Ralph Waldo Emerson, American philosopher and sage of Concord, is often misquoted on the subject of consistency. What he actually said was:

A foolish consistency is the hobgoblin of little minds, adored by little statesmen and philosophers and divines.

And then he added one more thought:

With consistency, a great soul has simply nothing to do.

There is wisdom here for business executives. If you read between the lines, you can see that Emerson is endorsing what might be called a "wise inconsistency." In other words, he argues for both a systematic approach to the world and a systematic way of breaking out of that worldview when opportunity comes knocking.

As I have explained in previous columns in JBS, I am an advocate of rigorous customer and competitor research leading to thoughtful, systematic growth that builds on your core businesses and established strengths. In fact, that approach is at the heart of a discipline I call "strategic market positioning" (SMP). Put simply, SMP is about getting bigger in businesses that lie within your competitive sweet spot while avoiding businesses that put you at a big disadvantage against larger scale competitors. Depending on whether you are the equivalent of General Motors or Ferrari in your industry, that may mean you go after the whole market or limit yourself to a narrow niche.

But is that enough?

Sometimes it is not. All too often, business leaders get trapped in their strategic ruts. They develop elaborate plans for where and how to create value (including plans based on the principles of SMP). But then they fail to adjust those plans in light of compelling opportunities that present themselves. They do not take adequate account of near-term market conditions when deciding when to buy or sell businesses. They write off businesses that have disappointed investors, instead of looking for ways to turn these situations to their own advantage. They worry too much about shareholder reactions to new initiatives instead of doing what is needed to build value. They fail to combine their thoughtful business strategy with a willingness to go against the crowd, buying low and selling high.

You could say that, despite all their good intentions and great planning, they fail to behave like capitalists.

Not all business investors have these failings. Besides working with many corporate clients, I also work with dozens of private equity firms. With the recent rapid expansion of private equity investing, there has been much speculation about the sustainability of this investment model and the level of returns that can be expected from these firms in future. Even so, private equity firms provide some of the best examples of what I call "strategic opportunism."

Need a good example? How about a company that has been bought and...
sold by both private equity and corporate owners? What can we learn by contrasting the actions and relative successes of these two ownership models, as applied to the same company?

In the early 1990s, Snapple Beverage Corporation (founded in 1972) was an innovative, fast-growing drinks company that was doing everything right. It had only limited penetration in the supermarket channel — 20 percent of its 1993 sales — but had great success in the so-called “cold channel” network of small independent distributors who serviced hundreds of thousands of mom-and-pop stores, lunch counters, and delis. Following the principles of SMP, it resolutely stayed out of the channels dominated by the likes of Coke and Pepsi.

The market took note. In 1992, the Boston-based private equity firm Thomas H. Lee Company led a leveraged buyout of Snapple for $143 million and took the company public a year later. The new owners intensified Snapple’s offbeat advertising campaigns and otherwise enhanced its market value.

In 1994, the venerable old Quaker Oats Company bought Snapple for the staggering sum of $1.7 billion. Quaker had enjoyed a big hit in supermarkets with the sports drink Gatorade and believed that it could recreate the Gatorade magic with Snapple, taking Snapple into the supermarket channel using the Gatorade distribution system and vice versa.

It was an SMP disaster of the first order. In the supermarket channel, Snapple was a minnow swimming with the sharks. It began losing money ($100 million in the three years that Quaker owned it). Quaker’s managers began refer to Snapple as a “cancer.” BusinessWeek called the Snapple acquisition one of the ten worst of the decade.

The outcome was inevitable but still stunning: Quaker sold Snapple in 1997 to the Triarc Company (a New York-based PE firm) for the modest sum of $300 million. Triarc wisely steered Snapple back into the cold channel, reversing its decline, and in 2000 sold the company to Cadbury Schweppes for $1.4 billion. Recently, Cadbury Schweppes put Snapple up for sale as part of the sale of their larger beverages business; Snapple is expected to command something like $1 billion.

The bottom line in this blizzard of deals: Snapple’s corporate owners appear to have either lost, or to be on their way to losing, a combined $1.8 billion, with an average annual return of negative 34 percent. Meanwhile, Snapple’s private equity owners have realized a gain of $2.6 billion, with an average annual return of 121 percent before the effects of leverage.

What did the corporate owners do wrong? Put simply, both Quaker and Cadbury had the strategy only partly right and the timing completely wrong. Both companies recognized that they had strong brands (Gatorade and Dr Pepper, respectively) yet lacked scale against the giants of the soft drinks industry, Coke and Pepsi. But they failed to realize the difficulties of combining Snapple’s strength in the single-serve “cold channel” with the strength of Gatorade and Cadbury Schweppes in the mass-market grocery channels.

In terms of timing, both companies missed opportunities to acquire Snapple for a fraction of what they ended up paying, and Quaker was encouraged by impatient shareholders to prematurely free itself from the stigma of a failed deal. Why did Quaker not buy Snapple before it was public, and why did Cadbury pass on the company when they had the chance to buy it for $300 million? A big part of the reason is that most corporate executives are terrified of failure. Failure messes up careers and is awkward to explain to shareholders. In 1992, Snapple was too risky for most corporate buyers, and by 1997 it was considered untouchable.

By contrast, neither of the private equity owners was constrained by public investor perceptions. More important, they saw beyond the short-term challenges that Snapple faced. Thomas H. Lee recognized that Snapple had carved out a successful niche despite being a tiny fraction of the size of the drink industry giants. Triarc recognized that Snapple’s problems in 1997 arose in large part out of Quaker’s attempted expansion into mass markets and that at its heart Snapple still had a strong business in the so-called cold channel.

So what are the lessons we can take from this?

Harking back to Emerson’s prescription, we also have to think outside our adopted box. The key is to look beyond short-term operating results and examine how a business is positioned for long-term success. If recent results have been disappointing, is this an operating problem or a strategic problem? Is recent poor performance the result of minor operating problems, or of ill-conceived management decisions that can be quickly fixed? Or does recent performance reflect some fundamental strategic challenges (strong competitors, concentrated customers, etc.) that will be much harder to change? If it is the former, then chances are that there will be an opportunity to acquire the business at an attractive price and create value through the turnaround. If it is the latter, duck!

Conversely, we have to be on the lookout for businesses that are “fighting above their weight.” In these situations, shareholders and investors often ignore a business’s fundamental strategic challenges and apply irrational extrapolation following two or three years of strong growth. Again: if you are witnessing a heroic but unsustainable performance, duck!

Quaker and Cadbury could both have made Snapple moderately successful by keeping it focused on the cold channel and running it separately.
from their larger mass-market soft drink brands (as Pepsi has done recently with some of its niche beverage acquisitions, such as Izzy). But that would have required changing the formula for where and how each company wanted to grow. More important for this case, corporate culture and the asymmetry of rewards for executive management made it difficult for either company to buy Snapple at the right time and price.

Buyers who apply the discipline of strategic opportunism will find ways to overcome these corporate biases. They know when to accelerate their moves or bide their time based on market conditions. They are not afraid to adapt their strategies to take advantage of opportunities that become available. And the "great souls" to whom Emerson referred will always have something interesting to work on!

About the author

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