THE TIME TO TRANSFORM IS NOW
DANISH COMPANIES ARE UNPREPARED FOR A POTENTIAL DOWNTURN

By Jesper Damm, Christian Gruss, Matias Pollmann-Larsen, and Awais Shafique

It’s hard to avoid. Seen from any angle, there seems to be consensus that the global economy is losing momentum after a period of robust growth. Weakening business sentiments and consumer confidence, decreasing global trade, and increasing debt levels are only a few of the indications that the risk of a downturn is real. Not surprisingly, in a highly interconnected world where the Danish economy closely follows the global one, Denmark is likely to be significantly impacted. This raises the question: Are Danish companies prepared for the slowdown?

We analyzed total shareholder return (TSR) over the last five years as an indicator of how prepared Danish companies really are for a potential downturn. Our theory was that there is evidence that companies that perform well before a downturn have secured competitive advantages that make them more likely to win during, and after, a downturn. TSR measures the return of all cash flows to investors in a given time period, and is therefore a good measure of both overall readiness and the development of individual components that contribute to it. The TSR analyses of 50 of Denmark’s largest companies show a significant contraction year-over-year and performance well below global benchmarks across sectors. When we look at the components of TSR, we see that the contraction is driven by a decline in operating performance indicating companies are losing competitiveness when it comes to growth and earnings. In other words, Danish companies do not have strong foundation from which to face a potential downturn. There is no time to lose in remedying this situation.

Performance of Danish companies is getting worse
A weighted average of 50 of Denmark’s largest listed companies reveals TSR contracting by 19ppt last year compared with the last five years. (See Exhibit 1.) About 50% of this contraction is driven by a decline in operational performance, both revenue growth and margin improvement, as companies have gradually been losing competi-
The companies are now at a level where the operational performance is not delivering any return at all. Market mood, as measured by the multiple changes, is also contributing negatively with a 9ppt decline. This is, however, less surprising given the political and macroeconomic situation. The effect of financing remains stable, indicating no major change in capital structures.

The TSR contraction in itself is worrying because both operational performance and market mood can be expected to sour in a downturn. Even more alarming—and a wake-up call for CEOs—is the fact that operational performance, already declining, is now at a contribution level of zero. With companies not in a position to directly influence the market mood, operational performance is the key lever to drive TSR.

The decline in operational performance is consistent across most sectors, although we do see differences in the magnitude of the drop. The decline is most pronounced for industrial goods (down 16ppt) and health care (down 12ppt), closely followed by financial institutions (down 7ppt), and consumer goods (down 7ppt). Conversely, operational performance is stable within technology, media, and telecommunications (no change), and increasing for transportation and logistics (up 13ppt). It is normal for industries to vary, however a more alarming trend is the global benchmark. Comparing the performance of Danish companies with the average for S&P 500 companies in each sector shows that Danish companies are significantly below global performance across all sectors. (See Exhibit 2.) The relative underperformance is again most significant for industrial goods and health care where the benchmark companies have delivered double-digit operational improvements indicating deeper issues for those Danish companies that have experienced decline. Based on their TSRs, the Danish companies are no longer following their global peers—they are already falling behind.

The time to act is now: preemptive transformation

It is often said that time is money, and this is never more true than when it comes to business transformations. Our analysis of hundreds of transformations involving restructuring found that preemptive change generates significantly higher long-term value than reactive change. Outperformance following preemptive transformation is a fact not only in the aggregate, but across most industries, since preemptive transformations take less time, cost less, and increase leadership stability more, than reactive change. The effect of preemptive...
The earlier a company transforms, the better its future performance

Average three-year relative TSR post-transformation

Reactive
Preemptive

The earlier the better

Source: Sources: Compustat; S&P Capital IQ; BCG Henderson Institute.

1Performance measured as TSR relative to the industry average.

2Reactive transformation defined as negative TSR relative to the industry in the year.
collective transformation ambition. Once the future direction has been set, communication is critical to engaging and energizing the company. As the transformation starts to take shape and the case for change becomes clear, the company can shift gears from planning the transformation to leading it. This means immediately kicking off a Triage/Rapid Assessment and no-regret moves—initiatives that are relatively easy to implement in the first hundred days and that can generate results in 3 to 12 months. These initiatives should close performance gaps in a few critical areas, reduce costs, improve top- and bottom-line performance, and free up cash in order to fuel longer-term initiatives. In parallel, the company must launch broader initiatives to re-invent itself for the future and build sustainable performance with a focus on innovation, growth, and long-term value creation.

For an in-depth analysis of preemptive transformation, including success factors and a six-step approach to success, please refer to the BCG paper “Preemptive Transformation – Fix it Before it Breaks.”

**About the Authors**

**Jesper Damm** is a Partner and Managing Director in the Copenhagen office of BCG. You can reach him at damm.jesper@bcg.com.

**Christian Gruss** is a Partner and Managing Director in the Copenhagen office of BCG. You can reach him at gruss.christian@bcg.com.

**Matias Pollmann-Larsen** is a Principal in the Copenhagen office of BCG. You can reach him at pollman-larsen.matias@bcg.com.

**Awais Shafique** is a Project Leader in the Copenhagen office of BCG. You can reach him at shafique.awais@bcg.com.

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