AVALON-OC&C BUSINESS SUMMIT 2013 PANEL DISCUSSION

‘How to succeed in a volatile global world’

General introduction of the panellists and the panel subject: By Raj

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Part I: Q&A by Raj: I will start with the Asian crisis because there are lessons to be drawn from it for the situation we face today although the crisis is not similar

Frank: You were in Korea, when the lights went out in Asia in 1997? What was the general mood when the crisis hit? What was the impact on the economy? What types of companies did buck the trend?

*At that time, I had experienced a good combination of locations, because I was in Korea at the time as President of Illies and had decided earlier that I would be taking my family for the Christmas holidays to Indonesia which was equally hit by the Asian crisis. Korea at the time had just had the federal elections in the middle of December when Kim De Jong was elected to be President when the crisis hit. When I arrived with my family in Bali, and switched on CNN, I remember the first thing I saw was Kim De Jong crying and proclaiming that S. Korea was bankrupt. I then turned to my wife and said we have to go back immediately. The hotel where we were in also changed the currency on their menus to USD the very next day. At that time the Korean Won had fallen from 900 to the USD to 1950 to the USD. The stock market lost about 60% of its value. The IMF had to come in and for the "proud" Koreans, this felt quite unacceptable. The three largest chaebol boards in Korea at the time, Daewoo, Samsung and Hyundai called for a gold collection drive and within a month's time the private citizens collected 227 tons of gold; rings, keys etc. and that they had kept at home. The system was you give the gold to the banks and you will get a fixed exchange rate within a certain time; typically 2 to 3 years. This did not help the crisis a lot, but it showed that the Korean people stayed together, stood together and said we will have to come out of this, we all have to tighten our belts, and we have to make sure that Korea leaves this crisis very quickly. At the time, companies were of course in facing difficulties; companies like Hyundai and Samsung were able to increase their exports. Before the crisis, very few people knew about Hyundai and Samsung; within a few years after the crisis, everybody knew who they were. So those companies who were globally competitive were able to succeed and were able to take over other companies. Companies who were not able to sell their products abroad disappeared. Big companies like Hanbo Steel, Daewoo etc. all disappeared within no time. Hence those who were setup correctly were prospering and some of the companies (*that were not*) disappeared. In fact today, Mahindra and Mahindra owns Ssangyong, Tata Trucks owns Daewoo Motors, so there is a direct connection.*

Girija: You have spent 2 decades in various parts of APAC. You can add to what Frank has told us by giving an example of a company that did not get hit badly by this crisis and tell us why.

I will talk more about when the crisis hit ASEAN. Thailand, Indonesia, Malaysia stopped their currency from being convertible so let me talk about what happened in Singapore that time and what happened to the Singapore companies. So, you've had a situation where Korea had gone under, Thailand had gone under. In Indonesia, the government changed which was good, because they got into a democracy. Singapore was left alone, an open economy where exports were 280% of the GDP, so what did Singapore and the Singapore companies do? At the time, the country collapsed by -1.5%, and the Singapore dollar went from 1.4 to 2.5 to the US dollar. In such a situation you have to look after the businesses and you have to look after the people. So while there were layoffs, the Govt. moved fast and reduced business costs. Income tax cuts, corporate tax costs, PF costs were all cut. Hence businesses did not have as many layoffs as they would otherwise. Once that was done, the country's economy was stabilized, and in 1999 Singapore grew by 7%. That's the kind of return one country had when three other countries around it collapsed! So what are the lessons one can see in this situation? You have to very quickly take action to reduce costs of your business; companies and countries both need to do this. At the same time, you need to be flexible about labour as you have to reduce their costs and the taxes as well.

Jean Charles: Were there any companies in APAC that were hit initially and then managed to spring back to success? What did they do and how?

I may not be the most qualified person to talk about this crisis, because at that time first of all Legrand was not very strong in Asia and I was just arriving and I think this crisis took the whole world by surprise. I remember when I took up this position; my boss told me over there you will see double digit growth for a long time so you will become very comfortable. And when I arrived in December, the entire economy of Asia was down, which started in Thailand. I guess everyone was still in euphoria about the Asian economy. I could compare what happened in Singapore and what happened elsewhere. What I found at that time was we were more in a kind of wait and see position because we were not used to conditions changing so fast. In certain countries like Indonesia, we had to stop our big plans of investment midway and within one year we recovered our money. Hence, I think in this situation, I think one should stop plans of investment as there is no other option.

Frank: When the Indonesian Rupiah fell by 80% what chance of survival could exist for any ordinary company? Did any high flying invincible company in Indonesia bite the dust? Were they so blind that they did not see it coming?

I think for Indonesia, it was two crises at the same time. It was an economic crisis and a political crisis. I would say for most difficult problem of the country was crony capitalism. He (Suharto) was very smart, he even gave companies to his enemies so they would depend on him, and that was largely how the Indonesian economy at that time worked. A few good companies did survive the companies like PT Astra in their cooperation with Toyota. The famous Kijang car, known in India as the Innova, spread out into South East Asia as a result of the crisis of 1997-98. The biggest company that went bankrupt belonged to the Suharto family and in May 1998, he had to resign. Since then Indonesia developed into a democracy and a very stable economy. Hence, for them I suppose it was a very difficult time but with a positive result in the end.

Uday Khanna: With the benefit of hindsight, what would you have done to not get blown away by this crisis if you were the CEO of a successful fast growing company in Indonesia from 1995 onwards?

*Firstly, India does not have politicians who take accountability, nor do we have politicians like Singapore who know the right steps and take them. One of the things which was surprising was why didn't anyone anticipated the situation? There is a strategic tool known as scenario planning originally started by Shell and any company of a reasonable size should be able to plan for multiple scenarios. Hence you should be able to recalibrate your plans based on how things are moving. The second thing I would say is to stick to the fundamentals of your business and consumer centricity, distribution system, branding etc. I think Unilever Indonesia is one of the most successful Unilever companies in the world after Unilever India, and that management actually through anticipating, through looking at the bottom of the pyramid, through branding, etc. and fundamentals of business like not having large debt and not getting carried away with the fact that everything will go on well, (*became successful inspite of the crisis*).So, it's not rocket science but to manage a business under siege, it is possible to simply anticipate and prepare.*

Pieter: What lessons other lessons does the Asian crisis teach us? I mean, just taking a hedge at all times is an obvious defensive solution. Do tell us how a company in Indonesia that depends upon domestic raw materials could exploit this sudden surge in competitiveness to become very successful globally. What practical steps would you recommend as a strategy consultant?

I am glad you asked me that question and not a different question of how do you predict a crisis as even when you have things like scenario planning in place, no one really sees a black swan coming. Also if you've been long enough in the industry, you already know that there is going to be a crisis somewhere and crises are getting faster and faster and more unpredictable. Hence one of the things to do in that case is being prepared. One of my clients for example is a large dairy company and the three best markets they have are Nigeria, Indonesia and Greece, and all of these 3 countries have gone through very terrible crises and the way they have survived is through a very good strategy which was combining local sourcing with international sourcing, hence the moment there is a crisis, they can adapt to currency swings and other things. A very different client in a different situation is more often the benefit of a crisis. And one of the things we have seen all over the world is in the value segment; what customers tend to do in a crisis is spend less money but still they want to spend some money and go for the value segment. We've seen it in airlines as well as in the restaurant and retail world. For example in 1998, two brothers started a very small company in retail who was using their food value chain to sell shampoo and other consumer products. What they guaranteed to their customers was that we are extremely cheap with no guarantees. What you will then observe is that such companies increase their market share during crises and then remain level, and then again increase with following crises. One of the explanations for that is that consumers like to get into the value segment when in a crises. Hence as a consumer company, exploiting the crisis this way is one of the first things that you can do.

Girija: You started to build TCS in China around 2000. Your company's planning process must have been going on during the Asian crisis. Most companies would have dropped or postponed APAC plans at that time. What made you join TCS to lead the foray into APAC at that time, when you had so many other career options?

After having seen the Middle East crisis and the Asian crisis including the SARS crisis, I believe if one has the guts, a crisis could be the best time to invest. We built TCS at that time when everyone else was running around and figuring out what to do. We opened offices in Australia, China and other countries, and the rest is history.

Part II by Raj

Soon after Asia recovered, the dotcom wave mesmerised many a sane person in another part of the world. We will skip the dotcom bust because the lessons are obvious and fast forward to the Great Global Meltdown of 2008.

Very few people saw it coming. Not just companies but entire countries wobbled and some are still wobbling. The buying power of the people suffered and along went top lines and bottom lines of several businesses thousands of miles away. The wily Wall Street banks were blamed and investors fell for the lure of easy earnings. It has left a deep permanent scar on the corporate psyche and people talk about the new normal without understanding what it means. To me it is not a new water level but a realisation that change can and will happen and sometimes from outside one's industry and that understanding risks is now as important as understanding opportunities.

Pieter: Some analysts argue that managerial compensation was such that it encouraged excessive corporate risk taking for personal gains. This is a major cause of the difficult situation that companies got into. What is your view?

I don't have difficulty with high bonuses if people perform very well. Also, as we have seen in financial institutions, bonuses typically had a short term angle to them; they were not in shares that you could cash in on after 5-10 years. If that was the case, people would start acting much more responsibly. When I was working with merchant and investment banks early in my career, these banks were mostly partnerships, hence they got huge bonuses but also put their own money at risk and that's the major difference. Hence, bonuses can be Ok, but with some long term orientation to it. The second thing is apart from the bonuses, several countries went through liberalization very quickly however all governments' failed to have enough countervailing power to take any actions against these institutions which were cross border. Governments could have had better regulation over packaged products and I'm not sure whether even currently that is the case.

Uday Khanna: Can you suggest ways to ensure that managerial compensation does not become a perverse incentive to take unacceptable bets? What other aspects of good governance could have saved companies during the Global economic crisis?

According to me, the softer values like culture and ethics are most important. Like we saw in the US crisis there were many companies who did not fall prey to what the investment bankers were doing and continued to be successful. This was largely because they had integrity, ethics,etc. Hence, unless these are in place, no amount of regulations will work. Firstly, there needs to be a reduced gap between CEO compensation and the rest of the team, as this is not conducive to team work. Secondly, bonus need to be tied to short term and long term performance and also not be way out of line with the salary given. Lastly, the bonuses should be given out in such a manner that they are required to be compulsorily invested in the stock of the company for long periods of time like 5-10 years. These kinds of reforms are in fact being talked about in the UK.

Frank: You have led your company through the crisis in Japan, an even bigger crisis in S Korea when the won fell to a third of its value. You would have witnessed successful and unsuccessful clients in Asia and Europe during the Global crisis of 2008-2010. What lessons can you share from all that?

*We are a 158 year old family owned company and have seen and been through several crises. Firstly, you need to have an innovative product mix of good quality which is competitive. Secondly, you should not grow too much on credit and bank loans. This makes it possible to stay independent of banks. Thirdly, you should keep a balance between domestic and export business. Exports also increase the quality of your product as you need to survive in foreign markets. Fourthly, (*you must*) always hedge foreign currency exposure. Several companies during the crisis went bankrupt due to exposure to foreign currency. And lastly, always be ready for an upswing, don't cannibalize your company, although its necessary to cut costs, be prudent etc. When the business comes back you have to be there.*

Jean Charles: Your Company, Legrand is the World's largest producer of electrical and digital products used in homes and commercial buildings. During the crisis the building sector tanked, your Group's revenue dropped by nearly 16% but you still maintained profitability at the pre-crisis level of about 17.5%. Most companies dread a fall in revenues because profits usually get wiped out. What strategies did your company deploy to survive such a deep cut in sales and then in the following year actually grow revenues?

If I could draw a parallel between the crisis of 1997 and 2008, the main word which comes to my mind is "anticipation". In 2007 I remember that our HO in France, before going for summer holidays, it became obvious to us that this crisis would expand all over the world and definitely affect us. So when we came back from our holidays, all MDs were called for a meeting and told us that with a 15% drop in volume, we had to maintain the same level of margin. Hence, the MDs were forced to revisit their strategy and look for other profitable ventures. In the end we were able to make the required margins due to good antipication. Also, our group has never been in a panic mode, so during all the *difficult years we have been able to perform well without comprising on our long term goals, people, customers and values. This is also important for the after-crisis period like when we were in 2009, we were very fit and organized enough to adapt ourselves to any type of situation. Hence from 2009 onwards, our profits went up very significantly and from 20% operating margin in 2009, today we are at 20.7%.*

Girija: I have noticed a subtle change in strategy deployed by a rank outsider in the IT industry who rose to become the No 2 in India. I am talking about Cognizant. Whilst the rest of the IT players were still debating about fixed fee vs. Time & Materials, Cognizant went for a new model – business outcome based pricing. You cannot get more aligned with a customer's interests than that. Why was it not obvious to the other IT players that they could use that customer strategy?

Certainly, Cognizant has done very well. However, what I will say is that the model of outcome based fees was not new and I don't think that was the reason for their success. When the Global Finacial Crisis hit in 2007, TCS decided to come closer to the customer and decided that this was the time to go out and buy. Citibank was in deep trouble, and TCS put USD 500 million on the table, got 17,000 people off the Citi BPO, moved them to TCS and created the biggest BPO in India in 2008. Today, TCS is the largest market cap company in India at USD 60 billion. It is now ahead of HP and Accenture. And that is because bold decisions to buy companies in Asia and Latin America were taken.

Uday: Which industries in India are waiting to be transformed by someone coming up with a new customer strategy? (A new, innovative business model, as it was)

In my view, there is enough space in any industry where a player could come and disrupt the market through a business model or a pricing model, or a product delivery model. Hence irrespective of the macro-economy, potential in India is immense. My personal favourites are in affording housing, affordable healthcare and tourism.

Part III Raj:

The Indian economy's recovery from the Global economic crisis was sharp but short-lived. Most people did not see the slowdown coming despite the slowdown in investments in infrastructure followed by several quarters of policy paralysis caused by exposures of one scam after the other. The Government fell asleep at the wheel instead of driving the economy to where it deserved to be. The last year saw low growth and the first two quarters of this financial year saw a dismal growth of 4.5%. We also saw a 20% depreciation of the Rupee which has now corrected itself to 15%.

Jean Charles: **A global survey done in 2012 predicted that by 2018 India would become the 2nd most competitive country for manufacturing. If the Rupee remains between 60 and 63 to a dollar, that day could happen even earlier. If in the meanwhile, if the Western economies start looking up, should MNCs consider investing now in Indian manufacturing in order to source components or products from India for the global markets? Why would Legrand not do it?**

Yes they should. Legrand is built on two pillars; one is organic growth and (the other is) *inorganic growth. We have now been here for over 15 years and India is one of the best success stories within the group. We started with an acquisition and since then have been expanding through new products and businesses helping us grow by over 10 times in the last ten years. We began with a focus on the domestic market but now our products have reached the same level of quality and consistency as global standards demand. We have now established India as an export hub for Asia.*

Pieter: **You probably think it is a joke when we talk of 4.5% real GDP growth to be a crisis. We really need much more to solve our socio economic problems. You come from a country that exports, exports and exports. Would it make sense for Indian companies to stop worrying about the 'Low' GDP growth and utilise the Rupee's fall to win in international markets by becoming seriously export oriented?**

You can use the current situation to increase cost competitiveness and increase exports. However, one cannot only compete on price; countries like Bangladesh and Vietnam are also trying to be extremely competitive hence price advantage is a temporary one. India could use the situation to its advantage and compete on time to market, supply chain, quality, other elements in the value chain which could strengthen India's long term position.

Uday : **I know that Frank believes that Indian manufacturers should start exporting seriously so as to not just tap the opportunity but also to get their quality right, make their supply chain more effective, etc. If they don't they will become uncompetitive even in the Indian market when international companies become here to take advantage of the opportunity. It has happened in some sectors like white goods, consumer electronics, cars, etc. Uday, please share your advice on how to grab this opportunity with the business leaders who are present here today.**

Firstly, if companies in India do not become competitive on quality globally, the way globalization is happening, somebody could very well come from outside and setup an export quality oriented unit in India itself. From personal experience, the reason why Hindustan Unilever is now competitive is because we used to have an export division where benchmarking against global standards was being done right from 20 years ago. A lot of Indian companies don't benchmark because they feel domestic demand is so strong that there is no need to think of exports, but this cannot be a long term goal. Secondly, with so many graduates coming out every year, there should be a strong push for manufacturing to come up to increase employment. However, government policies need to be favourable for manufacturing to kick-off in a big way. A lot of units which moved out from China in fact have been setup in Vietnam and Bangladesh due to more favourable environments.

Q&A session for the audience

Q1: I was very impressed that you thought you could get international quality out of India because in the 20 years I have spent in the country, I find that India's ability to deliver sustainable quality is the single biggest challenge any business here faces. We have seen problems with companies like Johnson & Johnson who were not properly cleaning their equipment before making their drugs, companies like Ranbaxy who have had disastrous quality controls on their drugs, we have seen companies such as Mahindra & Tata who have produced cars that look superficially nice but then fall apart after 6 months. Even when the quality in one day, in one week, in one month year or in one year is ok, the moment your back is turned there is no buy into quality from your workforce. If given half a chance they will abandon your standards and you will find your Legrande stuff failing all over the place. Most international companies I have worked with have this problem, most Indian companies have this problem and many of them do not even notice. How can we get a quality mind-set in India that reaches down to the shop floor and is not just at the board level?

Uday Khanna: *I think you are absolutely right. Quality is a direct function of the management of a company. There are companies in India who have won the Deming's prize more than once so it is possible to reach those levels of excellence. It requires an attention to detail and in the case of a company who is trying to grow in the export market, then not cutting corners to do so. However, you will only get to that level if companies get serious and decide to use the best companies in the world as a benchmark. Due to their proximity and global competitiveness we tend to measure ourselves against China, where as a result of a lack of quality control the majority of products produced are junk and beyond that, the fact that they reverse engineer your technology. We need to move away from this and look at the best competitors globally. However, even in doing so there might be some issues as India also possesses many infrastructure bottlenecks which may hinder any steps a company may take in this direction. It is the responsibility of people like us and professionals such as us to refuse anything of substandard quality. In the old days, when there were foreign exchange constraints, the standard of the products in the FMCG sector was substandard due to a ban on imports. Therefore you had the export zones where you could benchmark and be internationally competitive and learn how to ply your trade in those markets and when the tariffs went down you could take those learning's and apply them to your domestic business. It is an issue with individual's mind-set here. To give you another example, my company Lafarge, has a plant in Chhattisgarh, which is one of the most backward districts in India. In 2011, using a set of 20 different parameters the plant was voted the best across their operations in 70 different countries. This was because of the plant manager, his training techniques and the overall attitude and approach to their work. Even though achieving and sustaining high levels of quality is a long way off, it is attainable. You need the will, a good eye for it and on the management. And there is a good example in this country for every bad one. The biggest success story in terms of maintaining quality is perhaps the software industry that has beaten every single global benchmark in terms of reliability.*

Frank: *Product quality or quality in general is always a management issue. No workers want to produce junk.*

Raj: *I am not being patriotic but India has the most number of Deming award winners and is so far ahead of other countries in terms of number of winners, that if you added the total winners from the countries with the 2nd, 3rd and 4th highest number of all-time winners, then India would still be ahead of that combined number. Having said that, India is also home to companies which adhere to pathetic quality levels and we need to make people understand that what they produce is an extension of their personality and how they are perceived. Therefore they should take pride in their quality because only then will it improve.*

Q2: Due to government policies and regular increases in taxation, we live in a state of constant uncertainty. How do you stay motivated and continue to improve yourself and your company when your efforts are constantly being hindered by the government who seem intent on hurting rather than helping business?

Jean Charles*: It is a part of life regardless of which country you are in. We cannot say that we are happy or unhappy but being bound by these constraints. Constraints make it a little harder for everyone but you need to find a method that allows you to adapt and use that to form a strategy and navigate the road ahead. It can help you work harder and smarter instead of being a hindrance.*

Q3: What would be the top 5 inward looking actions would you suggest for a company during an extremely volatile period and/or a crisis?

Girija*: You have to find a balance between your long term outlook and your short term outlook. It is extremely important to find a balance because if you only focus on the short term problems, there are sure to be problems further down the line. In the short term you have to look at managing costs, fixing margins and ensuring your pricing is on point. The short term remedies are much easier to pin point and put into action as they are the ones that are quite obvious. The real challenge lies in the long term fixes and corrective actions and their approach to this will separate the companies that will survive and those that go bust. In this regard, you have to consider whether you are looking at expanding into a strategic area or whether you are considering any acquisitions or whether you are improving you competitiveness. More than any specific issues, it is ensuring that you find a strong balance.*

Jean Charles*: A crisis is obviously better when it only extends to the short term. Either way, it has many merits. It shows your partners, colleagues and employees that even when the going is tough that you are committed to keeping your values and your long term strategy. It also allows us the chance to really connect with and get through to our employees. Certain sales staff that may be experiencing single digit sales growth from 30 to 40% will be now more willing to conform and listen as they may not be making their incentives given the harsher climate. It allows you to keep the core but streamline operations and be frugal, which will give you an upper hand when the market returns to its normal state.*

Uday Khanna*: You have to be value led and vision driven. This has to be encapsulated in your long turn vision and that is the only real key to sustainability.*

Q4: One of the elements of volatility is sensible and sustainable government policy. There have many instances in India across telecom, power, mining where companies have got shut down without advance warning. What are the learnings we can take away from other parts of the world, which will help us to better manage and anticipate the whimsical nature of decision making in this country as this does affect the sustainability of a corporation in India?

Uday Khanna*: We are all extremely familiar with the difficulties of doing business in India. India as a country is ranked at approximately 140 in the world in terms of the ease of doing business. We have reached a bit of a problematic state with our policy makers as there is no clear set of rules, method and/or oversight on how and what laws are constructed and enacted. There is a huge governance issue as the legislator is being asked to asked to sign off on laws which say 'as may be prescribed subsequently'. In the micro sense, it is possible to survive by being ethical.*

Q5. A large portion of the common citizens of this country believe this crisis will end in FY14 with the elections happening next year. With the young population and number of new graduates coming out of colleges, coupled with the job market shrinking, do you foresee this economic crisis spiralling into a socio-economic crisis and has any one of you observed any other economies of the world in similar situations?

Pieter*: There is no clear answer to this as we have seen in the past with Southern European countries where 50% of graduates are unemployed in a traditionally prosperous country, as well as the situation in the 1930s.*

Uday Khanna*: There is a concern on giving jobs to the young population but in fact the number of projects with held up work is large. In a country with 1.2 billion, there is still a problem of unskilled labour. However, at the micro level I don't see any business which cannot achieve 25-30% growth provided they position themselves well with the right people and the right vision.*

Raj: Ladies and gentlemen, we have been treated to some great insights by our panel. I will not repeat them but we will put it up on our website for you to read. I will conclude by saying that they have all shown that it is definitely possible to succeed even in the worst of times. You need to align closely with your customer, hedge your bets, look at markets that are growing even as some others are not, etc. On that happy note, I will hand you over to the young lady from the EDB Singapore, who will tell us how the APAC market can be captured by using Singapore as a base. Thank you, audience and thank you, panellists.