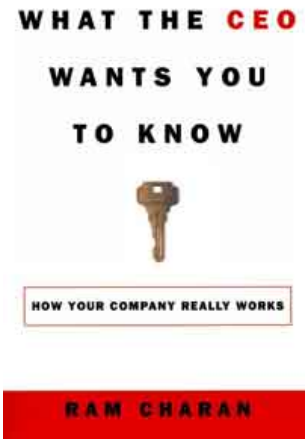
BusinessSummaries

WISDOM IN A NUTSHELL

WHAT THE CEO WANTS YOU TO KNOW

How your company really works



By
Ram Charan

Random House 2001
ISBN 0-609-60839-8
123 pages

The Big Idea

From running a multi-billion dollar business to selling fruit on the street, the CEO and the vendor share the same street-smart instincts or “business acumen” that are the essential skills to running a business. A CEO wants his or her people to understand business basics, from cash flow, to ROI, to sniffing out new opportunities and eventually becoming more involved in the decision-making that leads to bigger profits. The more you get what the CEO wants you to know, the faster your company will grow!

Part 1

Business Acumen

The universal language of business

1. Why Jack Welch thinks and talks like a street merchant

No matter where you go in the world, street vendors are all alike: they borrow money to get their produce (inventory), sell at a profit, pay off their interest by making more sales faster (inventory velocity) and making sure they don’t bring home any leftover fruit but bring home cash instead.

Every morning the vendor arranges his wares in an attractive manner (merchandising), calls out to potential customers louder than his competition (advertising), adjusts his prices throughout the day (increasing value to customer by slashing prices), and focuses on the bottom line with a very keen sense of what sells and what works.

You don’t have to be an MBA graduate from Harvard to hone these skills and understand the basics of business. The key is to send the executives back down to the floor, where the nitty-gritty everyday sales calls, rejections, complaints, and individual decision-making that affects the bottom line is more real than anything that occurs within the confines of a board meeting.

The Universal Laws of Business Acumen

Learn to see your company as a whole and make decisions that enhance the overall performance.

If you are in promotions and you don’t give a flying fig what goes on in the finance and planning department, how can you possibly think up a campaign that will address the money issues, move stock off the shelves faster, or make customers come back for more? Coordination is the key in any organization and

seeing things as one unified whole is the beginning. Think like you own the business, after all…it is paying you.

2. How your company makes money

How cash, ROA, growth, and customers work together to create a profit

Cash generation is the difference between all the cash that flows into the business and out of the business in a given period of time. CEOs want their people to be cash-wise, from a sales representative negotiating a 30-day payment down from the usual 45, to a janitor turning off more lights during lunch hours, the little things all count and add up at the end of the month. When accounts receivables (money owed to your company by customers) are not properly scheduled for collection, to the management of accounts payables (money the company owes its suppliers) a company's oxygen (cash) is the lifeblood and can spell bankruptcy if there is not enough to go around.

Manage for cash!
Even scheduling the billing can make a big difference. From sending out the bill earlier like on a Wednesday, your company can receive the check earlier than the usual Friday, so you won't have to wait several days before the check turns into ready cash.

Return on Assets

The things you've invested in are called assets. From the office equipment and assembly plants to inventories of materials or components – regardless of the size of your business, you're using investment capital (usually someone else's money, unless you inherited it) to grow your business. Tangible assets are things you can see and touch. They are sometimes called fixed assets.

Even a woman on the street selling fruit knows she has to sell her wares faster and rotate her inventory or turn the stock over if she is too make a good return on her investment. To pay the interest on her loan for the fruit, and to restock her cart, she needs to sell more quickly and repeatedly throughout the days of the week to get back and make a profit over lets say her 5% interest.

Wal-mart sells its toilet paper so quickly it gets back the money spent on inventory plus it makes a profit, every single day! Talk about zero time!

Margin refers to net profit margin after taxes, or the money earned after the company pays all expenses, interest payments, and taxes. Gross margin or the amount from which net profit margin is derived, is fundamental to understanding the structure of any business.

Gross margin is calculated by subtracting costs associated with the making and selling of a product or service from the total sales.

When it comes to inventory velocity, deliver like Dell does…

The computer company Dell has excellent management of the idea of velocity. It makes each PC to order and its components hardly have time to warm up the shelves. It sells computers so fast, and makes money up front that its year-end inventory doesn't require much space.

The less inventory the better…

Amazon.com is one company that used to have a warehouse-free system for its books. With the introduction of warehouse inventory for books, the company may be facing problems it didn't have previously when books were never stocked in actual spaces, but delivered directly to customers.

Getting to know your customers

All you need to find out the pulse of your consumers is common sense. Go to where they shop and observe how they shop. You would be surprised how much common sense is not used in some business decision-making.

3. Putting the pieces of the puzzle together

Understanding the Total Business of your Company

Employees will contribute more when they know what really goes on in the business and how they fit into the total scheme of things.

Answer the following questions and see if you know what the total picture is like and see things the way the CEO does.

- What were your company's sales during the last year?
- Is the company growing? Is the growth picture good enough?
- What is your company's profit margin? Is it growing, declining, or flat?
- How does your margin compare with your competitors?
- Do you know your company's inventory velocity?
- What is your company's return on assets?
- Is your company's cash generation increasing or decreasing?
- Is your company gaining or losing against the competition?

What you can do to address these issues:

Look for ways to increase productivity or improve customer satisfaction. Remember, there are many ways of to rally people around a new and exciting product launch, or even a new way of greeting and serving customers…

Cash generation, margin, velocity, return on assets, growth, and customers should be part of everyone's vocabulary in your company, and when it is, the CEO will be leader of a well-informed organization with real "business acumen".

Part II

Business Acumen In The Real World

4. Cutting through the clutter and noise

From complexity down to simplicity: Figuring out your company's three most important priorities.

CEOs use their business acumen to determine clear, specific priorities and action item that make money for the company's shareholders or owners.

The best CEOs use their business acumen to reduce complexity, to the basics of moneymaking. They love a challenge.

GE's Jack Welch focused on the fundamentals, and sold the aerospace business of GE to whom he believed would emerge as dominant player: Martin Marietta. Changes such as the fall of the Soviet Union clearly showed the US defense budget would shrink back in 1989, leaving Welch to make a big decision, but ultimately a wise one.

So do you know which product really makes money for the company? Do you know which one consumes the most cash? Which one makes the least?

5. Be fruitful and multiply!

CEOs know that wealth is linked to the price-earnings multiple or PE ratio. The P is price of an individual share of stock. The E is earnings per share or how much profit the company made for each share of stock. The P is divided by the E; but you can easily find these numbers listed in the Wall Street Journal.

A higher P-E ratio means more shareholder wealth. A CEO with business acumen understands that. How you run the business affects the P-E multiple. Coke performs better for its shareholders than Pepsi, for instance.

A publicly held company that grows its sales and revenues, profits or earnings over time without lowering velocity increases its P-E multiple.

GE is perhaps the best example of a company that has consistently made money for its shareholders. In March of 2000 its P-E was 45, higher than most companies of comparative size.

Whether it's answering calls promptly or introducing a new product, the CEO knows the P-E ratio gets a boost. Employees also stand to benefit from increased wealth; they can get a share of the profits too!

Part III

How Can You Get Things Done

The edge in execution

6. Knowing what to do

Leading your people

Simply put the right people in the right jobs! If a person is not well matched to his or her responsibilities, and cannot make the best use of her talents and skills, you will have an under-performing liability coming to work every day. As opposed to a person who is matched to the right job for her, she will happily come to work early, be more enthusiastic, and more productive. This simple idea (common sense) of matchmaking between jobs and people is what every CEO should know.

Remember, the longer you wait to transfer or remove someone who is not matched to the right position -you lose money.

Coaching constructively

Make every presentation a learning exercise. Offer real feedback and say what is on your mind. CEOs write emails to their employees to coach and boost confidence. Be very specific about what you want out of your people, for each and every role that needs to be fulfilled.

If the problem is behavioral, be diplomatic but direct. The faster you correct a behavior, the better for your business.

7. Why Sam Walton should have won the Nobel Prize for Business

The Art and Science of working together

Synchronicity. Watch how a rowing team moves together in slow motion. Every stroke is essential. If there is no synchronicity and the teamwork fails, they lose the race.

Wal-Mart has a Social Operating Mechanism created by Sam Walton. In the early 1990's Wal-Mart's regional managers would visit Wal-Mart stores and its competitor's stores every Monday to Wednesday, gathering goods and comparing prices. This was to find out if their strategy of offering prices 8% lower than competitors was actually being executed. They were able to observe how the merchandise moved, what the ambience was like in competitor stores, and how employees behaved.

Customers hate an organization where the people are not synchronized and communicating.

Communicate with your people, and do it often!
Sam Walton used Thursday mornings to conduct 4-hour sessions with managers so information could be exchanged, so people knew what was going on, what sweaters needed to be moved out of which stores, whether inventory should be adjusted.

You don't have to follow the Wal-Mart way of doing this, design your own method.

8. Where the rubber meets the road

Real world CEO view of the big picture

Learn how to link priorities with people. Dick Brown of EDS used conference calls to communicate urgency of priorities, and opens each call with the highlights of the month. Dialogue was candid, concise, and constructive.

Performance should be reviewed and followed-up. Bi-weekly emails, informal and direct, reinforce the business priorities and goals.

Ask for suggestions! Cost-cutting ideas can come from anyone. Maybe your managers don't need to travel first-class or book five-star.

Part IV

Your Personal Agenda

9. Think globally, act locally

Link your own priorities to the bigger picture of your entire company. Do you believe in what your company stands for? If you work for a pharmaceutical company that refuses to help lower the prices of its drugs in poorer developing countries, can you really go to work with enthusiasm every day?

Assess the total business

- What were your company's sales last year?
- Review the question listed earlier in chapter 3.

- Make a list of all the things that affect your company's moneymaking ability. Do you have any new competitors? Are there currency fluctuations or changes in interest rates? Is the industry doing well as a whole?

Focus!

- Determine 3 clear business priorities and how will they make money for the company?

- If you can't explain your ideas and plans in simple language, try going back to basic common sense.

Synchronize!

- Are people exchanging information freely in the company?
- What is the speed of decision-making?
- What is the quality of these decisions?
- Do people find meetings constructive or energy draining?
- Are decisions and agreements adhered to or are they quickly forgotten after the meeting?

Now that you know what a CEO wants you to know, take the initiative and think, act, and get moving!