in "buggy whips".

It was also evident that the company looked at acquisitions (beyond "bolt on" investments) as being too risky if they did not have "all the pieces". E.g. the best technology, a strong marketing organization, strong infrastructure, and a large base of existing, protected business.

The company felt that the only avenue left would be to invest in new areas and undertake all of the development themselves. As we proceeded in the front end identification of options, each opportunity viewed offered more risk by going it alone than with external investment.

The result of this project exemplifies the changes in strategy in growth platforms well beyond this single case. The change in our focus with this client involved many steps but 4 were key:

1. Determining if the strategic fit also fit external developments and trends. If not, it is best to change yourself before changes are forced upon you by factors outside your control. Thus, an expanded view and “stretched parameters” were allowed.
2. Once a platform was quantified as attractive, the next step was to look at obvious acquisitions that “brought all the pieces” and were positioned **today** for sustainable contribution.
3. If there were no such candidates attainable, then a Staging Strategy was the next most attractive vehicle. We will expand on that below.
4. Only if the above fail do we consider internal investment as preferred to develop new platforms.

The key new component was the staging strategy. Though more complex and involved than other ways, it may actually serve to lower risk and create much greater value over time. The basic components are:

- Quantify the opportunity so critical success factors are well known.
- Look at those success factors as pieces in a puzzle and determine the optimal way to combine them.
- Work each piece individually.
- Do a risk and financial assessment of each investment.
- Have a clear strategy about the end point but be flexible about the tactics.

Results may look like the following:
You target Market ”A”, a different segment of another market that you are presently serving. You determine that Product “B” is going to be a strong growth product in both the near and long term. The business model and means of capturing and protecting this business are closely aligned with what the company does in other businesses.

The most important success factor is access to customers who are the most critical in this market. Regardless of the offering, these customers will not substantially buy from suppliers who do not have credentials or a “track record” with them. Your first step is to acquire a company serving that market today with sales categorized as being higher than their product value would indicate. Thus, you have a starting point with the best credentials and marketing. This also has strategic value beyond the existing critical mass acquired. You typically won’t have to “over pay” for a product and assets that are not the best in class.

The next step is to acquire or gain access to (license, partner, etc.) Product “B” that will be the means of adding bottom line contribution even though the real key may be the customer intimacy.

A last step may be the acquisition of a capability that will improve Product “B” to ensure sustainable competitive advantage with the volumes and margins that will optimize returns.

We have found that most organizations give up after Step 2, or skip to Step 4. However, we have seen a growth trend in those companies that recognize the advantages of Step 3.

- It lowers risk because you can stop after the first investment and it typically doesn’t involve an aggressive bidding environment.
- It requires a smaller first acquisition which won’t be dilutive and will actually create the cash used for subsequent investments.
- It may be the only option available other than continued investment in existing areas without commensurate potential for contribution.

A few keys to success, as well as difficulties, in developing a staging strategy are:

- Staffing. A staging strategy is a more complex approach and requires experienced management that is often in short supply.
- Organizational commitment that doesn’t judge each puzzle piece as an independent investment.
- Organizational flexibility with new options becoming known with each piece added. It also requires flexibility up front by making the first acquisition one that may not bring the key component that fits the existing business model. (Bringing an old product to a new market instead of making an investment in superior technology).

In Summary:
If you have exhausted what you believe are your acquisition options, it may be time to consider new approaches in strategy. In other words, if the "low hanging fruit" isn't available, it may be time to get a ladder and work your way up to where the best fruit may be.

Scenario Planning—An exercise

When looking at trends and/or external factors that considerable investment may be based upon the following parable is worth remembering:

A battleship traveled with a flotilla of other crafts, such as destroyers, cruisers, supply ships, etc. There could be dozens in the fleet spread out around the battleship.

One night, with the lights from the other ships visible for miles around the battleship, a new light appeared directly ahead. A seaman reported this to the Captain who gave instructions to send a message to the craft ahead to change course. The response was that the battleship should change its course.

The captain told the seaman to send another message and to use his name (Admiral Certainty) and that they are ordered to change their own course. The reply came from Seaman Third Class Confused still telling the battleship that it would have to make the course change.

The captain then instructed the seaman to send one <u>final</u> message that they were a BATTLESHIP and the other craft would have to change its course.

The final message came back and said: "But with all due respect, we are a <u>lighthouse!"</u>

This is a great way to challenge and question data and information upon which investments are made. Ask yourself to generate as many "lighthouses" that you can which represent potential mistaken assumptions or new interpretations of data that appears clear.

Quotes of the Month

"If you can stay calm while all around you are in chaos, then you probably haven't completely understood the essence of the problem". *Source unknown*

"You cannot discover new lands, without the courage to lose sight of the shore." *Source unknown*

"Do not go where the path may lead, go instead where there is no path and leave a trail". *Ralph Waldo Emerson*

Business Factoid

"Moore's Law" revisited

Gordon Moore (Intel co-founder) predicted some 30 years ago that every dollar will buy double the amount of processing power every 18 months, and that the number of transistors on a chip would grow exponentially. "Moore's Law" has held true, though the sustainability has been put into question many times, new developments always seem to make the prediction prove correct.

Hewlett Packard announced in September of last year that they have created a computer memory chip using new molecular technology that takes miniaturization further than ever before. Using previously patented technology (nano-imprint technology); H-P scientists have designed a 64-bit memory unit that is smaller than a square micron. The memory contains 10 times more bits per square than today's most advanced DRAM computer chip memory devices. The chips need to be smaller to be cheaper, faster, and more energy efficient. The H-P technology, partly developed in conjunction with UCLA will move chip miniaturization even faster than Moore's Law would predict. The H-P work also combined for the first time both the memory and logic by manipulating molecules caught in a grid of super thin platinum and titanium wires.

The lesson for all of us is twofold. First that the impossible may be possible to those that set their sights on achieving it and believe they will. Secondly, technology other than your own may be moving at speeds that can create competitive advantage if you understand and plan to use it.

We hope you learned something from this and/or stimulated an action that leads to new opportunities for you and your organizations.

A final thought: We hope that all of our readers take a moment and dedicate thoughts and prayers for those who are involved in the war with Iraq. This includes members of our Armed Forces, their loved ones and families, as well as the people in Iraq whose lives have been compromised by the actions of their leaders.

Previous issues of our newsletters can be found at www.paragondevelopment.com/resources.html.

Our best wishes for success and happiness in 2003!

Your friends at:

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