KPMG

Issue 5, Mar/Apr 10

Agenda

Insights into growth, performance and governance

Is your model obsolete?

How emerging economies will revolutionize the multinational

Make intelligence pay

Seven ways the right data could transform your performance

Circus master class

Why managers must unleash their inner PT Barnum

"If you're applauded, worry. Great moves are greeted by yawns"

The strategies behind *Warren Buffett* – and what he might do next

AUDIT ▪ TAX ▪ ADVISORY

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"To rise to the occasion, America needs to act anew and think anew.

That's what Abraham Lincoln told the American people in 1862, suggesting that the dogmas of the quiet past would not help them in their stormy present.

His words seem just as apt today as the U.S. faces its greatest challenge since the 1930s. But it is impossible – if you consider the economic and political resilience this nation has shown in past crises and the ingenuity, vision and character of its business leaders – not to regard the future with measured optimism.

The rise of China as an economic superpower should not blind us to the size, influence and underlying vitality of the U.S. economy. The U.S. reacted swiftly to the global economic crisis. As a percentage of GDP, the federal government's stimulus package was significantly greater than the investments made by rival economies. If government's role is managed wisely and if business thinks anew about its models, strategies and performance, the economy will recover. To assist in that thinking, we explore such great U.S. success stories as Cisco, IBM and News Corporation in this issue.

Agenda's insights into growth, governance and performance are now online. At **www.kpmg.com/agendaonline** you will find a variety of content – some written exclusively for the web – all produced with one aim: to help you run your business."

Alan Buckle
Global Head of Advisory, KPMG

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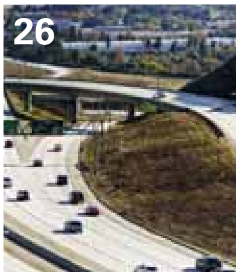

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The grid to power a revolution

New electricity networks could help profits and the planet

If you believe the hype, 'smart grid' infrastructure could be as lucrative as the internet and as life-altering as the combustion engine.

The smart grid delivers electricity using two-way digital technology to control appliances at consumers' homes to save energy, reduce cost and increase reliability and transparency. The U.S. Department of Energy estimates that smart grids could save at least US$46bn (€31.2bn) in the next 20 years. The Commerce Department is also exploring ways to speed up the patent process. It can take 40 months for green technology patents to be granted, and the aim is to reduce that to a year.

The U.S. administration unveiled Austin, Texas, as the country's first grid-friendly city, with 410,000 smart meters. The next stage is for solar-powered homes and wind turbines to deliver energy back to the grid.

China has offered a 50% subsidy for smart grid systems, a move analysts say may stimulate US$10bn (€6.8bn) investment. Governments in Australia and Canada have committed to smart grids through regulation or investment,

15%

fall in carbon emissions smart grids could deliver

and the European Union is developing a technology platform for smart grids to shape electricity delivery from 2020 onwards.

Start-ups with innovative metering ideas have benefited from early handouts, but multinationals have spotted the opportunity too.

BP Solar expects future growth, and lower prices for panels, to be driven by the grid. IBM has signed a grid integration contract with Energy Australia. General Electric has just taken an equity stake in smart grid software company Tendril and is working with Google to develop a solution to give consumers more information on energy consumption.

Google CEO Eric Schmidt believes the grid could lead to a "second Industrial Revolution".

The smart grid has proved a lucrative business for start-ups and multinationals

Jim Richardson/National Geographic/Getty Images; The Moviestore Collection

microtrend

Chief Performance Officer

As public finances tighten, more countries may follow Barack Obama's example and appoint a Chief Performance Officer (CPO) to make the public sector more efficient. Former consultant Jeffrey Zients, the U.S. government's first CPO, says he will not be redesigning government but focusing on "execution and results". Zients is responsible for providing the tools and technology to help the 24 major agencies and departments deliver value for money. The federal government spent around US$2.98trn (€2trn) in 2008, a deficit of US$455bn (€309bn).

Qatar's economy steps on the gas

Qatar made its fortune with oil but has diversified so successfully – attracting investment from celebrity restaurateur Robert De Niro and auctioneer Sotheby's – that this Middle Eastern monarchy is expected to enjoy double-digit growth this year.

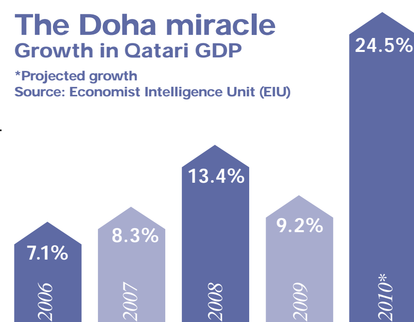
Apart from a bid to host soccer's 2022 World Cup, Qatar has kept a low global profile, focusing on the development of its biggest natural asset: liquefied natural gas (LNG). Qatar will soon account for a third of the world's LNG supply, and its reserves will last around 150 years. It recently began shipping LNG to China in a 25-year deal. "Qatar is the polo pony of the Gulf economy: small, flexible and able to move quickly," says Oliver Cornock, a Gulf specialist at Oxford Business Group. "It has one of the most robust and secure economies in the world." Public debt stands at only 6% of Qatar's US$83.2bn (€56.4bn) GDP.

Qatar's size – its population is 1.4 million – has, Cornock says, helped the government to diversify, hedging against oil and LNG price fluctuation. After being bruised by past oil crises, the country aims for 80% of its income to come from outside the energy sector by 2015, encouraging innovation and R&D among private firms and easing restrictions on foreign investment.

The Doha miracle

Growth in Qatari GDP

*Projected growth
Source: Economist Intelligence Unit (EIU)



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Why Denmark works

But can flexible labor model be exported?

Danes can be fired at a week's notice and pay the world's highest tax rate, yet Denmark often tops polls as the happiest nation and has the fifth highest GDP per capita in the world.

The Economist Intelligence Unit predicts that Denmark will soon be the best country to do business in. Experts believe the policy of 'flexicurity', a response to rising unemployment in the 1990s, has made Denmark, a country with no natural resources and no single dominant company, one of the most competitive economies in the world.

Flexicurity blends a flexible labor market, generous social security and an active employment policy with rights and obligations for the unemployed. Workers pay an average of 42% income tax, but trade job security for a guarantee of time-limited but generous unemployment pay and, because hiring and firing can happen from one day to the next, they are confident they will get new jobs fast.

Poul Nyrup Rasmussen, the prime minister who masterminded flexicurity, says: "It's made Danes feel more economically secure and able to adapt to economic change." One in four Danes changes jobs each year (70% say this is good for morale) and the unemployment rate is still only 4.1%.

Opinions differ on how exportable this model is. Denmark has a century-old tradition of dialogue between employers and unions – which may not be the case in other countries seeking a quick fix.

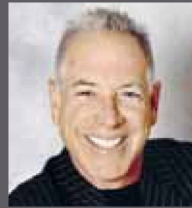
Hans Skov Christensen, CEO of Dansk Industri, the employers' federation, says: "Companies face a Darwinian struggle in a globalized economy. Only companies who can adapt rapidly to constant changes in market demands will survive and you need flexible labor markets to be able to adapt".

Flexicurity means Danes now feel much more secure than Hamlet

Running the same risks?

Has the credit crunch persuaded many companies to revise their risk management strategies? Not according to Sir Deryck Maughan, former head of investment bank Salomon Brothers, who told a *Wall Street Journal* conference that the finance industry had not "faced up to the intellectual failure of risk management systems, which are still hardwired into many banks and trading floors." Mike Nolan, Head of Risk and Compliance at KPMG and a Partner in the U.S. firm, believes risk metrics are as crucial as growth when evaluating deals, and says the chief risk officer should be part of the decision-making team. Find out more at **www.kpmg.com/succeeding**.

leading edge



Welcome to Web 3.0, where retail conquers all

Businesses need to understand the technologies that could revolutionize their markets, says James Canton, chairman of the Institute for Global Futures (www.globalfuturist.com)

A new era beckons

Lightning-fast mobile transactions over interactive TV auctions. Auto sales conducted by intelligent agents. Real-time selling via social networks. All these emerging digital markets represent an historic opportunity for business. Online retail consumer spend in the U.S. alone, which stood at US$150bn (€101bn) in 2009 and worldwide is worth more than three times as much, is still a fraction of total retail sales. By 2015, however, the projection is that it will be worth US$1.4trn (€1trn) globally.

The wireless way forward

There are four billion cell phones on the planet today, two billion people will be on the internet within five years, and 90% of future cell phones will offer internet transaction services – we're talking a huge audience of internet users. This is happening much faster than media reports suggest and companies – and IT leaders – need to be ready for this accelerated, fast convergence.

A global revolution

One of the most exciting aspects of this sea change in retail marketplaces is its genuinely international nature. The growth in 'm-banking' has been driven by sub-Saharan Africa, where mobile connectivity offers a cheaper and more reliable alternative to fixed line internet access. India is adding 10 million mobile subscribers every month. The use of phones for transactions in Japan and Korea (where many people are now happy to buy plane tickets via a handset) is well documented, but the potential for m-commerce growth in North America and Western Europe is enticing for telecomms companies and should be equally interesting to retailers looking for growth.

Towards a new reality

Alongside more recognizable forms of commerce is the currently developing idea of 'augmented reality', where our view of the real world will be supplemented by additional information provided by handheld devices (and, potentially, by a yet-to-be-invented headset or pair of glasses). This might sound like sci-fi, but it's already in use on some smartphones. The potential for businesses to push their services with GPS technology – marketing directly to people in a specific geographic area at any one time – is already being exploited on a small scale, and could become commonplace.

Building blocks of a cultural shift

The outlines of the new era can already be discerned. Web 3.0 – where the internet takes on a life of its own, fulfilling requests before they have been made and applications shift between computers, mobile devices and other hardware – will unite billions in a cyber-marketplace. 'Smart products' connected to the web will create their own network. And a digital eCash standard will emerge for the sale of online goods. We will want to entertain, buy, sell and meet online even more tomorrow than we do today. Businesses need to be part of the conversation.

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What's on their 'to do' list?

They belong to different generations and different sectors, but these five North American business leaders all face the same issue: how to deliver growth in uncertain times

01 JIM BALSILLIE

48, co-CEO, Research In Motion

BlackBerry, the flagship brand of Research In Motion (RIM), has revolutionized smartphones since 1999. But as rivals hit back – and new models proliferate – can RIM stay on top?

The story so far RIM began life in 1984, set up by Mike Lazaridis, the company's co-CEO. Sports fanatic Jim Balsillie (he has tried to buy three NHL ice hockey franchises) joined in 1992 and together they sharpened their operational focus, making RIM the world's fastest growing company in 2009 according to *Fortune* magazine, with profits increasing by 84% over the past three years.

What's next? RIM has sold 75 million BlackBerry smartphones worldwide but the market, while still enjoying double digit growth, is very crowded. Worries over competition have hit the company's shares. As younger users ditch traditional handsets, Apple, Nokia and Palm expect to grow market share. RIM has launched its own app store, bought developer Torch Mobile to beef up its internet browser and launched sleeker models like the Storm to woo a younger crowd. A push into Africa and the Middle East may help offset any loss of share in the U.S. but new applications could be crucial.

He'll succeed if... BlackBerry App World pays off, the browser improves and the financial results reassure analysts about growth.

02 RICHARD G WOLFORD

64, CEO, Del Monte Foods

Eight out of ten American households may buy Del Monte products but CEO Richard Wolford isn't complacent. Greater marketing spend, centralization, social media and dog's breakfasts all feature in his plans to accelerate growth.

The story so far Made famous by the slogan "The man from Del Monte, he say yes", the 93-year-old firm focuses on North America, where its core operations are canned goods and pet foods. The latest quarterly results show net income up 24% year-on-year to US$62.6m (€43.8m). Wolford, a results-driven boss who lets the brand have all the profile, once worked in a rival's Hawaiian warehouse and joined Del Monte as CEO in 1997.

What's next? The downturn has been fruitful for Del Monte. Despite worries about overcapacity in the industry, canned food sales have risen and the group has offset higher commodity costs with its pricing. Prudent fiscal policies have kept debt levels low, enabling Del Monte to ramp up its marketing spend in 2009, focusing on recession-friendly, healthy meal options. Creating an online community of pet owners, Del Monte found that many dogs love fried breakfasts and launched egg-and-bacon-styled Snausages dog food to invigorate the sector. Canned food does have an image problem, however, and Del Monte may need a new strategy when consumers begin to feel more affluent.

He'll succeed if... Overcapacity remains a threat, rather than a reality. The hefty marketing spend grows share. The move to a single marketing HQ in San Francisco increases efficiency.

Go further

Find out more about these companies and their leaders at: *www.rim.com*; *www.delmonte.com*; *www.cooperindustries.com*; *www.grupobimbo.com* and *www.darden.com*

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03 TERRY KLEBE

55, CFO, Cooper Industries

When economic crisis struck, this historic industrial conglomerate was ready. Now its CFO has to position it for the upturn, and a greener future.

The story so far Cooper Industries' history could not be more emphatically American – and its future direction is emblematic of the way major, diversified U.S. groups seek to reinvent themselves. The company was formed in 1833 when brothers Charles and Elias Cooper sold their horse to fund an iron foundry in Ohio. Today, Cooper Industries enjoys annual sales of US$5.1bn (€3.7bn) selling electrical systems, tools and lighting in 23 countries. Terry Klebe, a former CIO at Cooper who became CFO in 2002, showed his worth in the crunch, cutting costs to beat profit expectations. "In 175 years, the company has never adjusted this rapidly," he says. Revenues in its core markets remain under pressure.

What's next? Klebe shed non-core businesses, freeing up resources to achieve record cash flows and make the right acquisitions to diversify globally. Cooper is now focusing on the dual opportunities of emerging economies and green infrastructure, investing heavily in Saudi Arabia, growing market share in China and developing new eco-friendly lighting and 'smart grid' electrical products as its traditional construction markets suffer.

He'll succeed if... Cooper is nimble enough to seize M&A opportunities. Global expansion gains momentum: in 2009, 39% of revenues were generated outside the U.S. The company has the right cost base to flourish in the green infrastructure market.

04 DANIEL SERVITJE

50, CEO, Grupo Bimbo

The smell of baking bread is Daniel Servitje's earliest memory. Now he runs the world's biggest breadmaker, Grupo Bimbo, which last year increased its debt by 800% to buy American baking giant Weston Foods for US$2.4bn (€1.6bn).

The story so far Servitje's father founded Grupo Bimbo in 1945 and soon made it Mexico's biggest baker. Named CEO in 1997, Daniel showed his mettle straight away, investing in a massive technological overhaul in the midst of a recession. The Weston Foods deal has sent profits soaring and increased the group's presence in a lucrative market. "It was a risky decision in this economy," admits Servitje. Bimbo has also expanded in other areas, doubling its Chinese operations in 2008 and shifting to oxodegradable packaging in 2009.

What's next? Fears over debt have been assuaged by a bond issue and repayment of a bridging loan. Now Servitje just has to show the Weston deal was worth the money by generating growth. Another acquisition or two in China is likely as Grupo Bimbo seeks to expand in Asia.

He'll succeed if... Grupo Bimbo keeps an eye on debt. It manages to grow in the U.S. and China without losing ground in Mexico which, even after Weston, still supplies 47% of sales.

05 CLARENCE OTIS, JR

53, CEO, Darden Restaurants

Darden Restaurants is the US$7bn (€4.7bn) king of the 'casual dining' high-volume, sit-down restaurant business. Former investment banker Clarence Otis Jr joined Darden as treasurer in 1995 and became CEO in 2004, one of few African-Americans to run a Fortune 500 firm.

The story so far Bill Darden set up the Red Lobster seafood chain in 1968. Today, the conglomerate's biggest brand is the lucrative Olive Garden chain, which generates around US$3bn (€2bn) in revenue from 690 restaurants. Otis has united the five key brands in a new head office and streamlined R&D in one giant kitchen, remaining sensitive to each brand's characteristics and culture. "Leaders really think about others first," he says. "They think about the people trying to help them get the job done. They think about the people they're trying to do a job for." So he has resisted cutting its 180,000 workforce (believing customer service is more important than ever) and refused to let Darden engage in a race to the bottom as rivals discount.

What's next? Otis expects new restaurants to generate most growth. An admirer of Wal-Mart's supply chain, he has introduced cutting-edge software to coordinate meal delivery to diners, and direct purchasing to trim costs. His next priority – apart from healthier menus – may be to position the different brands as effectively as the Marriott hotel chain.

He'll succeed if... He is right in believing that the downturn won't change dining habits for good. Darden gets the mix of new restaurants right, especially by finding the right venues for its new upmarket Seasons 52 chain. It keeps outperforming its rivals.

"Leaders think about others first – the people who help them get the job done, the people they do a job for"

Alfredo Estrella/AFP/Getty Images

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What business intelligence can do for your bottom line

Fancy improving your performance by 34%? If you can get the right information to the right people at the right time, such a jump is possible

BY PAUL SIMPSON

Next time someone tells you investing in business intelligence is a waste of money, tell them the story of J.P. Morgan chairman and CEO Jamie Dimon. In October 2006, Dimon decided that the bank's growing business in securitizing sub-prime mortgages "could go up in smoke" and pulled out of the market when it seemed to be booming. The triggers for Dimon's decision were two pieces of business intelligence.

That very month, at a regular review of the bank's mortgage servicing business, the head of servicing noted that late payments on sub-prime loans were soaring at an alarming rate. And J.P. Morgan's investment bank saw credit default swaps, a means of insuring against failing sub-prime loans, becoming much more expensive. That was enough for Dimon. He ordered his managers to bail out of sub-prime, a decision which saved the bank billions and left it, after the credit crunch, in a much stronger competitive position.

1 Confront reality – and be profitably surprised

Andy Neely, deputy director of AIM Research and a professor at Cambridge University's Institute of Manufacturing, says J.P. Morgan's escape indicates the transformational value of business intelligence. "Good business intelligence should provide surprises. Management hold many assumptions about the way organizations and markets work. Used well, performance data and insights challenge these assumptions, providing that 'aha!' moment. There are more mundane aspects – giving insight into operational performance and prioritizing investment – but when it delivers surprises, it becomes truly valuable."

Used wisely, business intelligence can help managers follow former General Electric chief Jack Welch's advice: "Confront reality – not as you wish it were, and not as it used to be, but as it really is." Simply by crunching its customer data differently, segmenting its buyers more effectively and using that to shape its sales strategy, online retailer Amazon increased revenues by 8%.

One of the many ironies of the credit crunch is that companies are tempted to invest less in business intelligence when they ought to spend more. Gartner estimates that in the next two years, 1,750 of the world's largest companies will regularly fail to make insightful decisions because they don't have the right intelligence at the right time with the right people.

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Who'd have thought it?

Classic mistakes in handling intelligence

Making the decision before the intelligence arrives. General Custer wanted to impress head office by attacking the Sioux in 1876. His scouts warned him the enemy was several thousand strong, but Custer had already decided to attack and charged at the Little Big Horn. Outnumbered nine-to-one, he and his men died within the hour. His scouts survived: Custer had been so disgusted with their reports he'd sent them to another unit.

Using the past to predict the future. Usually, the past is a fair guide. But not always, as the *Chicago Tribune* discovered in 1948. Correspondent Arthur Sears Henning, who had called four presidential elections correctly, was sure Thomas Dewey had beaten incumbent Harry Truman. So the paper ran the headline "Dewey Defeats Truman" before votes were counted. When Truman won, he brandished the paper in triumph (below).

Distrusting the source. When a wooden horse turned up outside Troy, an event the prophetess Cassandra had said would be catastrophic, the Trojans accepted the gift – even though a blind priest called Laocoon shouted: "It might be full of Greek soldiers". Ignoring his plea to "poke it with a spear and see if anyone yelps", the Trojans lost the war.

Keeping intelligence in silos. Philip II's invasion of England in 1588 might have prospered if he had thought harder about communications between the Spanish army and navy. His commanders did their best – the Duke of Parma's 30,000 troops were poised at Dunkirk – but had no effective way of communicating progress. An attack from land and sea might have troubled Elizabeth I but the Spanish army had no idea when the armada would reach the English Channel.

Ignoring intelligence because it doesn't fit. In the 1940s, U.S. diplomats in China told Washington that its key ally, Chiang Kai Shek, was losing the Chinese civil war. Yet historian Barbara Tuchman said: "No matter how much evidence was amassed, nothing induced Washington to loosen the silver cord that tied America to Chiang Kai Shek". The State Department, Tuchman claims, effectively said: "Don't confuse us with the facts". China went Communist in 1949.

W. Eugene Smith//Time Life Pictures/Getty Images

2 Use intelligence to transform your performance

Since the 1980s, companies have been doing business in the information age, yet KPMG's research suggests that seven out of ten executives still believe they get the wrong information to make decisions. What's going on?

Neely believes organizations often make do – even though they mistrust their data – because of a misinformed skepticism about the rewards of investing in business intelligence. "Managers often see it as an IT issue, but research shows that companies need to simultaneously create infrastructures for management and IT. If you develop one or the other, the best you can hope for is an 8% improvement in performance – if you combine the two, your performance can improve by 34%."

The advent of groundbreaking business technologies often follows a familiar pattern. Evangelists hype up the technology, early adopters invest on the strength of that hype and are disappointed. But by analyzing their failures, they can adopt a more realistic approach to the technology which delivers genuine value. Now the hype about business intelligence solutions has begun to clear, credible evidence of their value is emerging.

Knowing shoppers' budgets were tight last year, Wal-Mart, crunched its inventory data to reduce stock (cutting costs by 6%) and to identify which product discounts would most help consumers. The resulting influx of new customers compensated for lower sales per customer and boosted profits.

3 And you don't need to break the bank

A 34% increase in performance would turn any CFO's head but Linda Imonti, Global Co-Leader, Business Intelligence at KPMG International, says: "The fear is that people will come in and say you need to invest millions of dollars to get this right." A good CIO, Imonti says, will first try to meet business needs with tools the organization has already invested in. Besides, she says, the aim isn't to have the biggest database in the world: "The bigger test is turning that data into information and using it as intelligence to make decisions."

"The fear is that it will cost millions to get this right. But small investments can deliver real improvements"

Bernd Trautwein, Partner, KPMG in Germany, says the bill for business intelligence isn't that steep. "Our research suggests that a global consumer goods company will probably be spending around 2% of IT investment [on intelligence]." Calculating the ROI on that spend may not be easy, but Trautwein says: "The question is whether the CFO feels he could reduce the amount of people managing, reconciling and analyzing data."

There are, Imonti points out, other gains: "If the investment helps you manage your supply chain more efficiently, you will be able to predict a percentage reduction in costs. Similarly, if you can handle sales information more rapidly and efficiently, you could predict a certain increase in sales."

Sometimes, the gains can be unexpected and delightfully simple. All Mattel, the world's largest toy-maker, did was collect more detailed information from high-volume retailers on the goods they returned. Analyzing that data helped it reduce the costs of defective returns by over 30%.

Neely believes the real gain is much bigger – and hard to quantify: "There are major challenges in improving the quality of data and eliminating inconsistencies, but companies that have backed their business intelligence with long-term investment claim impressive levels of ROI. And we're not talking about short-term paybacks, but a fundamental shift in performance."

4 Be careful about what you measure

IT is a convenient scapegoat whenever a business intelligence investment fails to deliver but, Imonti says, the real responsibility often lies with the CEO: "The first question you have to ask is whether you're measuring the right things. Are these metrics on your CEO's dashboard? How does measuring days of inventory, for example, relate to the strategy?"

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The original gift horse: The Trojans' failure to heed intelligence lost them their war against the Greeks

Go further

Effective use of business intelligence is explored in *The Granularity of Growth* (Wiley), while the lessons companies can learn from the Oakland Athletics can be found in Michael Lewis's *Moneyball* (W.W. Norton & Co). Andy Neely's ideas on the 'Performance Prism' are explored at www.performance-measurement.net/news-detail.asp?nID=31.

Defining metrics might be simple, making sure they are used is tougher. "You can have the best solutions in the world but unless you enable your enterprise-wide team to use them, you have lost the battle," says Imonti. "And if senior management keep using the old measures, it's all over."

Neely adds a word of caution. "Remember the old adage that 'you get what you measure'. When telesales staff are monitored on the length of time it takes them to deal with customer calls, it is not uncommon to find them cutting people off mid-call just so the data looks impressive. Malevolently or not, staff will adopt 'gaming tactics' to achieve targets they have been set."

Neely says the classic example is the British National Health Service, where an apparently logical target – reducing waiting lists – leads to outcomes "that don't necessarily improve the quality of healthcare for the public at large".

5 What you're not measuring matters

The Oakland Athletics are one of baseball's most intriguing stories. With a budget 60% smaller than the New York Yankees, the A's have punched above their weight by ignoring conventional wisdom and using data-driven management to recruit players. General manager Billy Beane found that if you analyzed how often a player reached a base and how many bases they reached after their hits, you could measure a batter's power more accurately than such yardsticks as stolen bases, which had been used by scouts since the 19th century. The stats persuaded the A's not to follow the traditional strategy of buying players at high school: they found the hard stats on a player's performance at college forecast achievement more accurately than a scout's subjective forecast of a high school player's development.

In *The Granularity Of Growth*, Mehrdad Baghai, Sven Smit and Patrick Viguerie argue that firms should emulate the A's and drill deep into their data. Their research found that the global economy has millions of growth pockets – some worth as much as $200m (€137m) – and that the chief differentiator of organic growth between 200 top companies was whether they were in the right growth pockets. These pockets – often geographical or specialist sub-divisions within a sector – might not be obvious in general sales data. But, their research suggested, choosing the perfect portfolio of pockets was much more likely to deliver organic growth than any attempt to increase market share.

6 You can't solve this issue with IT

"Many companies believe implementing a new platform will solve their problems," says Trautwein, "but if processes aren't standardized, you're probably not deriving the right decisions from it."

Trautwein advises: "Don't run the project from IT, run it from the business." Imonti says it is crucial that business units buy into the new approach and that buy-in is much less likely if the solution is perceived as being imposed by IT.

That said, you can't ignore IT, because the issue of who needs to see what information and what they can do with it is complex. "A basic mistake is making all information available to all people to make any decisions," says Neely. "You need to provide the right information to the right people at the right time. This can mean senior managers relinquishing control over certain decisions."

CIOs need to ensure their company retains a certain flexibility and doesn't rely too heavily on one vendor. In companies with strong information cultures, they may also want to engage with the business by launching a task force to ensure they are delivering the intelligence managers want.

7 A journey of a thousand miles...

...begins with one step, as the ancient Chinese proverb says. Trautwein suggests that managers considering investing in business intelligence should heed this. "To go from 0-100% in one big step is too big, too complex. You might want to start with a small project, where you can measure success, or build agreement that this is a step-by-step process over a long term."

There are many ways of deciding whether your investment is succeeding, but the best criteria, Trautwein suggests, "is whether the quality of support for decisions has improved." If managers start to trust the data they use – and the data is timely and accurate – they have a better chance of making the right decisions and being profitably surprised by the data they receive. With the global economy on a long and winding road to recovery, this is hardly the time to be flying blind. ●

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"Ask yourself: could a fool run your business? Someday a fool probably will"

Warren Buffett's deep understanding of capital, grasp of value and folksy charm have made him America's favorite tycoon. Agenda analyzes the strategies that got him where he is today and considers what might be next on his to-do list

BY PAUL SIMPSON

Warren Buffett once said some businesses were so strong they could be run by a ham sandwich or, to use another of his favorite examples, by "an egotistical orangutan". His admirable refusal to believe in the transformational power of human genius when confronted with a corporate train wreck, instinct for undervalued cash-generating businesses and willingness to look stupid in pursuit of the right deal have made Buffett an icon to fellow billionaires such as Bill Gates. Yet he is not lionized in business schools, where clever ideas – even if they are not borne out by nitty-gritty reality – are worshipped, and due-diligence and a thorough understanding of balance sheets and market sentiment don't resonate.

Buffett started young. "I became interested in stocks when I was six or seven. I bought my first stock when I was 11 and I picked up Ben Graham's *The Intelligent Investor* when I was 19," he said once. *The Intelligent Investor* is the definitive exposition of value investing. At its simplest, this means buying shares you believe are seriously undervalued. Buffett didn't just read Graham's book, he worked for Graham, using his theories to earn a small fortune. One of his most spectacular value investments was his purchase of Coca-Cola shares. In 1988, after the stock market crash and the New Coke launch had turned investors against Coke, he bought US$1.02bn (€750m) of stock in the soft drinks giant. By 2007, his investment was worth ten times the original sum and had generated an annual return of around 20% for Buffett.

Let's return to the beginning of this story. In 1956, when his mentor Graham retired, Buffett was already worth US$174,000 – US$1.4m (€1.03m) in today's money. Still in his mid twenties, Buffett returned to Omaha to invest in stocks. He had vowed to be a millionaire by the time he was 30 but had to wait until he was 31. When he was 34, he acquired his first significant business, an obscure textile mill called Berkshire Hathaway.

So much wealth so soon could have fatally inflated Buffett's ego. But Jonathan Davis, editor of *Independent Investor* and a regular *Financial Times* columnist, says Buffett turned his wealth into a competitive edge: "Buffett is a long term investor. Many people say they're long term investors but if you're working for a mutual fund, you can't be. The nature of long-term investments is that you have a bad year or two along the way – if that happens at a mutual fund you lose customers or your job. But Buffett soon got into a position where he was rich enough, and had enough control, to invest for long-term value."

Buffett's success as an investor owes a lot to shrewd use of the funds generated by his insurance companies. "He's careful what risks he insures against," says Davis. "But if those companies are performing well, the cash they generate is effectively free capital for him."

The supreme capitalist

Long-term value investing sounds absurdly simple but David L. Ikenberry, professor of finance at the University of Illinois's College of Business, says: "CEOs at a lot of public companies might want to think long term but they often focus on top-line growth in sales or market share. That doesn't resonate with Buffett. What he understands – probably better than almost anyone – is the equation between the cost of capital and the return on capital. So he studies the figures, and if that equation doesn't add up, he has the discipline to walk away."

That focus helps Buffett. "He really is one of those people who, if you ask him to buy your company, will say 'I'll ring you back in 30 minutes' and will call you back and give you a decision," says Davis. Microsoft founder Bill Gates says: "You can describe a business to Warren in ten minutes and he'll know the questions to ask."

Buffett only needs ten minutes because he has

Ben Baker/Redux/Eyevine

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What's next?

1 Buffett's US$44bn (€32bn) purchase of Burlington Northern Santa Fe is an indirect wager that the price of commodities and energy will rise, the dollar will weaken and that China will use much more coal – which Burlington Northern ships. The US$10bn (€7.3bn) debt from this deal may deter other bold moves in 2010.

2 He has reinvested in healthcare and pharmaceutical giant Johnson & Johnson and bought a million shares in medical device firm Beckton Dickinson, so healthcare may be a new focus.

3 Buffett has bought more shares in Wal-Mart, Dow Chemical and Nestlé and owns 9.4% of Kraft. He owns 4.5% of Korean steelmaker Posco and may seek other bargains there.

4 His US$5bn (€3.7bn) rescue of Goldman Sachs is a classic Buffet deal. As with American Express and Coke, he moved in when market sentiment was against his target and struck a deal that effectively insures him against any major loss.

"Buffett understands the equation between the cost of capital and return on capital better than almost anyone. If that equation doesn't add up, he has the discipline to walk away"

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Buffett's icons

Mae West
Buffet often quotes the original blonde bombshell. He recently chastised himself for losing focus on the basics with her one-liner: "I was Snow White, but I drifted".

American Express
Buffett looks for big demographic shifts. In 1963, he first invested in American Express, anticipating a massive shift to credit card use in America. His next such move may well be healthcare.

Candy
"Never buy a business with a price in mind," is Buffett's motto. He bought confectionery firm See Candy in 1972 for US$25m (€18m). Some buyers might have sold it soon after at a profit but by 1998, it was generating more than twice its purchase price in annual profits – and required no extra capital.

The Sistine Chapel
Buffett likens his job to painting the ceiling of the Sistine Chapel. Buffett likes to buy firms whose owners, like Michelangelo, "love what they do".

probably already done his homework. He is a voracious reader – of the *Wall Street Journal*, *Moody's Manual of Industrial and Miscellaneous Securities* and annual reports (he studies the footnotes and extraordinary items meticulously). In 2005, deciding South Korea was better value than Wall Street, he learned the Korean accounting code and leafed through a stock market guide for five hours (reviewing 1,700 firms) to create a US$100m (€73m) portfolio of stocks.

Through exhaustive research and tireless networking, Buffett probably knows the back story of every U.S. company he might invest in. With typical homespun wisdom, Buffett once explained his modus operandi: "If I get interested in an industry, I like to go in and ask every CEO: 'If you could put a silver bullet through the head of one competitor, who would you choose and why?"

Buffett can decide quickly because he relies on criteria identified in chapters eight and 20 of *The Intelligent Investor* and Berkshire Hathaway's annual report. In chapter 20, Graham urges investors to consider the margin of safety. Or, as Buffett once put it: "Don't buy a company for $80m if it's worth $83m." Ikenberry says Buffett's childhood reinforced this lesson. "A lot of entrepreneurs who were born in the Great Depression are debt averse. They saw the damage risk and debt can do." Before buying a stock or a company, Buffett rehearses a short sentence in his head: "I'm buying this because…" If he can't finish that sentence, he walks away.

Walking away is one of the secrets of Buffett's success. As he said once: "The disadvantage of being in a type of market environment like Wall Street in the extremes is you get over-stimulated." Wall Street makes its money on activity, but as an investor – and acquirer – it often pays to be inactive. Gerald S. Martin, associate professor of finance at the Kogod School of Business at American University, says managers could learn from him: "Buffett shows that it pays to be pragmatic and cautious. Many CEOs will enter into a transaction and get so wrapped up in it that it becomes a self-fulfilling prophecy. They won't walk away from it when they should."

> *"Only evaluate companies within your circle of competence. The size of that circle isn't vital. But knowing its boundaries is"*

The companies Buffett buys look very different – they make lollipops, run trains and sell insurance – but they resemble each other in crucial ways. They are run by owner/managers Buffett trusts ("If I could make US$100m with a guy who makes my stomach churn, I wouldn't do it – it'd be like marrying for money"), have little debt, generate capital, consistently grow earnings-per-share (ideally, with a gross profit margin of around 40%) and have a durable competitive advantage ("a moat" as Buffett calls it). As an investor, he likes stocks such as American Express, Coca-Cola and Procter & Gamble that have a grip on their customers' imaginations (or, to use his phrase, "a share of mind").

Buffett's credo is: "You only have to be able to evaluate companies within your circle of competence. The size of that circle isn't important, knowing its boundaries is vital." So he focuses on banking, insurance and manufacturing. Ikenberry says: "He doesn't invest in technology companies or businesses with strong intellectual property where it's hard to accurately value the assets."

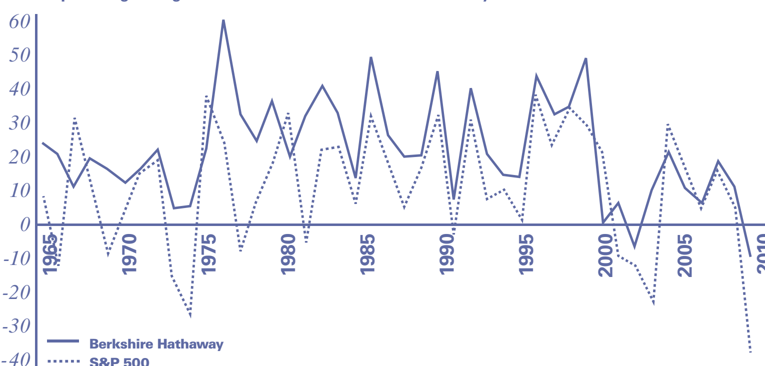
The vindicated dinosaur

This strategy cost him dear in the 1999 dot com boom. At one point, a digital business making a US$9m (€6.6m) loss on sales of US$13m (€9.6m) enjoyed a market value of US$21.4bn (€15.8bn). Shunning such stocks, Buffett was derided as a dinosaur. Berkshire Hathaway shares rose by 20.5% less than Standard & Poor's index of America's top 500 listed companies. But Buffett stuck to his guns – and was vindicated as boom

Taking stock of Buffett

How his shares have outperformed the crowd

Annual percentage change in share values. Source: Berkshire Hathaway



Since 1965, Berkshire Hathaway's share value has consistently outperformed the Standard & Poor's 500 companies. In 1999, when Buffett shunned tech stocks, shares lagged the S&P 500 by 20.5% – and then the dot com bubble burst. Between 1965 and 2008, BH shares rose by an average of 20.3% a year, compared to 8.9% for the S&P 500.

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For a man who makes millions on Wall Street, Buffett is surprisingly open about his strategies and secrets

Pictorial Press/Alamy, Ed Freeman/Getty Images, Ben Baker/Redux/Eyevine

turned to bust. Buffett's stand proved the value – and difficulty – of value investing. As one analyst noted: "Most investors find it painful psychologically to buy stock no one else wants." Or, indeed, to ignore stocks that, by any rational yardstick, are horrendously over-valued.

Buffett's reputation as the Sage of Omaha has survived the dot com bubble (he invested in bonds and made a mint) and the credit crunch. Both disasters, for him, proved Graham's adage: "You can get into way more trouble with a good idea than a bad one because you forget the idea has limits." As early as 2001, after concluding that soaring U.S. stock prices could not be justified by any rational assessment of corporate profits or America's GDP, he felt that buying businesses often offered better value than stocks.

His management style suits austere times. Don Graham, chairman of the Washington Post, says: "There's no VP of PR, no VP of strategy, no VP of anything. Berkshire has fewer than 20 staff at its HQ. The next company with that many staff at HQ is probably outside the Fortune 1,000." But he doesn't need a big HQ because, Martin says: "He likes good managers who don't need micromanaging and gives them the capital they need to make a good business grow."

The inconsistent sage

The beauty of being a sage is that the aura can obscure occasional inconsistencies. Buffett is a long-term value investor but, paradoxically, as Martin says: "His annual returns from short-term risk arbitrage transactions have been great. But he only engages in risk arbitrage when the right opportunities are presented."

That aura has come in especially useful since he took on US$10bn (€7.6bn) of debt to clinch his largest ever deal, the takeover of railroad giant Burlington Northern. Some debt for a man who, in 1998, boasted: "I never borrowed money, even when I had US$10,000."

The deal concluded Buffett's two-year quest for what he called an "elephant acquisition". Davis says: "Berkshire Hathaway is so big there are relatively few companies it can acquire that would make a real difference." Absorbing Burlington Northern will take time, which is why Martin says: "He may take a breather. He always wants to know there's enough capital in case of emergency."

Burlington Northern suggests his appetite for risk has grown just as almost everyone else's has shrunk. The contradiction is typical of Buffett. The railroad deal and his bold investment in Chinese electric car maker BYD are long-term wagers on a big trend – the environment – and on businesses he believes have a "moat". Neither deal will be his last. He is eyeing up healthcare (see panel on p13) and his scouting for acquisitions and stocks is global: "His motto is 'it's got to be good value,'" says Martin, "and inside the U.S. it can be hard to find good prices."

The young Buffett had many advantages: an entrepreneurial spirit, a brilliant mentor and a small fortune. But the truly shocking aspect of his journey from millionaire speculator to billionaire folk hero is that there is no magic to it, just an extraordinary understanding of value and capital. It's not hard to say what Buffet does, the hard bit is understanding why more people don't do it. Buffett's success suggests more CEOs should have the guts to be misunderstood. As he said once: "If you're applauded, worry. Great moves are usually greeted by yawns." ●

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Time to reinvent the multinational

If you haven't seriously debated how emerging economies have revolutionized your industry, your business model might be obsolete. Time for a strategic rethink

BY WILLIAM J. HOLSTEIN

Karl Marx was right in a way. A spectre is haunting capitalism – just not the one he imagined. Instead of a proletarian uprising, managers of the world's largest corporations are wrestling with a different kind of revolution: the fact that the vast majority of their employees, sales and facilities are outside their home country. In a global economy that has recently given violent, conclusive proof of its volatility, their ability to manage their sprawling organizations is under threat.

Call it the next fundamental evolution of the multinational. Once the quintessential U.S. corporate, IBM now employs about two thirds of its 400,000 staff outside the U.S. and generates about two thirds of its sales overseas. IBM headquarters in Armonk, New York, cannot make every decision in a company that operates 24/7 around the globe. In a rethink of its management structure, in 2008 IBM lumped all its business in emerging markets (Latin America, Eastern Europe and Asia) into one organization headquartered in Shanghai. "We're trying to lower our center of gravity," says Michael Markovits, IBM vice president of business and technical leadership. That is IBM-speak for devolving decision-making from head office. "We're saying, 'Let's try to get decisions made as close to the customer as we possibly can'," says Markovits. "We're trying to shift our culture from command and control from New York to empowering local leaders to make decisions."

"Brand owners collect most of the profit in an industry. And companies like Haier are going after the large sums flowing to the brand owners"

Multinationals have operated in many countries for decades, with varying degrees of decentralization. But surging sales in geographically distant (from the U.S.) and culturally distinct countries such as China and India pose a far more complex challenge than, say, a German-based multinational operating in France. When overseas markets account for 80% of sales, as is the case for Coca-Cola, a company's center of gravity can undergo a wrenching shift.

Established multinationals also face a tough new breed of competitor: companies based in India, Brazil and China that aim to dominate their home markets and expand globally. China's Haier is now the world's fourth largest manufacturer of white goods, while Brazil's Embraer – once a regional manufacturing powerhouse – derives 93% of its US$3.8bn (€2.5bn) annual aerospace sales from outside Brazil.

"In some markets – like fast moving consumer goods – the worry isn't that companies from China and India will make inroads into Europe and North America," says Martin Scott, Partner, Transaction Services, KPMG in the UK. "I can't see, for example, an Indian food company suddenly taking over the U.S. soup market. What multinationals do need to worry about is that if their markets are saturated and static in Europe and North America, and their five- or 10-year growth plan sees them growing strongly in India, Brazil or China, they need to make sure they structure themselves to be successful in those countries.

"They will be competing head-to-head for sales and growth against very strong local players in those enormous markets. If your thinking is driven by Europe and North America, will that work in emerging economies?"

Geoff Colvin, *Fortune* writer and author of *The Upside Of the Downturn* says the challenge is especially acute for businesses with powerful brands: "Brand owners typically collect most of the profit in an industry. Until now, developing economies have been happy to cash in on their labor cost advantage. Now companies like Haier and Lenovo are going after the enormously larger sums that are flowing to the brand owners."

Back to the core

Remaking organizational charts, as IBM did, is only part of the response to this new era. The way organizations are structured will need to be reconsidered, corporate cultures and HR policies need to be revolutionized and CEOs need to reflect on how the emerging economies will affect their core business.

In good times, Colvin suggests, businesses often forget what their core is. It can take a downturn or a market-redefining competitive threat to focus leaders. Japanese audio and electronics group Pioneer has already redefined its core, leaving the flat-screen TV market, where low-cost competition from China is fierce, allowing it to run its DVD business with Sharp and focus on audio.

As firms restructure, they need to place the corporation's assets where its business is, and redefine its boundaries. Focusing on core

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Plane dealer

Aviation may have hit unexpected turbulence but Brazilian aerospace group Embraer is to pitch for United Airlines business after a hefty loan from China

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Global shifts

Pundits agree China will become the world's largest economy. They're just not sure how soon

1895
U.S. replaces China as world's largest economy

2009
China replaces Germany as the No 3 economy

2015
Geoff Colvin says China could be the largest economy

2050
Will China, the U.S. and India form the top three?

Olympian feet

Fresh from an ambush marketing triumph at the 2008 Olympics, athlete and sports good giant Li Ning wants to be China's first truly global brand

competencies and making shrewd use of outsourcing, leaders are examining their value chains to see where they have competitive advantage and where they do not.

"Being vertically integrated through a value chain probably isn't the best way to run your business," says Scott. "It's very hard to make stuff, distribute it and sell it all at once. You might say, 'other people are better at transactional finance, so let them do it'."

Advanced Micro Devices has taken the radical step of spinning off its semiconductor manufacturing arm into a separate unit, Globalfounders, which it now has a minority stake in and runs as a joint venture with an Abu Dhabi investor.

The rationale behind outsourcing is changing. as KPMG's Scott says: "An outsourced unit in India makes sense when it's dirt cheap to do something there. But there's a growth in wage expectations in these countries – the economy rises and wages rise. Also, once everybody's done it, you lose your advantage, particularly when everyone's done it in a country where you're investing and growing. If you're expanding in India, there's now no real advantage to outsourcing your finance function there."

> *"We're trying to lower our center of gravity. We want key sellers to come together locally. But you can't delegate haphazardly"*

Out of control?

Decades ago, global companies created largely self-sustaining subsidiaries in different countries. Country managers wielded enormous power. As offshore sales boomed, multinationals created regional management structures to move ideas and people around a region, while making all the big decisions at headquarters. Strategy and execution were often driven by managers trained in the U.S. business style, with limited insight into global markets. The recurring tendency for product names and slogans to translate bizarrely into other languages suggests that many heads of overseas sales reluctantly decide it is easier to ignore the market than take on head office.

The shift in global sales puts centralized decision-making under pressure. In IBM's case, its emerging markets HQ in Shanghai (run by a Latin American) helps various divisions – services, software and hardware – combine to win sales in emerging markets. "We want key sellers for software, services and hardware to come together locally – and decide locally," says Markovits. Shanghai handles smaller deals, larger transactions percolate up to Armonk.

IBMers team up across the world to win deals. This diversified decision-making relies on an internal computerized system that lists employees with key skills. An IBM engineer in Bangalore can find a colleague in Sydney who has the exact right knowledge.

This approach cuts across traditional demarcations, hierarchies and 'command and control' management styles, so companies need new kinds of leaders and, in some cases, new models of organization to succeed.

This realization struck Johnson & Johnson, the healthcare, pharma and consumer goods giant, as long ago as 1922, when Robert Wood Johnson II – son of one of the group's founders – toured the world to see if U.S. isolationism might hurt exports. His trip convinced him that decentralization was key. With 250 firms selling

Paul Gilham, Goh Chai Hin/AFP/Getty Images

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products in 175 countries, Johnson & Johnson has stayed decentralized but, with sales growing for 75 out of the last 76 years, why change? The company attributes its success to strong local managers with deep knowledge of their markets.

"To be comfortable delegating decisions, we have to do a good job of developing leaders in those locations," Markovits says. "You don't want to delegate haphazardly to people who can't handle the authority they're being given."

The new talent war

This realization is changing the face of the multinational. Companies like Colgate-Palmolive are devising systems to nurture far more local talent – and develop that talent by moving it to headquarters. Firms such as Alcoa, Coca-Cola and Pepsi are hiring non-Americans as CEOs, believing they will have a deeper grasp of global markets.

A survey by the Association of Executive Search Consultants (AESC) found that only 12% of headhunters in China, India, Brazil, the Middle East and Russia feel expatriates account for the greatest supply of talent, compared with 56% a decade ago. "We're seeing huge, explosive growth in demand for executive talent from local and multinational firms in emerging markets," says AESC president Peter Felix. Companies are scouring the globe for high-flying Chinese, Indians and Russians who have trained and worked abroad and want to return home. Felix says the ability to hire the best managers may decide who prevails in the multinational business wars.

It's hard for multinationals to groom talent from other countries, especially when cultures are very different. It takes years to identify gifted offshore staff and develop them. Sometimes, firms have to change their cultural norms to properly assess these executives, while head office culture may need to become more diverse as different nationalities join the team.

John Wood, a headhunter who worked with Colgate-Palmolive, which generates 75% of sales outside the U.S., says the group "encourages, rewards, moves around, provides incentives, and closely manages the careers of the best performers worldwide, no matter what their national origin".

Since 2007, Colgate-Palmolive has been run by an Englishman, CEO Ian Cook, while eight out of nine of its brains trust of top operating executives – and more than half its 200 senior managers – were not born in the U.S. The group has made senior managers accountable for identifying and nurturing high-potential employees from around the world. Linking it to dollars and cents is key. Long-term incentive compensation for those 200 managers rises if the company keeps 90% of its high-potential staff over a certain period.

If managements become truly globalized and 80% of sales are outside their 'home' country, will this affect the very identity of the company? KPMG's Scott suggests that global corporations should examine the fundamentals of where they are located. "The model of having a regional headquarters in North America, one in Europe, and one in Asia – a typical arrangement, no matter where the ultimate corporate brain is located – isn't necessarily the only way. If I'm growing like crazy in South America, shouldn't I be relocating there?", he asks.

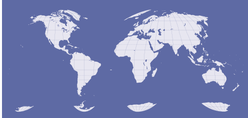
Do we need to reconsider the question of a traditional head office? Should, for example, sales be located in major markets, R&D near relevant research bodies and the CEO/CFO next to a key financial hub? There is speculation that some major Western companies may shift head office to China or India. None have yet said so in public but *Business Week* says one mid-sized global corporate is to move its leadership from Europe to Singapore, "to look through the Asian end of the telescope".

The challenge goes beyond personnel and location, cutting across the structure of the organization, its systems, its people and its boundaries. The question is, who will flourish in this new global corporate landscape? It may not quite be a Marxist revolution, but the CEOs of these multinationals are inventing the future. ●

William Holstein is a respected journalist and author who has covered the stateless corporation for Business Week *(see www.williamjholstein.com).*

Haier love

In the 1990s, Haier was the most recognized brand in China. By 2009, it had become the world's fourth largest white goods group



The core questions

1 Will the emerging economies restructure your industry? If so, is your strategy threatened by abrupt shifts in price, costs or technology?

2 How globally diverse is your senior management team? Only 39 of Fortune 500 CEOs were from outside the U.S. in 2009 – and ten of those were from just across the border in Canada. There were no Chinese CEOs and only five from India.

3 How close to your customers are you making decisions? No CEO has the depth of knowledge to make every decision. Consider devolving responsibility to the markets – and basing your head office, production or sales nearer customers or clusters of knowledge. In the 1990s, GM located small car design in Korea and small trucks in Brazil.

4 How flexible is your approach to emerging markets? Joint ventures, alliances and co-creation can help companies enter China and India. The 'launch or acquire' model may be risky and costly.

5 How does your quality compare to rivals in emerging markets? The Milan fashion house Ermenegildo Zegna found some fake Zegna wool cloth in China and was astounded by the quality. Your advantage in quality may not be as great as you'd like to think.

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What's Rupert's secret?

Media mogul Rupert Murdoch's career is a masterclass in the art of successful acquisition, which every CEO can learn from

BY ROBERT JEFFERY

Memorable Murdoch deals

■ **20th Century Fox**
News Corp paid US$575m (€380m) for the studio in 1985; in 2006, it was valued at US$11.7bn (€7.7bn) after a string of hits including *Titanic*, then the highest-grossing film ever made.

■ ***The Sun***
The UK tabloid was losing US$5m (€3.3m) a year when Murdoch bought it in 1969; 40 years on, it is the country's biggest selling daily newspaper.

■ **DirecTV**
News Corp's 34% stake in the cable operator cost US$6bn (€4bn) in 2003; profits for 2008 hit US$9.6bn (€6.3bn).

■ **Dow Jones**
The *Wall Street Journal* was the media asset Murdoch most wanted. He bought the media group with his first bid – US$5bn (€3.3bn), 30% more than many analysts said it was worth – and believes that, as the economy recovers, the price will prove a bargain.

If Rupert Murdoch had never bought a business, he might still be running Queensland's largest newspaper group. But he acquired his first company, Australia's Channel 9 TV station, in 1959 and as News Corporation's chairman and CEO has probably been the consummate corporate dealmaker of his day, with a particular genius for bold, transformative moves that take his business into an utterly new market or territory.

As News Corp's Q3 2009 results show – profits were US$25m (€16.6m), down $109m (€72.4m) year-on-year – Murdoch's empire faces some big challenges, notably the digital assault on traditional media ad revenues and the value of newspaper editorial, but as M&A activity creeps up, CEOs could do worse than learn from him.

Murdoch's acquisitions can look purely opportunistic but there's a strategy behind the hunches. His biographer Michael Wolff describes his forays into U.S. markets – including his purchases of 20th Century Fox and the Metromedia chain of TV stations in the early 1980s and the US$5.6bn (€3.7m) swoop for Dow Jones (which owns the *Wall Street Journal*) in 2007 – as "a set of brilliantly executed strategic moves that occurred mostly without any kind of analysis about why he might be buying and what he would be getting."

He was introduced to game theory at Oxford University by Robin Farquharson, one of its early proponents, and likes to think many moves ahead. His confidence in his own judgement has meant he has not been afraid to pay top dollar and, as unfashionable as this may now be, to take on debt. But thinking moves ahead helps maximize value. His 1969 purchase of the *News Of The World*, the British Sunday newspaper, made more sense when he bought the loss-making daily *The Sun*, turned it around and, a decade later, invested the profits, in the upmarket *The Times* and *The Sunday Times*. He transformed the entire business's profits by abolishing restrictive labor practices in 1986 and used the funds to back his biggest gamble: making Fox the fourth major U.S. TV network. "People claim to have ten-year plans but successful businesses are opportunistic and you take opportunities when they come," he says.

Murdoch is usually an all-or-nothing buyer, rarely content to take a minority stake. When he made his first U.S market acquisition – a Texan newspaper in 1973 – he rebuked two execs who had failed to seal the deal: "I didn't send you to negotiate. I sent you to buy the paper," they were told. When it tried to buy DirecTV in 2003 – the key to his entry into the U.S. satellite TV market – News Corp was outbid by EchoStar. Murdoch left a congratulatory message with EchoStar chairman Charles Ergen, then lobbied regulators to block his rival so he could step in.

He patiently courts targets years before he makes a bid. News Corp lieutenants met with the Bancroft family, who controlled Dow Jones, a decade before his takeover. Some bidders talk of merging cultures with acquired companies. Murdoch's instinctive preference – with the notable exception of MySpace – has been to get his own people in position to evaluate the business from inside.

Murdoch derides his own acumen – "I am sober after lunch and in some parts of Fleet Street, that makes you a genius," he said once – and because he never waxes strategic in public, he is easy to underrate. Barry Diller, who ran Fox for him, says: "He is at his best when he is cornered or in great adversity." He faces such adversity now as he strives to make two recent mega-deals – Dow Jones and MySpace – pay off. His record suggests only a fool would bet against him. ●

AP Photo/Mark Lennihan

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JFK's taxing paradox

As politicians wrestle with unprecedented levels of government debt, they might want to heed a speech America's most charismatic president gave in 1962

BY WALTER HALE

As the son of a maverick tycoon, John F. Kennedy didn't have much time for businessmen. "My father always told me they were sons of bitches," he said once. But as president, he understood their economic importance. And, in December 1962, he told an audience of business leaders in New York that the soundest way to raise tax revenue is to cut taxes. This was an unusual stance for a liberal, Democratic president. JFK's economic guru, J.K. Galbraith, wanted him to spend more government money. But Kennedy focused on taxes (though he did spend billions through the Apollo space programme) believing this would "cut the fetters which hold back private spending". His proposed cut in personal and corporate tax, equivalent to 2% of GDP, became law after he was assassinated.

Kennedy's paradox has not been lost on officials in the Swiss town of Zug. In 2008, 1,200 companies set up here. An economy once reliant on farming is buoyed by an unlikely oil boom: 13% of full-time jobs are in the raw materials sector. Corporate tax of 9.5-16% (the global average is 25%) has attracted firms from such tax havens as Bermuda to Switzerland, with offshore drillers Noble and Transocean and engineering group Foster Wheeler planning to move there.

Cutting taxes to raise revenues sounds too paradoxically neat to be true. But it is the strategy most governments have applied to corporate tax: since 1982, KPMG's Corporate and Indirect Tax Rate Survey 2009 says, the global rate has fallen from 46% to 25.5%. Confederation of British Industry (CBI) research suggests that policy makers hoping to trim deficits by taxing business ignore Kennedy at their peril. The most famous Irish-American president's advice has been heeded in the land of his forefathers. The Irish government gradually cut corporation tax from 50% in 1985 to 12.5% in 2003. By then, the Celtic Tiger had attracted more U.S. investment than Brazil, Russia, India and China combined. Between 1995 and 2005, the tax burden as a percentage of Irish GDP fell from 32.9% to 30.6%, although economic woes have since led it to raise VAT to 21.5% (the EC average is 19.8%). In France and the UK, where the tax burden accounted for a greater share of GDP, growth rates were 75% and 60% smaller than Ireland's, according to the CBI. The Irish experience has been mirrored in many east European and central Asian countries.

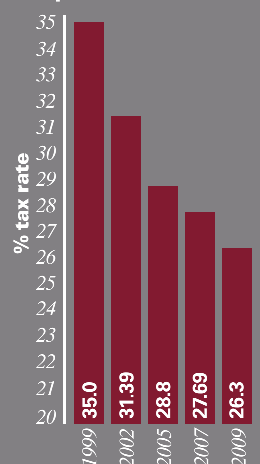
Corbis

JFK did not fret unduly about foreign direct investment (FDI). Today, no finance ministry can ignore this kind of investment: even the U.S. attracts 284 times more FDI now than in the 1960s. And companies are much more likely to emulate ad giant WPP, which will save tens of millions of dollars a year by paying tax in Ireland, and move head office to cut their tax bills.

None of this makes comfortable reading for finance ministers struggling to balance the books. They may prefer to maintain the headline corporate tax rate – while closing loopholes, limiting deductibility and targeting abuse – and raise indirect taxes. Governments will still chase FDI by offering incentives (like R&D credits) even if, as Zug's success suggests, a lower headline rate of tax might attract more business.

CFOs will have to become adept futurists and readers between the lines as politicians ponder tax policies. It is easy to blame politicians for not being honest, but in the 1988 presidential campaign George Bush Sr knew that "Read my lips, no new taxes" would win more votes than the admission that such taxes might be needed to balance the budget. As governments seek to emerge from the valley of debt, the only certainty when it comes to corporate tax burden, to use a paradox worthy of JFK, is that nothing is certain. ●

OECD Average Corporate Tax Rate



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With the business landscape changing by the day, here are ten challenges to prioritize in 2010

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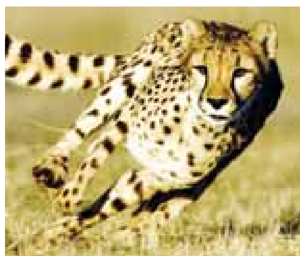

1

Speed sourcing

You would like to outsource part of your business, but need a return in four months, not nine. What can you do? Some firms are trying a revved up, slimmed down strategy called 'speed sourcing'. It isn't for the risk-averse, but the principles involved could help any CFO.

Instead of exhaustively reviewing every supplier, you focus only on companies in the very top tier or those who specialize in your sector. Instead of a detailed tender document, you issue a succinct 'request for services' which gives the essential info about your business and goal.

Suppliers then respond with a high-level pitch and, after a quick series of negotiations, a contract that focuses only on must-haves (key conditions, price, timeline, liability) is signed. One Fortune 500 clothing group which used this process outsourced some services in less than half the time it normally took.

For some, the risk of such a strategy is too great. Others fear that speed sourcing may leave buyers and suppliers with fatally different expectations. Still, with estimates suggesting 70% of IT outsourcing deals are renegotiated within two years, the standard approach isn't working that well.

2

IFRS as an opportunity

The next wave of IFRS adoptions in locations such as the U.S., Japan and India brings us one step closer to a single set of high-quality global accounting standards, but only smart CFOs will recognize that the benefits of IFRS can more than outweigh the costs of conversion.

"IFRS conversion can be a catalyst to help reshape the entire finance function and its people," says Gary Reader, who leads KPMG's Global IFRS initiative. "For instance, it can help improve the quality of the reporting process. A new global accounting language can emerge, which can help geographically disparate business units to work together more closely."

Similarly, Oracle CFO Jeff Epstein advises: "Waiting until the last minute is not sensible; our strategy has been to 'Simplify, Standardize, Centralize and Automate' and we've continued to do that as we've begun to adopt IFRS."

Understanding the accounting impact is essential but you also need to get to grips with the necessary changes to the systems, processes and people. The wider business impacts are likely to be more far reaching than you imagined.

3

Smarter logistics

Why pay all the time for a product you only use 70% of the time? Performance-based logistics (PBL), or 'power by the hour', offers a way out of this conundrum.

With PBL, suppliers are compensated for actual product performance, not the promise of efficiency or savings. Such tightly defined contracts help buyers control costs and maximise value.

The defense and aerospace sectors have already discovered the benefits. Every time the U.S. Department of Defense buys a jet or stealth bomber (above) from Lockheed Martin, it pays not for the physical product, but for how often it can fly. The department saves US$5m (€3.4m) on every PBL contract which is why, in 2009, it spent US$5bn (€3.4bn) through such deals. Some U.S. states – notably Florida and Maine – have begun using this approach.

For PBL to work, both sides need to agree how to measure performance. Serguei Netessine, associate professor of operations and information management at the Wharton School, says this represents what he calls "servicization: transforming the business from just buying parts and products to procuring services".

Martin Harvey/Gallo Images/Getty Images; Time Life Pictures/Department Of Defense (DOD)/Getty Images

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4

Is reverse innovation the way forward?

Developing in emerging markets first is an enticing strategy for multinationals

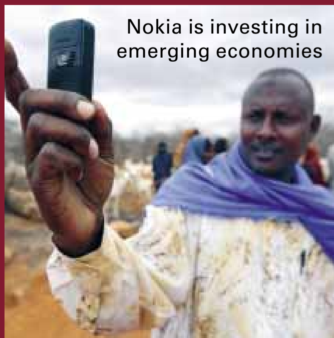
Globalization has traditionally been quite simple: innovate in the West and ship your products out to emerging markets. When U.S. companies moved into Europe or Japan, they found a customer base similar to their domestic one, which meant it was easy to adapt existing products. But emerging markets like China and India are now a significant force, and that means multinationals must radically alter their mindsets.

The middle class in India or China is fundamentally different to its American equivalent. The average per capita income of the Indian middle class is US$1,000 (€700); in the U.S. it's US$40,000 (€28,000). There's no product you can create for the West that you can simply adapt for India.

Reverse innovation offers an answer. It means focusing on customers in emerging markets – and their problems – first. By innovating and introducing products in emerging markets, they become applicable to developed nations too. When General Electric created a backpack-sized, low-cost ultrasound machine for rural China, it had to shift its centre of gravity. As well as development and manufacturing resources in China, it needed a strategic marketing capability there. It worked, and the product is now used in the West too.

The biggest challenge is organizational: if you can't get that right, you can make a mess both of your existing innovation and reverse innovation. The first step is establishing internally that emerging markets are a strategic priority. The CEO needs to visit those markets to see the challenges and opportunities. Next comes the courage to invest resources in emerging markets, with effective devolution of power.

GE, Unilever, Procter & Gamble and Nokia are already making reverse innovation a priority. But it will affect everyone eventually and will fundamentally reinvent the nature of multinationals.


Nokia is investing in emerging economies

By Vijay Govindarajan (www.vijaygovindarajan.com), professor of international business and director of the centre for global leadership at the Tuck School of Business at Dartmouth College, U.S.

5

Filthy business

Blame Gordon Gekko. Or the business leaders who behaved like reptiles.

With around 7% of the global workforce unemployed, employers should be fishing in a deeper pool of talent. Yet more than 50% of global corporations surveyed by finance recruitment specialists Robert Half said finding good staff has got harder after the credit crunch.

Demographics aren't helping. Firms that pay lip service to diversity may struggle as African-American, Asian and Hispanic communities account for 65% of U.S. population growth – but former General Electric chief Jack Welch believes the real problem is the scandals that have dented business's image: "Many people have come to the conclusion they just don't want to work for 'the man' anymore."

Many laid-off staff are reluctant to return to the corporate treadmill, while those in work may be discontented – the UK's Voluntary Service Overseas says 14% of British workers are considering a career break – and Welch says wooing recruits with better benefits and a more serious commitment to employee engagement will be key.

6

Software management

Do you know if all your software licenses are up to date – or whether they are being used? The cost of ignorance can be high. One U.S. firm was fined a six-figure sum after licenses lapsed on its design software, but surveys suggest that 72% of American businesses either track their software licenses manually or not at all.

With licenses, upgrades and vendor support accounting for up to 25-35% of total IT spend, many companies are asking third parties to conduct software audits or manage licenses.

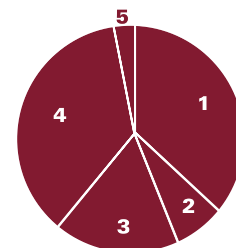
Edge Zarrella, head of KPMG's IT Advisory practice, says vendors are getting tough on non-compliance: "For companies with 20,000-100,000 seats, software management is a massive issue. Breach of license can be very serious."

Zarrella says auditing is the solution and, even if it is outsourced, should be the responsibility of a specific department or person.

The rise in outsourcing

Corporations' software management plans for 2010

Source: Forrester Research



1 *Currently outsourcing: 37%*
2 *Will outsource in next 12 months: 7%*
3 *Interested/considering: 17%*
4 *Not outsourcing or n/a: 36%*
5 *Don't know: 3%*

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7 Changing habits

Lord Melbourne, Queen Victoria's favorite prime minister, once noted that: "When it is not necessary to change, it is necessary not to change." In a world where leaders and companies are valued for sheer dynamism, this message is often lost. Fiona McLeod, who has led change management programs within BP for 20 years, asks: "How do we cure ourselves of our addiction to episodic change and move to a much more healthy culture of business improvement?"

One Economist Intelligence Unit survey found that 70% of managers didn't know how to measure if changes had succeeded. Some are so excited by the dramatic 'big splash' they lose interest in the follow-through. A credulous few go 'fad surfing' – applying fashionable theories rather than focusing on real issues.

It is useful to have a powerful symbol of change. When Gordon Bethune took over as CEO of Continental Airlines in 1994, managers feared that employees wanted to kill them. He broke the distrust with a pledge: for each month Continental was in the top three U.S. airlines for punctuality, he would pay a bonus. In ten years, the share price soared by 2,500%.

8 Virtual managers

You have the technology to manage a mobile workforce, but do you have the mindset? Mark Smith, a partner in KPMG's People & Change practice, says: "A mobile workforce demands a new management structure. You can't run things the same way as you do in an office."

Yet the rewards are great. A 2009 survey of 502 U.S. businesses by Cisco found that 62% of those whose staff use remote access said it had boosted productivity and 42% said it had cut overheads.

Smith says it is easy to overlook the HR issues: "With virtual teams, you need a good formation meeting as you establish the workforce to set the tone, define processes and be clear about accountability.

"You need new roles – for example, a technical specialist – and to build ways to recognize achievement." The technology, Smith says, needn't be expensive: "Many clients told us they used webcams, not videoconferencing, to see facial expressions and communicate more clearly."

Executives steeped in 'presentism' can find it hard to coordinate without controlling and manage by results. But being a virtual manager is fast becoming an indispensable skill.

9 Transparent leaders

How many execs blog about laying people off? Glenn Kelman, the CEO of major U.S. real estate firm Redfin, did. His company's blog has also told the world about its website crashing and about finding a torture chamber in the basement of a mansion it was selling.

Thanks to social networking, transparency is in vogue and although Kelman's cult blog is more forthright than most, he's not alone. Microsoft encourages engineers to blog about their work, online retailer Zappos tells suppliers how much profit it makes on a particular line and Southwest Airlines has set up an online 'water cooler' where staff can post about any issue that vexes them. Even Washington DC is becoming more transparent after the non-profit Sunlight Foundation began posting millions of public documents in a searchable archive.

Kelman believes transparency is an essential skill for the new generation of leaders he calls CEO 2.0. Venture capitalists have begun asking CEOs how savvy they are at blogging and tweeting. But too much candor leaves you open to web critics and can send any slip-ups viral. Leaders should retain control of their brand, personal and corporate.

10 Just ask

When physicist Isidor Isaac Rabi won a Nobel Prize in the 1930s, he attributed it to the fact that when he came home from school his mother would say: "Did you ask any good questions today?"

She had a point. Business writer Gary Cohen suggests questioning is an essential skill for executives. He calls it 'Just Ask Leadership'. But interrogating in the style of a prosecution lawyer – determined to prove your version of events – won't bring genuine insight. Cohen argues that learning to ask open questions can improve vision, ensure accountability and create better decisions.

When Darwin Smith became CEO of Kimberly-Clark in 1971, he asked colleagues: "What could we be best at? What could we be passionate about? How could we improve our economic performance?" The answers led Smith to sell the core business – paper mills – for tying up too much capital. The stock plummeted, but by the 1980s, with Huggies nappies accounting for 23% of Kimberly-Clark's US$7bn (€4.7bn) annual sales, Smith's questions seemed astute.

As business guru Peter Drucker put it: "The leader of the past was the person who knew how to tell. The leader of the future will be the person who knew how to ask."

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INFRASTRUCTURE: ARE WE GETTING ANYWHERE?

Governments have spent too little on everything from roads to broadband. Three specialists discuss a crisis that is hurting business

BY ROBERT JEFFERY

No matter what your area of business, infrastructure is a global challenge that has rapidly become too big to ignore. The latest public investments will only partially ease concerns about ageing power systems, imperfect transport networks and inconsistent roll-out of broadband. A survey conducted for KPMG International, *Bridging the Global Infrastructure Gap*, found that 90% of C-class executives believe there will not be enough infrastructure investment to support the long-term growth of their organizations.

Agenda asked three specialists for their views on how deep the crisis is and whether government and business can help tackle it together: Pat Flaherty, senior vice president of infrastructure at project management giant Fluor Corp; Ryan Orr, executive director of the Centre for Collaboratory Research on Global Projects at Stanford University; and Nick Chism, Head of Global Infrastructure at KPMG and a Partner in the UK firm.

Has recent stimulus investment eased the infrastructure crisis?

Flaherty The stimulus packages have been intended to create employment and boost economic confidence in the near term. They haven't helped us down a path of sustained investment that would allow the delivery of strategic infrastructure.

Chism The stimulus marks the start of what will need to be the greatest period of infrastructure investment in history. The world is seeing the strains caused by rapid population growth, economic development and years of neglect by governments. In the U.S., transport infrastructure is failing and you've had energy blackouts. In India and China alone, more than a billion people are joining the global middle class and want to own cars and appliances and send their kids to good schools – all of which requires investment in infrastructure.

Does business have a big enough voice in the infrastructure debate?

Orr Executives understand that the cost of poor infrastructure is inventories and logistics costs that are 2-3 times higher in developing countries than the U.S. When businesses recognize that the delay getting goods out of a port is making their logistics 40% more expensive, it makes it possible to prioritize problem areas at national level.

Chism When we talk about failing infrastructure, we typically think of the personal dimension and forget the impact on business – so when the railways fail, we think of the impact on passengers more than freight. But in India, for example, 30% of food produced is lost before it can reach the public. Businesses increasingly worry about energy supply too. Things like that shouldn't be dismissed as selfish interests, because issues of productivity affect us all.

What are the most common mistakes when prioritizing infrastructure spend?

Orr Governments often do a terrible job of prioritizing projects. The U.S. government, for example, has no process for merit-based selection of projects. It selects projects either through a formula-based allocation, spreading money like peanut butter across the states, or through parochial politics and congressional earmarking. So we don't get the projects that offer the greatest social, environmental and economic benefit.

Flaherty There's often a lack of commitment and foresight until infrastructure availability becomes an economic burden. But given the scale of many programs, and the time taken for planning permission and delivery, procuring agencies often cannot commit to projects that might transcend political administrations. Even today, many government entities are funded on an annual basis, so they must spend in a budgeted year.

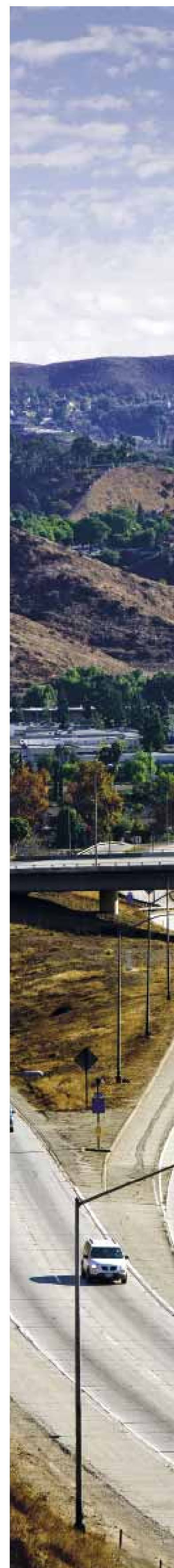
Chism Decision-making in government is geared to the short term. The governments who

The panel

NICK CHISM
KPMG's Head of Global Infrastructure and a Partner in the UK firm

PAT FLAHERTY
Senior vice president and business line lead for the infrastructure business at Fluor Corp, one of the world's largest engineering, construction and project management companies

RYAN ORR
Ryan Orr, executive director of the Centre for Collaboratory Research on Global Projects at Stanford University, examining the impact and management of infrastructure projects



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Ed Freeman/Getty Images

RAISING FUNDS
Although the credit crunch slowed growth, infrastructure funds operating on the secondary market still raised US$24.7bn (€17.5bn) in 2008 to take over or invest in existing PPP projects.

THE PRICE OF PROGRESS
A CIBC study says the world must spend US$35 trillion (€25 trillion) over the next 20 years to bring infrastructure up to scratch. The report blames cost-cutting on past construction projects and ballooning maintenance costs, especially in transport networks.

BUSINESS BURDEN
The cost to business of inadequate infrastructure is steepest in emerging economies. McKinsey predicts that India will miss out on US$200bn (€141bn) in GDP - and 35 million jobs – before 2018 if it fails to upgrade its infrastructure.

POWER GAMES
Two thirds of executives surveyed by KPMG reported that inadequate transport and power networks are increasing their operating costs, with dissatisfaction almost as likely in developed nations as emerging economies.

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Key projects

CHINA
Will invest US$586bn (€417bn); with 12 new highways, its 53,000-mile road network will overtake the U.S.

U.S.
High-speed rail will link Los Angeles and San Francisco in 2.5 hours and create more than 600,000 jobs at a cost of US$45bn (€31bn) a year.

UK
Wants wind farms to generate 25% of power by 2020, and is investing US$160bn (€112bn).

UAE
Abu Dhabi is putting US$1tn (€706bn) into infrastructure, including the new Khalifa City development.

AUSTRALIA
A new US$43bn (€30bn) broadband network is the country's biggest infrastructure project.

China is embarking on a huge investment in infrastructure

deliver infrastructure effectively think through the long-term consequences and get better value for money.

Which countries get it right?

Flaherty Countries with mature PPP programs – the UK, Europe, Canada and possibly Australia. In those countries, you can concentrate on being competitive because you know the projects will happen. Elsewhere, including in the U.S., there can be a lack of public support, political will and the right regulatory regime to deliver projects.

Chism China has an extremely impressive infrastructure with a good long-term vision. In India, infrastructure is the biggest factor holding back the economy.

Orr Chile and Australia have a good balance. The public sector uses the private sector to do the heavy lifting, but protects the public interest by ensuring the right projects go ahead.

It's often said that public-private partnerships(PPPs) under-deliver and ramp up cost. Is that true?

Flaherty Most countries with mature PPP programs can demonstrate a record of delivery that is at least as cost-effective as traditional methods of public service procurement.

Chism Most evidence suggests PPPs, used correctly, are a very effective form of procurement and offer value for money. They force you to take a whole-life approach. One reason PPPs get a bad press is that there's not much data on the comparable costs of traditional procurement. With PPP you get a tightly defined contract delivering consistent maintenance levels over the life of an asset. Because the records are transparent and the risks clearly defined, you might end up concluding a PPP hospital is more expensive than one that is built cheaply and poorly maintained. The test will be to visit them both in 30 years time.

Orr The private sector's cost to finance is often higher than the public sector, but a public-private delivery format transfers much of the risk to the private sector. And it doesn't mean the all-in cost to the taxpayer of PPP is higher – savings in delivery can offset the higher cost of finance.

Does the secondary market for infrastructure encourage cost-cutting and make delivery harder?

Orr Secondary buyers specialize in optimizing asset value. This can happen in two ways: actual cost-cutting, which drives up free cash flows, or revisiting the base financial model, reviewing assumptions and reworking the model so the cash flows appear more attractive. The first approach creates real value, the second is a bit sneaky.

Flaherty I don't think the private sector championed the involvement of financial ownership in projects. Governments were looking to get costs off balance sheet and secure private investment to deliver public infrastructure. The market allows new investors into the service delivery phase of PPP projects and provides the opportunity for new ideas and further innovation and efficiency.

Chism Governments alone cannot fund the US$40trn (€30 trn) of infrastructure required globally over the next generation. You need effective models for involving the private sector in infrastructure development, and you need pension funds and insurance companies, which value long-term, stable investments, to invest in operational infrastructure. A secondary market is inevitable and welcome.

"Governments do a terrible job of prioritizing projects… we don't get the social, economic and environmental benefit"

What trends in infrastructure investment do you expect to see?

Orr Infrastructure comes in waves, where new technology matures over 15-20 years and creates a strong value proposition for society. First it was aqueducts, canals, and ports, then roads, power and water and more recently airports, telecom, and fiber optics. The next wave will include renewable power, smart grid, and server farm technologies.

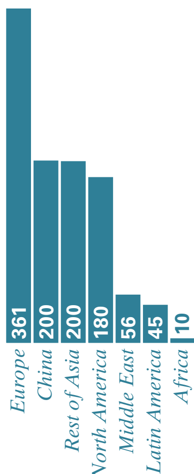
Flaherty If governments can follow up the stimuli with a sustained program of strategic investments that make cities and countries more competitive and desirable for investment, there's an opportunity to build on short-term actions.

Chism We face some major changes driven by demographics, developments in smart technology and the need to de-carbonize. Technology creates new infrastructure challenges – if electric cars are popularized, we will need charging points, for example. But in many parts of the world, people just want water, sanitation and electricity. ●

Thinking ahead

Estimated annual infrastructure spend to 2029 (US$bn)

Source: CIBC



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Nurture your profits

Cisco senior vice-president Chuck Robbins says a systematic approach to developing future leaders has generated billions of dollars in new opportunities

BY ROBERT JEFFERY

"We are going to attempt to become the best company in the world, and the best company for the world." Cisco Systems CEO John Chambers' bold mission statement requires the world's largest maker of communications equipment to clarify its strategy and develop new products as it expands into emerging economies and diversifies to offset slower growth in its core sectors.

Such goals could only be achieved if Cisco moved beyond box-ticking appraisals to find and nurture future leaders. "It's not about identifying weaknesses," says Chuck Robbins, senior vice-president, U.S. enterprise, commercial and Canada markets (pictured right). "It's about identifying strengths and getting those people into places where they can help each other."

Every employee's development is assessed annually – Cisco believes all its staff have the potential to become leaders – and bosses scour the business biannually for rising stars. Robbins says: "There are tons of people like me who've moved across the organization several times. It gives you better feedback. I might have a superstar on my team, but one of my peers could say 'he might be a superstar to you, but he doesn't work very well with us.' As we move faster, we need that kind of honesty."

Robbins says that traditional metrics such as P&L or sales targets don't always give a broad enough picture of the business's performance. "It's no longer just about delivering the numbers. Lots of people can do that every time, but they don't necessarily have the leadership capabilities to take the organization where it wants to be."

Business author Malcolm Gladwell argues that clichés about the 'war for talent' have created some damaging myths about the importance of talented stars: "People who are deemed talented are constantly being pushed into new jobs and new challenges so how do you evaluate their performance if they're not in a job long enough for you to make that evaluation?"

Cisco tries to avoid such problems with a program called C-LEAD. High-flyers are graded for their ability to collaborate, learn, execute, accelerate and disrupt (or "take well thought-through risks"). One program is designed to build leadership capabilities of employees at director level and above, while another focuses on developing competencies for mid-level managers and high-potential employees.

Cisco's brightest prospects join the Action Leadership Forum (ALF), a 16-week program led by senior executives and academics in which teams forensically examine market opportunities and recommend whether Cisco should pursue them. "The intensity of the program is amazing," says Robbins. "People know it's an opportunity to showcase their abilities." Though the program costs US$10,000 (€6,900) per participant, it is good for Cisco's bottom line. Only 2% of ALF veterans have left Cisco since it started in 2007, 20% have moved up and US$25bn (€17.4bn) of opportunities have been identified.

What Cisco wants, Robbins says, is "people with the courage to help us think about things differently, rather than just say 'this is the way we've done it, so this is how we're going to do it.' Cisco believes in changing when times are good, modifying ourselves according to the market model and focusing on market transitions."

Developing tomorrow's leaders is a global function. Chambers wants China to be Cisco's third biggest market by 2013. In 2006, the company opened a Globalization Center in India to offer core functions in a secondary location. Robbins admits that local cultural issues mean C-LEAD can't be a like-for-like scorecard in every country. In some cultures, being perceived as disruptive can hold managers back.

Cisco has challenges ahead. Its Q1 2010 profits of US$1.8bn (€1.25bn) were down 19% year-on-year, but with cash reserves of US$35bn (€24.3bn) it can focus on strategic expansion. That'll be crucial if it is to fulfil one of Chambers' dictums: "Never confuse hard work with results." ●

"Lots of people can deliver the numbers. But they don't necessarily have the leadership capabilities to take Cisco where it wants to be"

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Learning Curve

The PT Barnum precedent

Why businesses seeking growth should learn to unlock their inner entrepreneur

BY TERRY PULLEN

Circus-master PT Barnum is best remembered today for a remark – "there's a sucker born every minute" – he never actually made. But the creator of 'The Greatest Show on Earth' was more than just a great showman. Before assembling a collection of midgets, sword swallowers and elephants, Barnum had honed his business acumen in lotteries, real estate and newspaper publishing.

Like fellow business icons Benjamin Franklin and Thomas Edison, Barnum was a generalist who seized opportunities wherever he found them. With the rise of corporations like General Electric (which Edison co-founded) management was gradually defined as a specialist craft and generalists went out of fashion. But in the 1980s, Tom Peters suggested that big corporations needed to hire more 'skunks': renegades who innovate by refusing to let bureaucracy stifle them.

The entrepreneur within 'Intrapreneurship' has been championed by Harvard Business School's Rosabeth Moss Kanter, who argues: "After years of telling corporate citizens to trust the system, many companies must learn to trust their people – and encourage those people to use neglected creative capacities." Whole Foods Co, the world's largest natural food retailer, has embraced Kanter's ideas, dividing branches into teams responsible for their own P&L; new hires are only confirmed after a secret ballot of fellow team members.

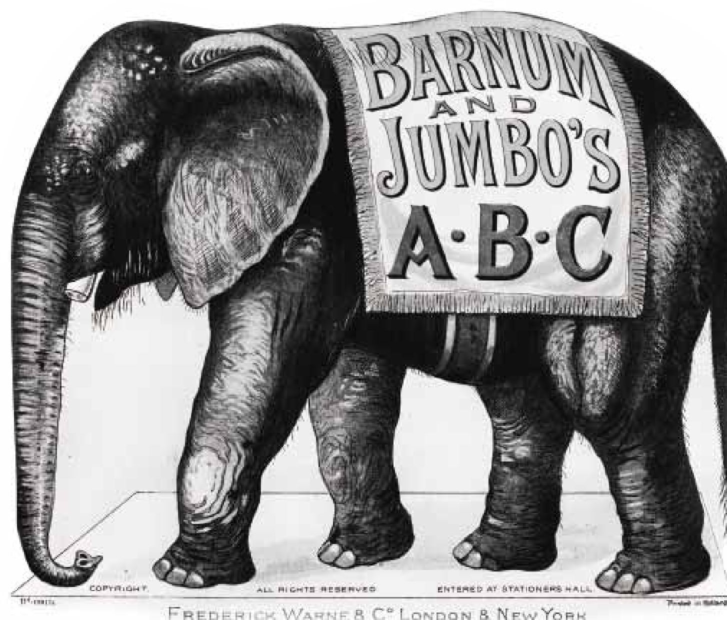
Think again Saras Sarasvathy, associate professor at the Darden School of Business, says firms put too much faith in MBAs. She says boards should deploy two kinds of thinking: causal reasoning, which is reactive and chases targets; and effectual, or entrepreneurial, reasoning which starts with a set of means but may take the organization into uncharted waters to find new opportunities.

Barnum certainly showed effectual reasoning when he decided to pay Swedish soprano Jenny Lind US$1,000 (€690) a night for a 150-night tour of the U.S. Despite never having heard Lind sing – and knowing few Americans had heard of her – he borrowed to take all the financial risk himself. He knew the gamble had worked when 40,000 people turned up to see her ship dock in New York.

Rethinking the organization When Darden's researchers studied 50 middle managers who drove growth, they found a sense of invention Barnum would have prized. All preferred to cautiously launch a new project rather than wait for hard evidence of success, and sidestepped bureaucracy. "Almost every decision on what to do next inside a company involves a trade-off an independent entrepreneur would not face," says Sarasvathy. Gap is encouraging an entrepreneurial spirit with a Results Oriented Work Environment (ROWE) program, where individuals choose their hours and job structure, as long as they meet targets.

Growing pains Entrepreneurialism is back in favor after a downturn blamed on managers' inability to question the system. Sarasvathy says: "Opportunities come from people having problems. So when things don't go well, it's time to act." In 1744, as U.S. Postmaster General and a media tycoon, Franklin had to sell off some inventory and launched the first mail order catalogue.

There are risks in encouraging corporate entrepreneurs – they aren't always the best leaders – but as countless bureaucratic initiatives to stimulate growth have come to nothing, CEOs might, as Kanter suggests, be better off letting managers unleash their inner Barnum. ●



The Granger Collection/Topfoto

"After telling corporate citizens to trust the system, companies must learn to trust their people – and let them create"

The virtues of intrapreneurs

1 They don't depend on authority or status
2 They care more about standards than beating the competition
3 Ethics matters to them
4 They are humble enough to keep learning
5 Process is as important as substance
6 They work across organizations
7 They care about results and are willing to be rewarded for them

Source: *The Change Masters* by Rosabeth Moss Kanter (Free Press)

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aob

Demystifying the cloud; business leaders on cell phones, start-ups and effective leadership

need to know

Cloud computing

What is cloud computing?
There is no exact definition – and that's part of the problem. Generally, the term is used to describe elastic technological capabilities which allow data or software to be hosted and accessed remotely. Among the major players are Salesforce and Google, whose founders Larry Page and Sergey Brin (pictured) view B2B cloud services as crucial to the future. General Electric uses a cloud to promote collaboration, while business services giant Rentokil Initial has moved 20,000 employees' email services to a cloud environment.

What are the benefits?
At its heart, cloud computing allows businesses to reliably and efficiently access computing as a pooled resource over networks – including the internet – instead of buying a patchwork of systems. It helps to rapidly scale computing resources, dynamically matching requirements to business demand. And it can help you shift to a utility-based pricing model where consumers only pay for actual usage.

Isn't there a security risk?
"Absolutely," says Bryan Cruickshank, Partner, KPMG in the UK. "The benefits of cloud computing are very attractive in the current economic climate, but it will bring new and emerging threats." In 2008, 700 million people were affected by data loss, according to KPMG's Data Loss Barometer. "Anyone using an external cloud service should check that the provider establishes, monitors and demonstrates ongoing compliance with a suitable set of security controls," adds Cruickshank.

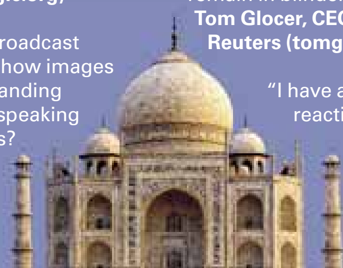
What questions should I ask?
You need to know who you're dealing with, and should assess the risk environment thoroughly. Check your provider can give you ongoing transparency of overall cloud capability and offers a flexible charging model. You should be able to move services to avoid vendor lock-in and reduce business continuity risks.

execs online

The edited highlights

"What we need in India to get more start-ups created – and to succeed – is a combination of an incubator and VC fund... In India, start-ups require a lot more hand-holding."
Rajesh Jain, MD of Netcore Solutions (emergic.org)

"Why did early broadcast television often show images of announcers standing in a radio studio speaking into microphones? Why did early adopters of cell phones sometimes stand in old phone booths to make calls from the street?... We have a tendency to carry over the limitations of the last era's technology to our first applications in a new domain. It is as if our imaginations remain in blinders."
Tom Glocer, CEO of Reuters (tomglocer.com)



"I have a visceral reaction to most attempts to impose policies on markets, especially around the internet, which has seemed to prosper well on its own set of organic rules, and with blessedly little regulation."
Gregory Papadopoulos, CTO of Sun Microsystems (blogs.sun.com/Gregp)

"There are no templates for being an effective CEO. When asked how to be a good leader, Jack Welch answered, 'Be yourself', and I would concur. Especially if you serve for many years, you can't fake it."
George F Colony, CEO of Forrester Research (blogs.forrester.com/colony)

Michael Grecco/Getty Images; Shutterstock

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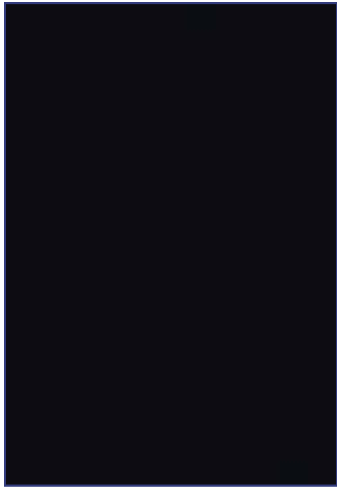
It’s a new world.
Are you feeling brave?



When the world is suddenly a very different place, how are you managing? Are you ready for a world where cash is scarce, but risk is not? Ready for a world that’s connected, but in ways you can’t connect with? That demands performance, but is merciless on costs?

KPMG firms are here to help you make this new place intelligible. We’ve tools that can allow you to unlock cash, improve efficiency, reduce risk, increase control – and prepare you for growth when the world turns again. So plant your feet firmly on this new ground. Visit **kpmg.com/agendaonline.**

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