Fit for the future
A CEO guide to succeeding in a changing world
www.kpmg.com/eu/en/succeeding
Introduction

Understanding what business leaders are concerned about in this changing world, was one of the key prompts for carrying out the first Succeeding in a Changing World (SiCW) Business Leaders Agenda survey.

With responses from over 1,000 senior business leaders from 10 countries in Europe and across 12 industry sectors the results provide a comprehensive overview of the issues they are facing. The results of this are available on: http://www.kpmg.com/EU/en/succeeding

The survey confirmed that the business environment remains challenging all over Europe, though levels of confidence are starting to return to the marketplace. Organisations in the UK, Belgium, the Netherlands and Greece say developing strategies for future growth is the priority, while in Germany, Austria, Spain and Iceland there is comparatively greater focus on solving short-term business needs.

Altogether businesses are still cautious – and are placing strong emphasis on the fundamentals of greater cost efficiency, managing cash flow and supply chains, and embedding risk into strategic planning.

Growth needs to be pursued in a disciplined, rigorous and realistic way, and beyond that, changes to governance and operated models, many formulated in response to the financial crisis, need to be institutionalised. Many businesses have deferred costs or made sweeping cuts across the board to improve short-term performance. Neither of these approaches is likely to deliver sustainable improvement in a higher risk environment.

This CEO guide covers the issues identified in the SiCW Business Leaders Agenda survey. The successors in this changing world will be those who ask more substantial questions of their business model and truly embrace the dynamics of the new market.

The successful CEOs will be those who excel at managing uncertainty and are committed to delivering long-term value by not only focusing on growth but also on implementing robust operating and financial models.

Jeremy Anderson
Head of ELLP Markets

Summary: Are you fit or fragile?

1. It is useful to know how you are performing in your sector, but it is more critical to understand how peers’ business models put them at an advantage or a disadvantage. CEOs should not, however, become so preoccupied with competitors that they overlook the potential for disruptive influences from beyond their peer group.

2. Many organisations have used the downturn to refocus on their core value-creating competencies. CEOs need to treat streamlining as more than just cost-cutting. It can help organisations focus more of their energies upon those areas that create most value. The benefits can be felt in improved margins and also in better decisions and business performance.

3. Business resilience is back on the agenda. The CEO needs to consider whether cost-cutting or layoffs have left their organisation vulnerable or more efficient and how well they can respond to unexpected events, both positive and negative.

4. The CEO needs to be clear who is scanning the landscape for new taxes and regulatory changes, whether industry-specific, such as capital adequacy, or more widely drawn, such as carbon emissions. It is important to understand the externalities in the business model, how these are changing and how these may be affected by new policies, such as tax regimes. Specifically, the sustainability agenda is creating both uncertainty and new growth opportunities in many sectors.

5. Now, more than ever, the CEO needs to lead by example. We have seen that charismatic leaders are not beyond reproach. Leaders also need to ensure that senior management are suitably incentivised and that their conduct is sending the right message to peers, stakeholders and the rest of the organisation.
In the words of Charles Darwin, “the fittest win out at the expense of their rivals because they succeed in adapting themselves best to their environment.” The words seem as relevant today as when he wrote them nearly 150 years ago, but does long-term success always rest on being a market leader?

This question preoccupies many CEOs and organisations often expend considerable time and effort on gauging how they compare with key competitors. However, the most successful companies, like successful athletes, often focus less on beating the opposition than on improving their own performance and service to their customers.

A preoccupation with one’s position against competitors can breed hubris and complacency when one is leading, and unnecessary panic when one is not. It can lead the CEO to underestimate emerging players and new, disruptive influences. There are risks that come with being leading edge, not least that one ends up at the “bleeding edge”, spending too much on R&D, developing innovative new approaches that are effortlessly mimicked by peers, and committing too quickly to new products and markets.

How effectively an organisation understands and adapts to a changing environment, while at times influencing its situation, is more important than striving to lead the pack. Without this understanding, competitor analysis can be a fruitless, backward-looking task that yields little strategic insight. It becomes a self-affirming exercise.

Competitor analysis is only worth doing if it yields real insight into strategy. It should seek to truly understand how rivals’ business models differ in terms of cost structures, funding, supply chain and risk and control culture, to assess what advantages or disadvantages result from what differences. In addition, it should look beyond the organisation’s traditional peer group for new ideas about efficiency and strategy.

To understand the issues within your sector visit the SiCW website at www.kpmg.com/eu/en/succeeding and view the results from the Business Leaders Agenda survey.
Sustainable Cost Efficiencies: Why every euro needs to count

After years of growth fuelled by easy credit and increasing consumption, the economic crisis has caused many organisations to reassess their business models and refocus on real drivers of value. In the past year, some organisations have moved beyond initial cost cutting and scaling back investment to implement long-term strategic change programmes. In contrast, some have not moved beyond these short-sighted steps and have only deferred costs or made one-off sweeping cuts to improve short-term performance.

Real operational streamlining should mean there is no going back to old habits and the operating and governance model is transformed. However, balancing streamlining and business demands give CEOs a formidable mandate – to simultaneously increase revenues and cut costs. To do this in a lasting way may require substantial investment, in new systems and strategies. For example, by re-empowering the finance function, the CEO can give the CFO more capacity to guide the business and deliver high-value information that informs strategy.

In practice, streamlining can permeate every part of the business. It can occur through standardisation or elimination of processes or by simplifying steps within a process. An example is to rationalise the approval steps in a decision-making process to find ways to not only improve speed and efficiency but also heighten accountability and therefore lead to better quality results.

For many sectors, transforming the supply chain and other supporting functions can not only reduce cost but improve the quality of service to customers. The CEO needs to consider how technology can be harnessed to transform and connect different processes while pursuing other enhancements including tax-efficient supply chain models, and leaner manufacturing, sourcing and procurement strategies. As the CEO considers outsourcing or shared services strategies, he or she needs to choose between make or buy models and between the flexibility of multiple vendors or the reliability of a single source.

How can the CEO be sure that business transformation efforts are working, without imposing yet another layer of reporting and bureaucracy? These changes may deliver benefits to the bottom line, but the benefits could also be reflected in other performance metrics, such as reduced overtime, faster decision-making and shorter response times. The CEO needs to lead by example in taking more time to delegate, and using this additional time to spend with key customers and people throughout the business. Leadership means sharing face to face what is happening, and engaging and empowering people to be part of the organisation’s future success.

CEO checklist

- Has your response to the downturn moved beyond cost cutting to institutionalising real and widespread transformation?
- Have you streamlined business processes and have you checked if these are delivering benefits to the bottom line? Is streamlining of processes starting at the point of customer engagement and co-design and extending right through your company’s value chain?
- What performance metrics have you introduced to measure the effectiveness of your change programme?
- Do you monitor overhead expenditure and has it recently started to increase again?
- How much time have you spent with customers in the last year?
- Have you really succeeded in improving discipline around cash and working capital?
There are valuable lessons to be learned from the many crises that have befallen businesses in the past two years. In a recession, or in the early phases of economic recovery, strategic planning should be approached as a structured process that brings together external market dynamics with deep insights from key customers and internal stakeholders, to map the future path of the organisation and build a resilient business model.

This planning process needs to establish how an organisation should respond to a range of scenarios or business disruptions. The loss of a key customer can be the biggest form of disruption that many organisations will ever face.

Preparedness for all such outcomes needs to include an assessment of financial impacts, plans for communication with internal and external stakeholders, and processes for identifying and mobilising backup and support systems. Are cash and working capital sufficient to withstand another rapid deterioration in business conditions? Stress testing can be a means to assess these risks; it is not just an exercise for the banks.

In times of austerity, strategic planning needs to be based on practical and cost-effective measures while remaining flexible enough to handle changes in people and processes.

Heightened counterparty risk has been a hallmark of the recent financial crisis and by no means confined to the financial sector. It may be something that was overlooked in strategic planning. The CEO should consider whether capital expenditure plans are flexible and capable of being delayed or postponed without major penalty or inconvenience.

It can be harder to build a culture of business resilience when the concept is associated with outlier events and continuity planning. In a bull market, entire risk management functions can be pushed to one side in the pursuit of new opportunities.

Scenario planning rests on good business intelligence. With unified IT platforms providing consistent data according to predefined key performance indicators, the CEO is in a better position to understand how different types of disruptions will impact the business at different levels of scale.

CEO checklist

• Is there resilience in your organisation? Have you prepared for a major event affecting your people, your bottom line or your share price?

• Have your business continuity plans been reviewed and refreshed in light of recently-implemented cost cutting and streamlining measures?

• Is scenario planning alive and well in your business?
Increased regulation and oversight are frequently highlighted as a primary concern for CEOs globally. They are harder to influence and can result in increased capital needs, higher taxes, and unacceptable risk/return ratios leading to businesses being curtailed or exited.

Since the onset of the financial crisis, regulation has increased. Tax authorities have also become more aggressive in their collection of tax revenue and have placed some organisations under greater scrutiny. Financial sector reforms and regulations imposed in western economies have had repercussions for institutions in Asia Pacific, even for those that had little to do with the financial over-engineering seen in London or New York. One impact these reforms may have on wider business conditions concerns the ability of organisations throughout the economy to access capital or extend lines of credit.

The emerging issue of sustainability has become another catalyst for new regulations and potentially other tariffs including carbon taxes or pricing mechanisms. The environmental debate has now moved beyond compliance and risk and the CEO is uniquely placed to have the right conversations with external stakeholders, including governments and regulators, and to demonstrate that his or her organisation is responding.

Another area of public concern where governments are being forced to respond relates to data privacy and security. Many businesses are increasingly reliant on electronic or mobile communications to market or sell their products, make payments and share personal data. Requirements to change how data is handled or stored can present challenges to an organisation if its IT architecture and key processes are not well mapped out. In the most extreme examples it can undermine critical delivery or payments systems, or lead to significant reputational damage.

The responses of many global organisations to the climate change agenda or data privacy concerns illustrate how they can be optimised through proactive engagement, with the CEO as a key spokesperson. The CEO has a responsibility to understand the external impacts of one’s own business model. He or she has a role to play in shaping regulatory policy ensuring that it is both appropriate, and harnessed to support future success.

Turning risk to advantage: The CEO’s critical role

CEO checklist

• Do you have any means to measure the costs and benefits of compliance activities to your business? Is there a clear link to brand protection and reputation?

• Can your systems be used to assess other externalities, such as carbon or energy impacts?

• Have you institutionalised a process to monitor regulatory developments in each country in which you operate?

• Are there areas where you can streamline compliance activities by applying common systems for detection, investigation and reporting?

Building lasting success: Institutionalising the right practices

Many organisations instilled a new sense of discipline in response to the downturn, but it was only when growth opportunities reemerged that these were put to the test. Management can slip back into old habits and costs rise once again. Institutionalising the things done during a downturn is not as easy as it may seem when the business is once again looking ahead and short-term survival is less of a concern.

Consistency is key. As the business environment changes, people may view stricter rules or guidelines as temporary and thereby dismiss them, particularly if their peers and managers are doing the same. At this point, policies and procedures should be reinforced and reviewed to ensure their ongoing relevance.

The CEO needs to demonstrate and make clear to everyone that the disciplines and rigours imposed during the downturn were not endured for nothing. More importantly, it must be stressed that those impositions were and continue to be part of a strategy to build a stronger business for the long term. In doing this, management needs to set the right tone at the top and lead by example; no senior executive can be beyond reproach.

This strategy can have external dividends as well. After the volatility of the past two years, many investors are looking for companies that can demonstrate sound management and generate more stable earnings. Recent events are a reminder that even the largest and most reputable of companies can come unstuck if they set overly ambitious quarter-by-quarter earnings targets and get blinded to the accompanying risks.

In any company, the CEO needs to understand what incentives will work. He or she should reconsider what earnings are paid back to investors as dividends and where bonuses are paid. The CEO must ask themselves whether these are aligning the management’s interests with the long-term benefit of the organisation. In the current climate and with public demands for greater regulation, the CEO should lead in this regard, long before regulatory pressures force his or her hand to do so.

CEO checklist

• Is your leadership team setting the right tone at the top and taking the lead in implementing company policies and procedures?
• What steps are in place to monitor, ensure appropriate adherence, and impose disciplinary actions on non-compliance?
• Are the policies and procedures built for adherence over a sustained period?
• Do communications with stakeholders demonstrate a focus on long-term success as well as short-term expediencies?
About Succeeding in a Changing World

The uncertainty of the economic climate combined with the complexity of business today, leaves the Board facing a number of issues. KPMG’s Succeeding in a Changing World programme is helping define and refine the business agenda away from traditional and emotional issues to facilitate the Board’s success against the backdrop of change. Whether it is ensuring the business is fit for purpose, poised for growth or focusing on the future, we are working with clients to ensure they can succeed in a changing world.

The KPMG’s ‘Business Leaders Agenda’ online survey has the views from over 1,000 European business leaders of what is on their radar over the next six months. To view the results go to: www.kpmg.com/eu/en/succeeding

For more information, or to discuss the issues raised in this report, contact one of our SiCW experts.

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