

# The Challenge

"Disruption has engulfed the New Economy. Emerging digital business models are undermining whole industries. Seeking survival, businesses everywhere are taxing current operations to support risky new offerings. XYZ Co is no exception. Once entrepreneurial, XYZ Co is now a low P/E player in a mature communications equipment sector. Recently acquired by an investment group, the new owners seek growth in market value. They have forced XYZ Co to spin off a NewCo to exploit a new category. A storm is brewing both inside and outside the firm... As Executives your job is to maximize the value of each business and the combined operations."

Attached is a selection of memos and personal notes that set the scene

# News Clippings Service

## Daily Tribune

21/3/20xx

### ANNOUNCEMENT

XYZ Ltd announces the appointment a new CEO, Mary Gerhardt.

Ms. Gerhardt joins XYZ Ltd from Lilliput Resources, a spin-off of AT&T, where she was VP Operations.

Ms. Gerhardt replaces Alec Water (the former CEO) who was killed in a tragic air crash last month.

XYZ Ltd was recently purchased from Founders and majority shareholders David and Geoffrey Kay by Munro Investments Group.

# MUNRO INVESTMENTS GROUP

FROM THE DESK OF THE CHAIRMAN

*Mary,*

*A quick note of congratulation and welcome. The Board has confirmed your appointment as CEO of XYZ Ltd.*

*As you will have realized from our discussions during your candidacy, the acquisition of XYZ was a huge strategic leap for Munro Investments. As the saying goes "failure is not an option". As we explained, the strategy is to use the current business to resource a new category opportunity. This will give us a high P/E ratio and allow us to lever further acquisitions.*

*My advice to you is to impose yourself quickly on the organization. The current management has run their own show for years – the Founders were totally distracted and should have sold up earlier. Expect resistance or at least ambivalence about your appointment particularly as you come from a company outside their industry.*

*Good Luck,*

*I will see you at your father's 90<sup>th</sup> birthday bash I hope!*

*Frank*

# MARKET WATCHERS INC. RUMORS ON THE STREET

## Flash Report

### **Munro Investments Group Interesting Strategy with XYZ Ltd Acquisition**

The Munro Investments Group acquisition of the majority of shares in XYZ Ltd is now complete and rumors are emerging of Munro's strategic intentions. Bluntly, Munro intends to use XYZ as a cash cow to fund what may turn out to be a disruptive entry into the B2B augmented/virtual reality (AVR) space. Munro is rumored to have purchased the rights to a new technology that eliminates the disorientation effects of AR and has what one technologist described as a 10-times improvement in the user experience.

XYZ Ltd was founded by serial entrepreneurs David and Geoffrey Kay who held 60% of the shares. The Founders were bought out by the Munro Investment Group and the brothers have moved on to run their medical charities. XYZ was an exciting growth-stock when first founded but in recent years the Founders lost interest and focused on their charitable endeavours. XYZ Ltd appeared to analysts to settle into being a (quote) "fat and happy" operation, with an inward-looking, self-satisfied culture. XYZ's stable, but underperforming cash flow is said to be the attraction for Munro; Munro clearly feels that a strong efficiency focus would increase free cash flow substantially.

Although interest in AVR as a technology never quite went away, entry into B2B AR is essentially an entry into a new offering category. Munro seems to believe that the human assets and industry connections of XYZ's engineers will be transferable to this emerging sector.

### **Recommendation: Caution**

XYZ may not be the clever investment Munro hopes. Rumors have been persistent for years that XYZ may be itself be disrupted by a new entrant. No one has stepped forward with definite plans, but it remains a risk.

The record of former high growth, hi-tech companies including XYZ recovering their growth status through developing new categories is weak. XYZ has a portfolio of failed prior attempts. It is arguable that the creative people who drove early entrepreneurship are long gone and resistance from current operations to funding new opportunities can be profound. Perhaps XYZ will be the exception – or not!

If you still hold XYZ stock, we suggest putting it on your 'watch' list or sell out to

# Memorandum

## HIGHLY CONFIDENTIAL

**From:** Mary Gerhardt. CEO

**To:** Executive Committee

**Subject:** Market Watch Flash Rumors Report

By now all of you will have read the latest *Market Watch Flash 'Rumors Report'*. Putting aside how confidential Board deliberations reached the Press, I want to confirm that the essence of the Report is true but incomplete.

Munro's intentions are, broadly, as stated in the Report. The Board does indeed expect XYZ to fund entry into the B2B end of the AVR market. This will mean the creation of a new operation (code-named, unexcitingly, NewCo) to be located at Darpenhorpe Research Park. As implied, some individuals will be offered the opportunity to join the new business. Henry Morgan, leader of our Darpenhorpe Lab has been tapped by the Board to lead the NewCo. Henry's entrepreneurial energy is appropriate to this project. I am sure we all wish him well in this key task.

The Market Report stated that XYZ is to become a 'cash cow'. This is an unfortunate choice of words as most view that role in a very negative light. For some years XYZ has generated excess cash flow but almost certainly underperformed. The cash flow was taken as dividends and used by the former owners to fund charitable ventures outside XYZ. The Munro strategy is essentially to increase the efficiency of the business and use the excess cash flow to build a new high-growth business that can sustain a high P/E ratio. If this is successful, Munro sees a long string of opportunities and potential acquisitions.

The strategic risk of a cash cow approach is starving the cow and killing the underlying business. Munro has stated to me that they want to see XYZ prosper and yield returns long into the future to fund other projects. In view of this, Executive compensation in XYZ OldCo will be tuned to 75% XYZ and 25% NewCo so everyone has 'skin in the game'. Another cash cow risk is a loss of belief in the future and good people leaving. I would urge you to encourage those so inclined to stay and seek opportunities in the new spin-offs. More details to follow.

The need to boost XYZ cash flow through greater operational efficiency will inevitably lead to a degree of resizing. My initial impression is that these can be handled through attrition and perhaps an early retirement program. That said, XYZ needs to plan how to meet the lumpy investment needs of NewCo. NewCo will be seeking start-up resources almost immediately and, if all goes well, will be looking for significant growth funding in the next two to three periods.

If you have questions about this Memorandum, they will be discussed at the next Executive Meeting.

## ANNOUNCEMENT

**From:** Mary Gerhardt CEO XYZ Ltd

**To:** All employees

**Subject:** Restructuring

To meet the requirements of our new owners, the following changes are announced in the overall structure of the firm.

**Sarah Hughes**, currently VP Logistics & IT, will take on the role of *Chief Operating Officer* for the old XYZ Ltd business. She will report directly to me. This operation will henceforth be known internally as LegacyCo.

**Henry Morgan**: currently head of the Darpenthorpe Laboratory will take on the task of driving our entry into the B2B Augmented Reality marketplace. This will be done through a new Division named NewCo, Henry's title will be *CEO NewCo*. He will report directly to me. The two operating divisions will be managed totally independently.

**Administrative Services**, being HR, Finance, and Treasury, will be grouped into a Shared Services operation providing expertise for a revenue-based fee of 5% to the Operating Divisions. The shared services will continue under their current functional leadership and will, for now, report directly to me as CEO of XYZ Co.

Please join me in wishing Sarah and Henry out best wishes in their new roles

*Mary*

CEO XYZ Ltd

# Memorandum

**Date:** 5 July, 20xx

**From:** Mary Gerhardt. CEO

**To:** Executive Committee

**Subject:** Game Simulation

As a result of yesterday's heated Executive Committee meeting, I have commissioned *The Business Games Works* to develop and deliver a game simulation of the proposed Munro Investments Group strategy.

*The Business Games Works* builds 'Serious Games'. These experiences help companies to come to grips with the managerial and strategic implications of their strategies. Once played, and if necessary modified, such games can be used to 'roll-out' the strategy to the rest of the organization.

Because of the intensity of the disagreement, *Business Games Works* has been commissioned to customize their core game code to reflect the issues that arose in the Executive Committee. The first session will be held soon. Meanwhile, I do not need to emphasise the need for secrecy.

You will be receiving an email soon from *The Business Games Works* that outlines the experience. They will be arranging to meet with you all individually in the next few days. I have used *The Business Games Works* previously and part of their process is to treat the game as if it were real life. So you will receive an invitation to a series of executive meetings couched as they would be in real life. I know from experience that the meeting will be fun as well as sparking valuable discussion.

Regards

*Mary*

# Business Games *Works*

## Email text

Welcome to the '**XYZ: Leading in a World of Disruption**' Game.

Below is a short description of the experience we will share next weekend.

*The Business Games Works* develops experiences for clients facing major strategic problems. These events allow everyone who participates to understand, align with and commit to the eventual solution by experiencing the leadership issues and contributing to their resolution in the safe environment of a game simulation.

The challenges of this specific experience are as follows:

1. LegacyCo must drive efficiency and yield sufficient cash and human resources to support the start-up and development needs of NewCo and the growth funding needed to carry it up the early part of the secular growth curve. This must be done while maintaining LegacyCo's market share and if possible increasing market strength
2. NewCo must negotiate its demands on LegacyCo for human and financial resources; develop an offering and drive secular growth. It must then successfully establish the offering by winning the race up the secular growth curve to market leadership.

The Game will consist of five teams competing head-to-head. Each team comprises a LegacyCo and a NewCo. The objective is to win – though be prepared, there will be losers! There are three ways to win.

- LegacyCo can develop more market value than any of the other LegacyCos, perhaps at the expense of strangling NewCo by withholding resources.
- NewCo can develop more market value than any other NewCo competitor perhaps by being properly resourced through an 'asymmetric bet' and making the 'right' decisions during the growth period. Such resourcing may compromise LegacyCo.
- A combined LegacyCo and NewCo can jointly create more value than any other LegacyCo and NewCo team; this requires cooperation but is **not** guaranteed to win.

The game is highly competitive. LegacyCos compete with other LegacyCos, NewCos compete with other NewCos. It is quite possible for a NewCo to win while its associated LegacyCo is crushed and vice-versa.

The Game involves 8 Periods of play. A short debrief will be held at the end of each period and a final debrief held at the end of the game that will apply the 'lessons' embedded in the game to XYZ's current strategic situation.

Each period of play explores a strategic issue that you are all but guaranteed to face in the next couple of years. Additionally, the game explores difficult behavioural issues that are known to occur in firms facing your strategic situation.

Throughout the game 'Chance' events will occur that raise specific issues for discussion.

Good Luck!!

*The Business Games Works Team*