

# RATOS

Incentive programmes – a necessary good

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# Incentive programmes – a necessary good (1)

- Incentive system difficult and complex
  - but potential dynamite!
  - Messi syndrome...
  - ...does not mean, however, that it can't be done
  - Requires special efforts, resources, continuous development

# Incentive programmes – a necessary good (2)

- Ratos vs. incentives
  - two major, internal main projects
  - continuous development
  - we belong to the elite in this area...
  - ...with 3.5 points on a 5-point scale

# Internal project (1)

- Foundation
  - alternative systems
  - taxes
  - countries
  - combinations
  - psychology
  - tailor-made from a smorgasbord

# Internal project (2)

- IPIP (Incentive Programmes In Practice)
  - philosophical/fundamental corner stones
  - real-world examples
  - benchmarks/best practice
  - internal structural capital project
  - presentation/information exchange/individual development

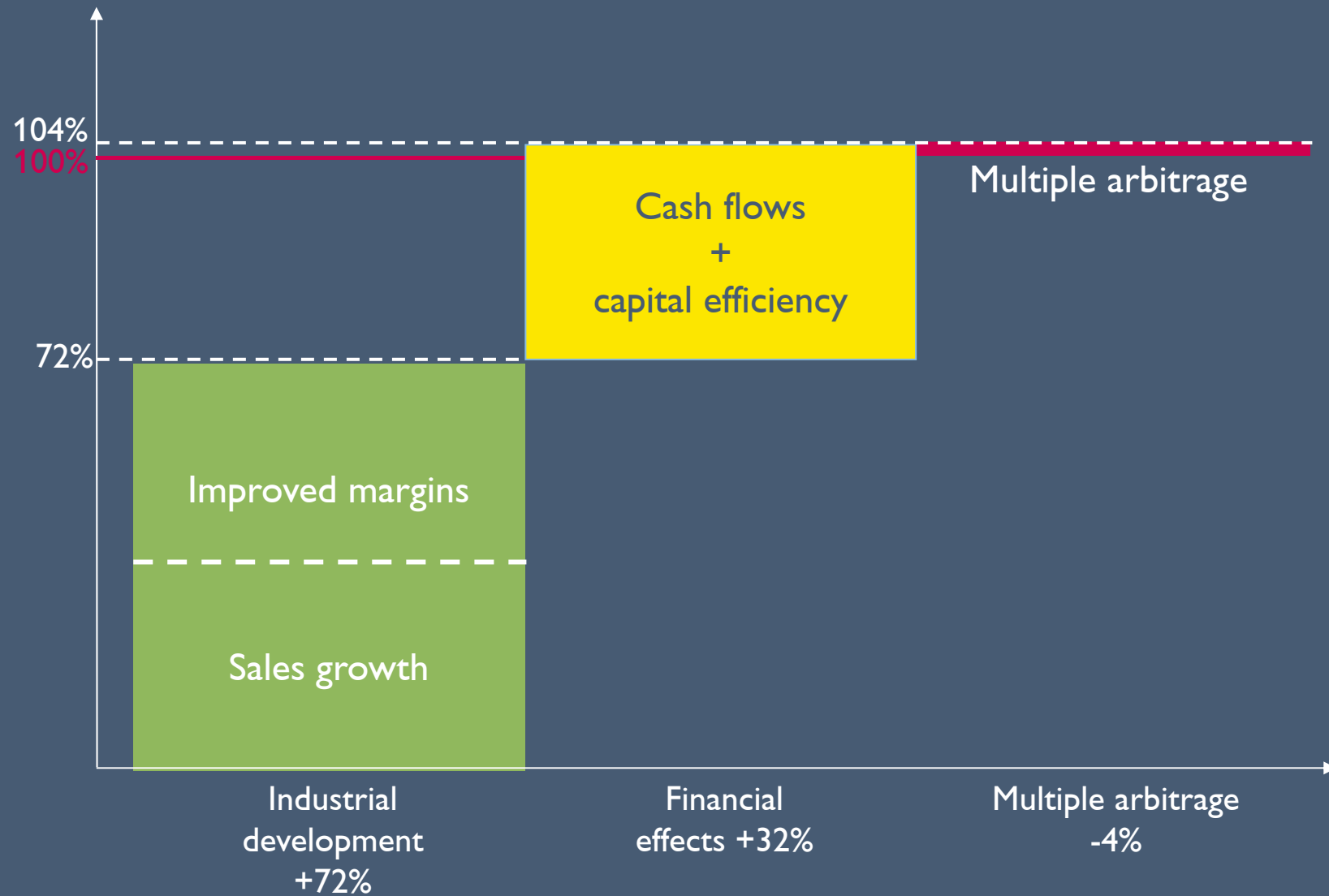
# Why incentive programmes?

- Debate wrongly focused
  - misses the point!
- *Level 3: Must we pay so much?*
  - YES (if you want Messi)
- *Level 2: Are people driven by money?*
  - YES
- *Level 1: How to use incentive programmes to influence people's behaviour!?*

# Influencing behaviour requires a structured effort

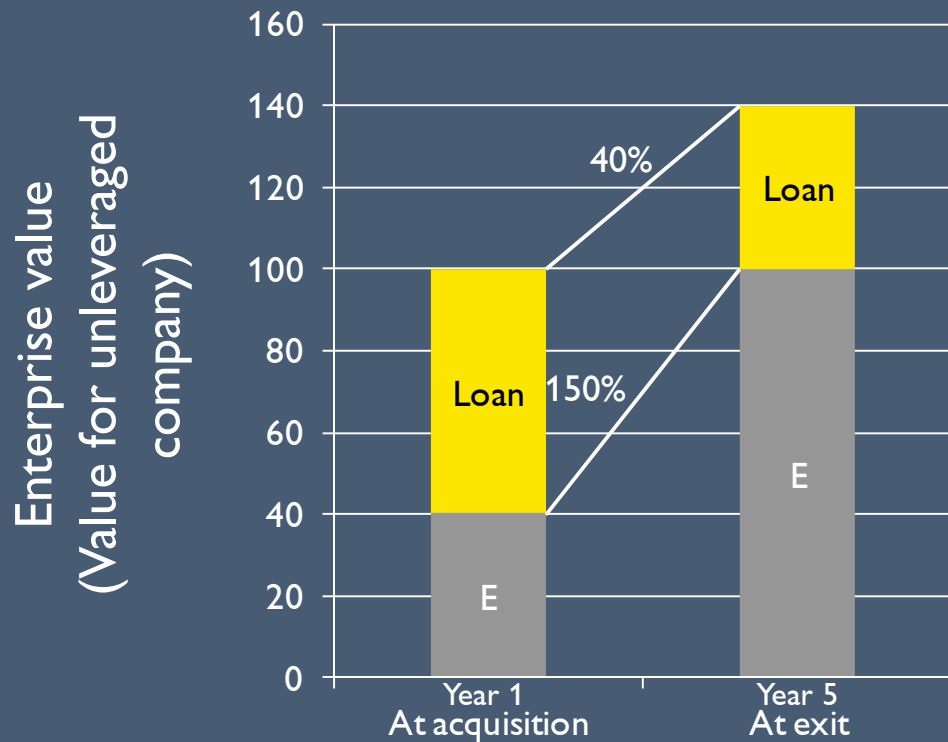
- Tie together understanding of the whole
  - operational plan
  - Ratos's business model
  - 20% IRR preferred!
  - incentive structure
  - whole and parts

# IRR = 26% – how?





# Value drivers



5 years EV +7% per year  
E +20% per year

- Profit development
  - Growth (organic and acquisitions)
  - Improved margins
- Cash flows & leverage
  - Capital efficiency
  - Investments, tax
  - Capital structure
- Exit multiples
  - Profile
  - Strategic position
  - Growth potential
  - etc

# “Profit improvement tools” (example)

## Sales growth

- Price
  - Pricing strategy
  - Discount system
  - Packaging services/goods
- Volume “existing market”
  - Sales strategy / focus
  - Brand strategy
  - Loyalty initiatives
- Volume “new markets”
  - New geographies
  - New products
  - New channels
  - New customer segments

## Operating margin improvements

- Purchasing
  - Consolidate purchase volumes
  - Renegotiations
  - Screening new suppliers
- Production rationalisation
  - Profitability analysis (ABC)
  - Make or Buy
  - Factory consolidation
- Overhead savings
  - Outsourcing
  - Shared services
  - R&D portfolio management
  - Process rationalisation

# Basic example

	2012	2013	2014	2015
Sales	1 000	1 000	1 000	1 000
EBITA	50	50	50	50
EBITA%	5,0%	5,0%	5,0%	5,0%
Working capital, BB	150	150	150	150
Net cash, BB	0	50	100	150
Cash flow for the year	50	50	50	50
Net cash, EB	50	100	150	200

	Acquisition 2012	Exit end of 2015
Acquisition multiple	7	7
x EBITA profit	50	50
Price debt free company (EV)	350	350
- Present net debt	0	200
Price for the shares (Equity)	350	550
	IRR: 12%	

# Real-world examples

- Company 1
  - tied-up working capital
- Company 2
  - pricing issues in production-focused company
- Company 3
  - investments in capital-intensive, capacity-focused sector

# Overall conclusion/recommendation

## Framework for this project

1

### Establishment of well thought out and well balanced incentive programme

- Incentive structure
- Leverage and return profile
- Scope (number of people)
- Scope (investment)

2

### Basic understanding among incentive participants with regard to company valuation and value drivers

- Overall understanding for company valuation
  - Company value (EV) vs. share value
  - Valuation method(s)
- Detailed review of Ratos's approach to value development and value drivers (IRR 20%)

3

### Annual communication relating to value development and value drivers historically and going forward

- Annual communication between Ratos and incentive participants
  - Assessed value development **from opening value to current value** – preferably with a breakdown by each value driver
  - Targets for value development **in going forward** – preferably with a breakdown by each value driver
- Ensure clear feedback between development/future and Ratos's approach to value development (IRR 20%)

Operational effect from incentive programmes requires a **firm foundation** and **recurrent communication** with incentive participants