ASIAN MANAGEMENT INSIGHTS

Unleashing Creativity

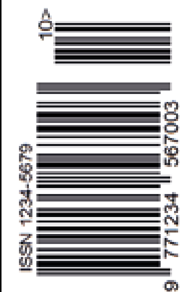
Innovating across cultural borders

Ethics and Values
An interview with Ratan Tata

Digital Canaries in an Urban Data Mine
Analytics for smarter city life

Surviving Beyond a Third Generation
Survival of the fittest family-owned business

An Oreo with Chinese Characteristics
A case study



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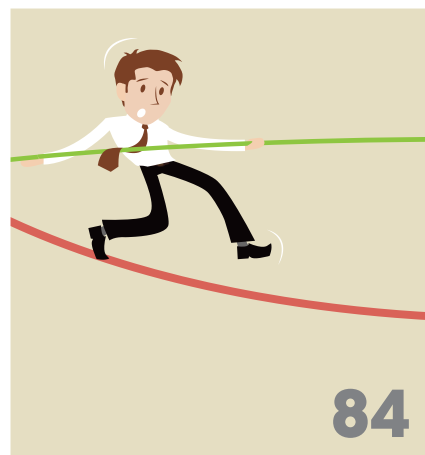
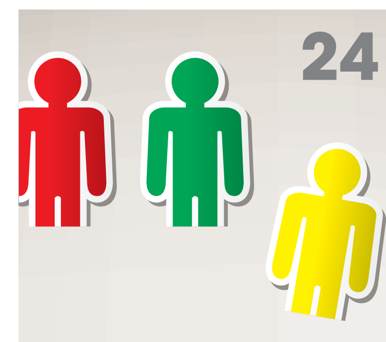
Asian Management Insights aims to develop a body of knowledge and a narrative of innovation and creativity for trends in Asian management. It brings together some of the best and the brightest of Asia's thought leaders and their solutions to address current Asian challenges.

– Philip Zerrillo, Editor-in-Chief, Asian Management Insights





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FROM THE EDITOR

Much has been written about the megatrends in all aspects of management that have taken place over the last decade or so, but rarely, if ever, do they include Asian examples, and certainly not Asia-based solutions. Yet one of the greatest of these major megatrends is the movement in the global economic centre of gravity towards the East.

Asian Management Insights represents a bold, but necessary step on the part of Singapore Management University. Published by the Centre for Management Practice, it aims to develop a body of knowledge and a narrative of innovation and creativity for trends in Asian management. It brings together some of the best and the brightest of Asia's thought leaders and their solutions to address current Asian challenges, and is focused squarely on Asia and the 60 percent plus of the world's population that resides within a six-hour flight from Singapore.

For most of the contemporary world, these are uncertain, if not turbulent, times. But in Emerging Asia, which has grown from 14 percent of the world's economy to more than 39 percent in a little over 50 years, these are also times of extraordinary opportunity and potential. While the economic clout of China and the established reputation of countries in East and North Asia are acknowledged, they frequently overshadow developments happening in, say, India, which has a median age of only 25—just ten years younger than China—and economies such as Indonesia, Vietnam, and soon Myanmar, which are among the world's most exciting opportunities for growth. Policies throughout the region are also proving particularly adept at attracting FDI, despite the intrusion from time to time of the spectre of financial or political turbulence.

However, Asia's economies have grown faster than its talent has developed, and human capital needs to be enhanced if key gaps in the region's managerial expertise, knowledge and innovation are to be filled.

The first edition of Asian Management Insights provides insights and thought leadership from academics and practitioners on topics as diverse as unleashing creativity in a cross cultural environment to data analytics, in an effort to align the importance of Asia with the advancement of management science. Moreover, with great wealth comes even greater responsibility in the form of ethical and social considerations, a point noted by Ratan Tata.

Asia is a region with tremendous cultural, language, political, demographic, and financial diversity. Scholars, practitioners, and policy makers that ply their trade here are never surprised when another layer of the onion is peeled back—only to reveal yet another opportunity for local adaptation, as well as regional theories and findings that can be taken westward, rather than constantly trying to apply the dominant western theories in a Procrustean manner.

And while regulators, business practitioners and policy makers are challenged to create solutions, those of us in academia face another [perennial] challenge: the inspiration and skilling up of future generations of those regulators, policy makers and practitioners.

Asian Management Insights is quick to acknowledge the challenge and seeks to fill this critical knowledge gap by inviting colleagues and management professionals in the region and elsewhere to share their fresh new academic research, insights and experiences by submitting their articles for review and publication. In our upcoming issues, we encourage submissions from authors about the unique challenges and practices of Asia. Our next issue focuses on managing and practising in the volatile and turbulent environment that is often a feature of this region. Turbulence challenges regulators and policy makers to innovate novel prescriptions in strategy and its implementation. In Asia, the rigorous testing of the status quo has helped the region reinvent itself several times over during the last 50 years; and there are often great riches to be had for those who are able to thrive during turbulence.

As Editor-in-Chief, I would like to thank all our contributors and editorial team, as well as the administration at Singapore Management University, for the hard work that always goes into publication of a journal, especially the very first edition. And on behalf of the team, I take pleasure in welcoming you to our world of shared knowledge and actionable ideas.

DR PHILIP C ZERRILLO
Editor-in-Chief
Asian Management Insights
pzerrillo@smu.edu.sg

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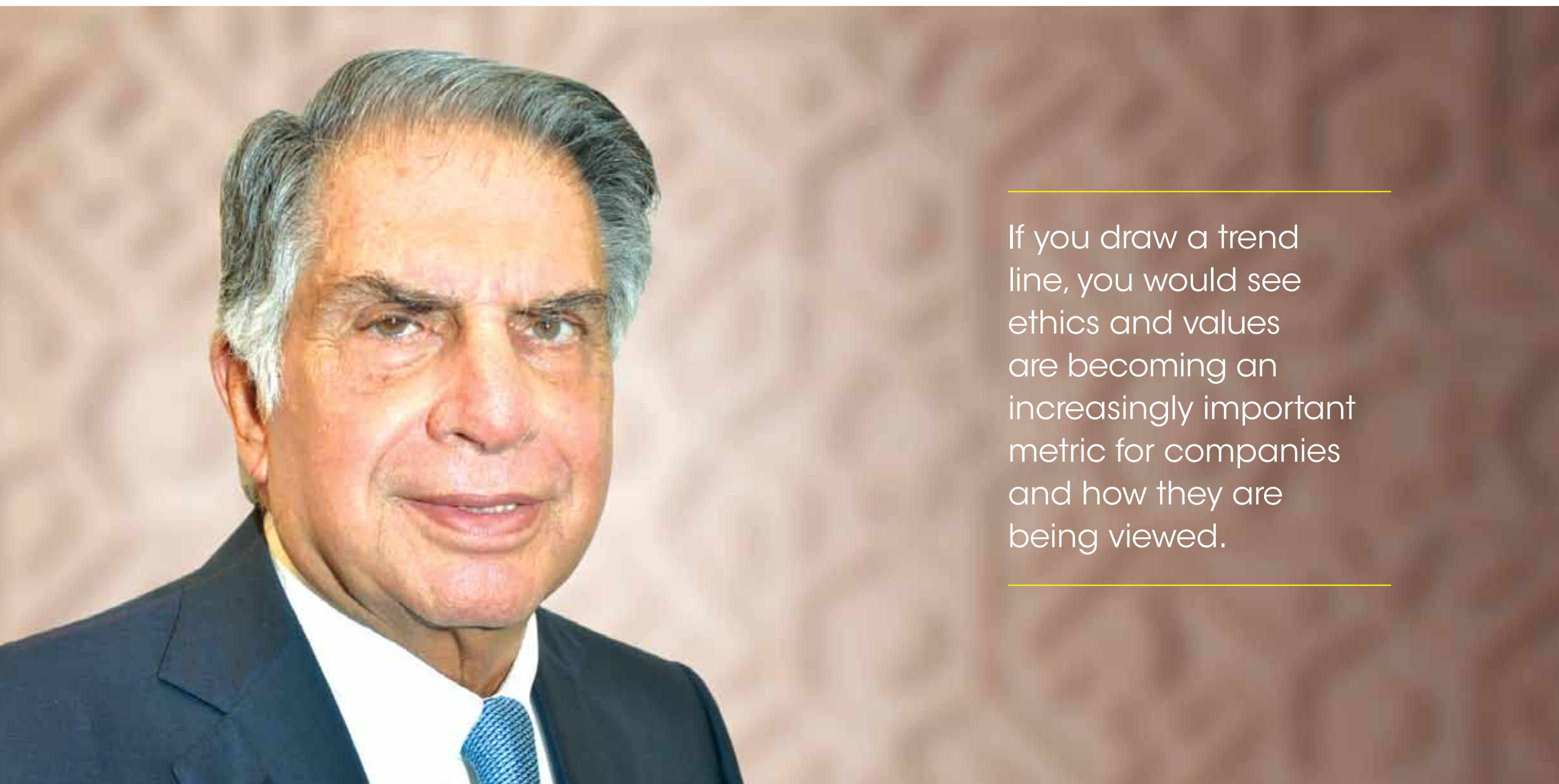
Manager's toolbox: ETHICS AND VALUES

Ratan Tata zeroes in on ethics and values as part of the science of management, and India's current economic journey, in this interview with Philip Zerrillo.



If you draw a trend line, you would see ethics and values are becoming an increasingly important metric for companies and how they are being viewed.

Looking back on your career, what do you think have been the biggest changes and challenges globally in the practice of management?

Thus far, I've seen that managing a company is as cyclical as markets or economies. In boom times, managers are more willing to take greater risks and are looking for faster growth, but will also seek to cut corners. I've seen these cycles where things get very tight, become very closely controlled, and then suddenly a great empowerment of the people takes place, followed by a great urge to go out and grow.

Another change is the increasing importance of ethics and values and it's an issue that seems to be growing steadily within managing groups. One is seeing decades of greed, as they were called, disappear and then come back again. However, throughout this time there has also been a growing respect for, or growing acceptance of, highly ethical companies. On the whole, if you draw a trend line, you would see ethics and values are becoming an increasingly important metric for companies and how they are being viewed.

To what extent does the media impact ethics?

I'd have to say that a segment of the media has turned out to be self-serving. This is not unique to India, and I think it's the face of media everywhere. I'm talking about their constant striving for sensationalism and the damage it can bring to a country, the stability of a government, the distortion of situations and facts–and in not reporting facts as they should be–have all done enormous damage to our country (India). And it's all happening under the protection of freedom of expression.

In my view, this comes down to a lack of responsibility. We saw this during the terrorist attack in Bombay. Ironically, I think the television news was the greatest source of information for the terrorists. If they needed to know what was happening outside, the logistics and so on, all they had to do was watch the news channels. Now the same holds true for much of the problems that we see around us here. News is taken, manipulated, selectively issued. And I think that's all part of the ethical behaviour that I was talking about earlier. You need to protect people's dignity. And I don't see that today.

Have there been technologies that have changed the business models dramatically?

I think the material sciences have changed the capability of products. We've seen products and companies go in a particular vein, and suddenly some of the materials they're using are considered to be toxic, or non-degradable, and the whole industry changes.

People have been talking about emerging markets for some time, although lately the conversation has turned to a question of confidence. What are your thoughts on the future of emerging markets?

I really believe that the emerging markets will continue to be at the forefront. Why? Simply, they are large markets and have large populations. To address these large markets, they are going to demand that companies look at the base of the pyramid rather than the top. I think in terms of economic prosperity, they're behind some of the developed markets, so there's scope for them to grow, and therefore there is potential for companies to scale up in those markets. They're low cost, with the availability of relatively low-cost labour. Then, as education and the knowledge-base improves, with many of the citizens of these emerging markets going to the same colleges and universities as anybody else, the ability to create and the ability to skate on the technology arena is very high.

The only thing that's not there, perhaps, is the same kind of challenge and opportunities that happen in a developed market. A very intelligent, creative Indonesian, for example, might end up in the United States, and never come back, because the opportunity in Indonesia would not be there. But I think that over time, and as prosperity grows, many countries–Singapore being one of them–would like to recreate the same kind of opportunities in their home countries as they might elsewhere, as well as provide the same facilities and the same quality of life.

So I believe that the emerging markets and the African continent would be the real growth area of this world. There will always continue to be a shift of the so-called "dirty" or less attractive processes to the developing world because the developed world wants to be free of them. Meanwhile the developing world will acquire the technology to go beyond those primary processes, and compete with the developed world in global markets.

How can companies unleash the kind of thinking that allows them to look at the bottom of that pyramid?

I think most companies want to enhance margins. In which case there's a natural gravitation to try and market products that have the highest margins that the market can bear, which, by implication, means you want to rise to the top where your margins are large and perhaps the volumes are small. And then there's the more difficult domain, which is the base of the pyramid, where the volumes are huge, but the challenges to be viable at those low margins, are more difficult. The only way for a company to create that environment is to challenge the people to develop products, to put themselves in the shoes of that segment of the consuming population, and to try to give them an exciting disruptive product. There are some negatives in that too. As in the developing world, I think people want to be seen to be prosperous. And if there's a product that's supposedly a low-end one, perhaps the snob appeal factor doesn't allow it to be a runaway success; people don't want to be seen with the lowest level of the pyramid. Nevertheless, I think there's a huge opportunity at the base of the pyramid.

In India, there's been a tremendous shift in liberalisation of the markets over the last 25 or so years. What have been the key constraints or benefits that this has led to and what has been the overall impact that you have witnessed on industry or society?

Speaking as an Indian rather than a businessman, if I look at pre-1991 when the market was opened up and most of the controls were removed, I think the greatest thing that happened is that suddenly the consumer had the ability to choose. Let me give you a couple of examples. In the automotive area, India produced two passenger cars for 30 or 40 years. They never increased the volume. They produced 50,000 cars a year, and you

waited seven years for your car from the time you placed your order, and that was it. Unless you were rich and could import a car at 150 percent duty, and you needed a licence to do that, the only car you could get was the one that you had waited seven years for, or had paid someone a premium to get his slot in the waiting list - and that was it. Today, almost every international carmaker is here in India, assembling one or more of their products in the country. And suddenly consumers have the opportunity to choose. As for the cars that were produced in those days, they hardly exist today. One company has closed, and the other company continues to produce very low volumes.

Cell phones and smartphones are other examples. Who would have thought that we'd have 800 million subscribers in this country? The chance to choose and the desire to be "connected" has been the most spectacular difference that one has seen.

What challenges will the slowing Indian economy present in the short to longer term?

I think the challenges are quite enormous. The slowdown isn't due to an external cause; it's something we've done to ourselves, and the impact of the slowdown is quite devastating for us. We basked in the glory of high growth rates for several years, over eight percent, sometimes briefly over nine, and that led to certain buoyancy in the market, as well as an unfortunate amount of inflation. I think the Reserve Bank reacted to that inflationary trend very harshly, which I can't blame them for, because it had shot up very fast.

But what also happened was that we started to tear ourselves apart with a period of scams and scandals—mostly politically motivated between one party and another—but it knew no bounds, and it drove the government into a sort of bureaucratic paralysis where, quite understandably, a government official would be hesitant to take a decision, lest three years from now someone came and told him he had done something illegal. So the net result was that everything slowed down, from infrastructure and mining to telecom; the courts got involved and made some decisions that they considered correct; the whole country came to a virtual standstill because nobody wanted to take a decision or felt they lacked the protection of their ministry, or the minister, or the government, in terms of what they do.

Do you believe that when there is a lack of certainty, investors are more reluctant to invest?

I think so. I think in periods of uncertainty people want to maximise liquidity and flexibility for themselves, while in boom times they are willing to take greater risks on uncertainty because there's a certain amount of buoyancy in the market. But at a time like this (of uncertainty), investors want to pull back, hold on to their liquidity, put it into bonds or safe instruments, and do whatever they can to conserve cash. This usually means that expansion and growth doesn't take place, new plans and new processes, as well as new products, are put on hold - and those all deter growth.

And I think this trend is unfortunate, as it won't stamp out the corrupt people, because they will still find a way to operate—but it has had a widespread effect on industry in the country.

Is India's young population a demographic bonus or asset? Or is it a challenge?

I think it is a challenge. It's a bonus or a liability based on what you do for the young population. Over 70 percent of the population has access to television; they know what's happening not only in the India around them, but also in the world. It raises their aspirations. Fifty years ago, a young person would probably have just looked at his whole life spent working in the fields. Today the same young person, with some education, is striving for his place in the sun, to make a name for himself. He desires a better quality of life and is going to pursue it. If you cannot give these young people the hope and the opportunity that they want to have, I think you have the grounds for a revolution in 15 years. If, on the other hand, you do give them the opportunity, you create a country that over time will hopefully emerge as an equal opportunity country based on merit, then I think you've got a tremendous bonus that you can exploit, that you can grow, that you can build. And it will have a cycle too, because just like other countries, that workforce will feel discontented and then start to decline. China is going through that cycle today.

Much has been talked about concerning the respective growth of China and India; what challenges do you see ahead for China, versus potential opportunities in India?

I think the political system in China enables China to do things more dramatically and faster and with less pressure of being voted back. I wouldn't say with less concern, because that wouldn't be fair to the Chinese government. I think they've been quite sensitive—but in India, we are paying a price for a running democracy, and in as much as there's no strong single party government - only a coalition of parties—it's much more susceptible to consensus and/or compromise than a strong government. So I would say that while China may have its skirmishes or differences of opinion, more so as time goes on with the government than it had in the past, the country will probably still go down a defined path with much more focus. India is in danger of dissipating itself again in self-criticism, scandals, scams, and so on, all of which end up hurting the country more than anything else. I'm not saying that we shouldn't be rooting out corruption, but we should root out corruption ruthlessly and not dissipate ourselves and blame everything around us and look for the snake under the stone, which may or may not be there. So, I think China will probably continue to emerge as the leader between the two.

What does the recent launch of the controversial space probe mean for India?

I don't know. I've agonised over that myself. On the one hand, I think the scientific community in any country wants to have the sense of not being inferior to those of other countries. India has been a country with a very strong nationalistic feeling that comes from years of foreign exchange shortage. The cost of self-sufficiency for India has been quite pronounced; for many years the state sector operated on the basis of the slogan of self-sufficiency at any cost. People wouldn't sell to you because you were part of the nuclear club that the West didn't like, or you weren't part of certain defence treaties. Thus for whatever reason, you had no choice but to build your own submarines and steel plants, while for aircraft, you'd go to Russia and collaborate. It's very much a Soviet view to elevate the scientific community, its various strengths, and not worry about the rest of the country. So if you were to talk in terms of priorities, I would question the Mars launch for drawing the kind of resources that it did draw. And if it is just to provide status or honours for a group of scientists, then I think it's wrong. However, if that scientific endeavour leads to a widely dispersed technology spin-off, then that's great.

If you were talking to a young manager about the future, what would you say to them?

I think I'd like to go back to the issue of values and ethics because if you look at the last 20 or 30 years, there's been a real destruction of the fabric of value and ethical behaviour in the country. And I believe that in a corrupt system, there's a giver and a taker. Most people look at the taker, but there's also a giver, usually from the private sector.

And I think one excellent thing that could make a difference, would be for every manager to take the view that they're not going to participate in this corrupt system, and that they're not going to get ahead over their competitors by confabulating in dark corridors of power in the night, but that they're going to fight in the marketplace openly and ethically, and that the best person wins.

The fact is that, speaking generally, we are so negative about our competition. We can't sit in the same room as one industry and seek what we should be seeking in terms of government policy and so on. There is a great urge for 'selective' protection or competition.

We tend to be five industry leaders going to the government privately and trying to get "something for me, not for others", or "do it for me, but make sure he doesn't get it", which means we're fragmenting ourselves in terms of the strength of the industry.

So the first thing I think I would do is to seek the manager's commitment to an ethical and a value-based operation and personal lifestyle. That will go a long, long way. I would also like to see young managers not look at their career only from their personal prosperity, but to give back something to their community or the country in general. And I'd also like to hope that this would be not something forced upon them by mandate or otherwise. This would help take away the elitist status of managers and enable them to become greater contributors to a country's prosperity.

Ratan Tata
is chairman, Tata Trusts

Philip Zerrillo
is the editor-in-chief of Asian Management Insights and dean of Post Graduate Professional Programmes, Singapore Management University

Management EDUCATION

By Howard Thomas

The path behind and the road ahead

Business schools have been among the great success stories in higher education over the last 50 years. At a time when many university systems around the world are struggling financially, there continues to be a steadily growing demand for management education. However, the field is now in a state of flux. Those of us who work within the discipline are currently engaging in an extended discussion about the very foundations of management education. We are rethinking the objectives of the field and are considering our best practices as we move forward.

I recently co-wrote a monograph entitled "Promises Fulfilled and Unfulfilled in Management Education" together with Lynne Thomas and Alexander Wilson[i] to celebrate the 40th anniversary of the European Foundation of Management Development. In this volume, we consider the original goals of management education; we examine what has been accomplished and what remains to be done. As we continue to evaluate the key issues that business schools will need to engage with in order to succeed in an upcoming volume on the Future of Management Education, two main ideas have particular interest: the value of ethics training and the importance of a global outlook. I will examine both of these ideas here.

The state of the discipline

Management education began in the 19th century with the original purpose of giving the emerging class of business managers a strong foundation in matters both practical and moral. It was designed to enhance the status of professional managers in public life. The earliest schools, such as the Wharton School and Harvard Business School, pioneered management programmes and the idea of business schools soon grew in popularity. Europe, France, Germany and the United Kingdom all established business schools and have been important catalysts in the expansion and globalisation of the field.

In the 1950s, as the notion of the business school became a recognisable concept, management education practitioners went through a period of soul-searching. Studies carried out by institutions such as the Ford and Carnegie Foundations critiqued business schools for lacking research output, academic credibility and legitimacy. The studies proposed that business schools adopt the model established by the social sciences, that is, generating scholarship with a clear focus on analytical models and scientific rigour. American and European business schools took this advice to heart and began working towards this model.

The problem, however, is that business schools were never designed to have a purely academic focus. They were always meant to provide pragmatic, real-life management skills to managers who would be going back into the marketplace. In the 1970s and 1980s, management academics and management consultants began writing readable books that addressed strategic issues such as competition, diversification and organisational change through the format of stories and cases. While these books were popular, they didn't engender the kind of intellectual and academic legitimacy that business schools wanted to achieve.

> Despite these identity struggles and occasional moments of crisis, business schools have grown in popularity over the years and are resilient to fluctuations in the economy.

Today, we are still struggling to achieve the fine balance between the academic and pragmatic approaches to management education. Business schools continue to face an image problem. The general perception is that management education is not a serious discipline and does not result in the professionalisation of management. Those of us who are practitioners within this field have our work cut out for us. We need to wrestle with our identity as a discipline. We need to work through very foundational questions: What is business for? What is our value as business schools? Who are the key stakeholders? How do we achieve a balance between treating management as a science and an art?

Teaching ethics and responsibility

As management education moves forward, it is important to consider how the field will deal with external shocks and crises. The financial crisis of 2008 and the ethical failures of companies such as Enron and WorldCom have had an impact on how business schools are perceived. In Europe and Asia, these crises and scandals have been taken as evidence that it is vitally important to study ethical issues in management education. In North America, there has been great concern about how business schools should be responding to the recession.

When these external shocks unfold, media commentators are quick to criticise business schools, whether fairly or unfairly. Business schools have been made to appear complicit in training the architects of these financial crises. From within the world of management education, the criticism has been that business schools tend to adopt a reactive approach to handling these scandals. Going forward, it will be important for us to think proactively about how to address the question of ethics in the discipline.

Our studies show that business school students become much more aware of issues of corporate social responsibility (CSR) and sustainability. They are putting pressure on schools to promote sustainability through organisations such as the U.N. Global Compact, the Global Leadership Responsibility Institute (GLRI) and Net Impact, a global student movement invested in the responsibilities of business. In response to student demand, business schools have started to acknowledge the importance of CSR and sustainability, and are increasingly making them a core part of the curriculum. This is a laudable move forward and it is likely to continue in the years to come.

In conjunction with an emphasis on responsible business, it will be important to include courses that explicitly address ethics and risk management. This means more than just studying the consequences of scandals, but thinking through the everyday ethical choices that managers face when working with other people and other businesses. It will also be important for the more quantitative branches of business schools to review the complex mathematical models involved in risk management. Enlightened mathematical modelling can go a long way to help mitigate the risky decisions that led to financial crises that we have seen in recent years.

However, it is also important for business schools to articulate that they are not entirely to blame for the corporate scandals that have taken place. It many ways, it was unfair that business schools were made scapegoats for these crises and scandals. Indeed, *The Economist* noted that the top executives who were on trial for corporate corruption are notable for their lack of business school qualifications. Nonetheless, at this critical turning point for the field, thinking carefully about teaching future managers how to be more ethical and responsible is a valuable step in the right direction. It will also prepare students to think more broadly about how to prepare for and deal with crisis. Over time, we believe that the proliferation of courses on ethics and responsibility will change the negative image that business schools have acquired.

> Business schools have been made to appear complicit in training the architects of these financial crises.

Globalisation

The other great challenge of the future will be to make management education a truly global discipline. Globalisation and its many ramifications involving strategic alliances in global trade have had a significant impact on management education. They have forever changed the competitive dynamic of business. The reach and effects of globalisation are specific to each particular region and cultural context. In the field of management education, it is imperative for us to give students the ability to recognise the particularities of individual regions, while also giving them the ability to think beyond borders. Within this brave new world, specialised knowledge is no longer enough: management students need to be trained to have an integrated international worldview. Business schools need to move toward a model in which national boundaries no longer matter and in which a knowledge of cultural and contextual intelligence is essential.

While business schools first emerged to deal with the specific management issues at work in America and Europe, over the last decade, there has been a marked increase in demand for a uniquely Asian business school model following the shift in the global economy from west to east. This shift provides new options and opportunities for management education to expand in these regions. Business schools around the world need to incorporate international and multicultural thinking into their curriculum to prepare students to do business in a globalised marketplace.

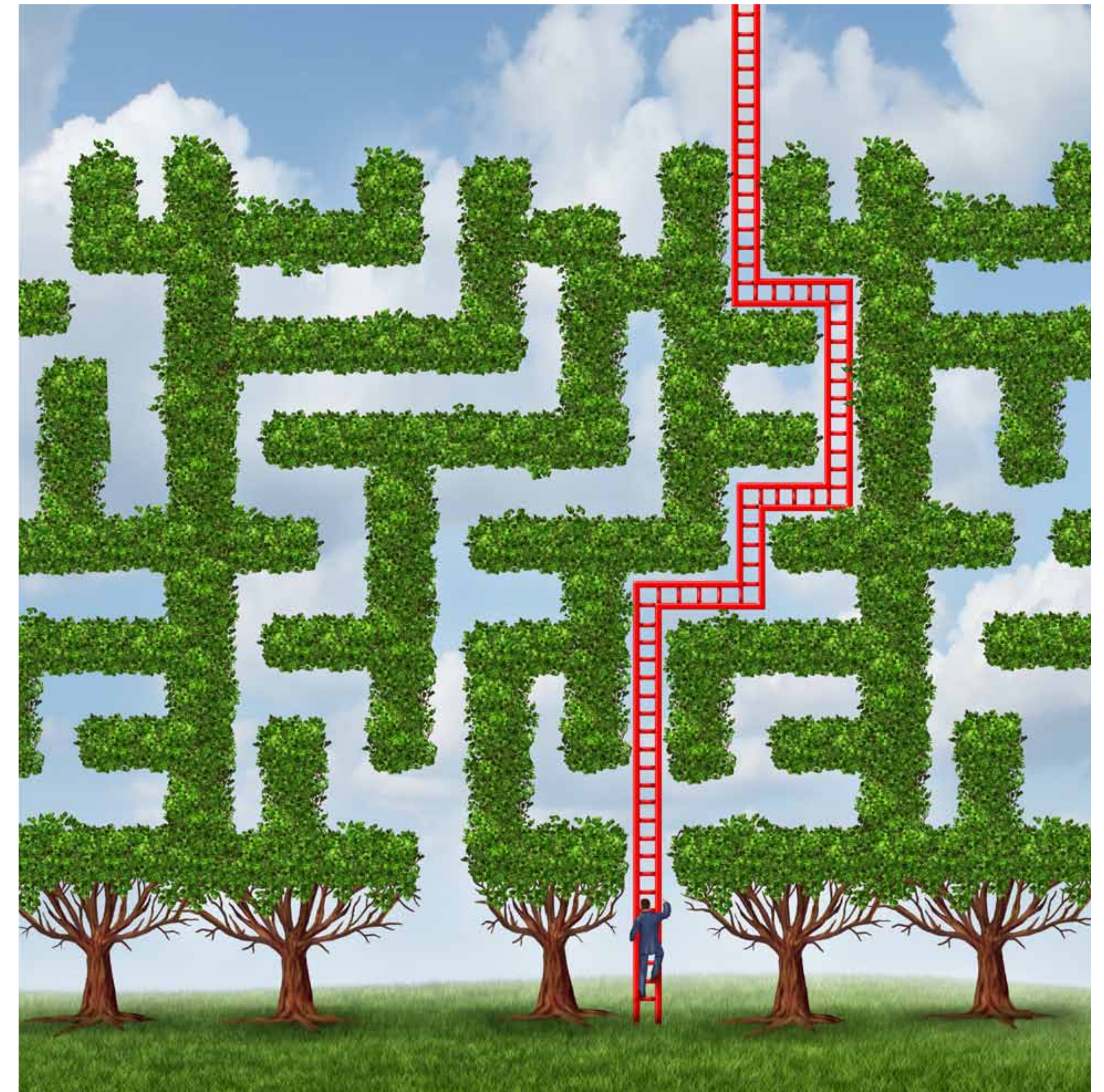
The European business schools are ahead of the curve in terms of their international outlook. They have traditionally had a more diverse student body and have incorporated a richer array of cultural perspectives into their curriculum. The European approach can serve as a valuable point of departure as management education thinks ahead. However, the inexorable shift in the balance of power to Asia means that business schools will need to move away from an Anglo-American focus. There would need to be a much more balanced emphasis on Asian, European and American viewpoints in management education.

There is now more demand for MBA and executive MBA programmes within Asia than ever before. In Japan, following the recession, some managers have chosen to pursue an MBA degree to improve their chances as they enter the job market. Japanese companies seeking to expand abroad are also sending employees to MBA programmes overseas. In China, Singapore and India, business schools are now emerging that will soon rival Harvard, Stanford and INSEAD. Local Asian business schools are attracting students of the highest quality and graduates of these schools are receiving salaries that are competitive with their counterparts in the West.

For business schools around the world to succeed, they need to share resources and exploit opportunities beyond their borders. This will mean forging alliances with other schools and actively engaging in research that has a cosmopolitan outlook. Students in classrooms from Mumbai to Massachusetts need to be thinking about the cross-cultural dimensions of managing in a global environment. The task of developing a truly global manager is no small feat. In today's world, managers need to be able to operate effectively anywhere in the world with a rich understanding of the economic and cultural context in that place. One important way to give students this global outlook is to encourage study abroad programmes and facilitate exchange programmes that allow students to think through business challenges in other parts of the world. It will also be important for business schools to have a diverse faculty that includes global perspectives.

Students in classrooms from Mumbai to Massachusetts need to be thinking about the cross-cultural dimensions of managing in a global environment.

There is now more competition between business schools vying for the same group of talented students from around the world. This competition offers an opportunity for management programmes to develop rigorous courses that will appeal to this wider, more diverse range of individuals. It also means that schools can learn from one another and identify which methods and approaches that are particularly effective. There is so much localised knowledge that is embedded in universities around the world; there is great potential for this knowledge to be transferred, particularly as technology continues to make the world a smaller place.



The road ahead

Despite these identity struggles and occasional moments of crisis, business schools have grown in popularity over the years and are resilient to fluctuations in the economy. The continuing demand for the MBA degree indicates that there are aspects of this existing post-graduate management education model that are very worthwhile. Part of this success can be attributed to the fact that they serve the specific needs of the communities that they relate to. Every day, they train some of the world's brightest managers, imbuing them with the skills and knowledge they will need to be successful business leaders. As I have demonstrated throughout this essay, this is an exciting time for us: we are in a period of transition. As we enter this turning point in the field's evolution, we can play a part in shaping the future of the management education and ensure that it remains relevant in the modern, global world of business.

Howard Thomas
is dean of the Lee Kong Chian School of Business (LKCSB) at Singapore Management University

The material in this article is derived from the author's recently published book: "Promises Fulfilled and Unfulfilled in Management Education".

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Unleashing creativity

ACROSS CULTURAL BORDERS

As the global economy integrates and companies pursue opportunities outside their traditional borders, it is increasingly important to innovate across cultural borders. This article explains how individuals can improve cross-cultural creativity.

By Roy Y.J. Chua

Hollywood studios are teaming up with Chinese film experts to capture the local market. Recent hits such as *Iron Man 3* and *Pacific Rim* added carefully crafted subplots and achieved box office success in mainland China. The reverse trend–Chinese film companies scoring hits in the United States–is still waiting in the wings. As Yu Dong, CEO of China's Bona Film Group puts it: "We lack international experience, in general.[i]"

At first glance, it might seem obvious that tackling cross-cultural innovation challenges requires creative individuals with deep foreign experience. As intercultural business relationships become the norm, professionals are frequently working in global teams to address everything from complex supply chains to integrating new acquisitions. Knowledge of foreign markets and creativity would seem to be the requisite skills. As counter-intuitive as it seems, however, my research has found that this combination alone is no guarantee of success.

Part of the issue is how we think about creativity. We often view it as sudden flashes of brilliance or a rare gift endowed to the lucky few. However, research has demonstrated that creativity requires a great deal of method. It isn't always a sudden flash that produces an idea that didn't exist before. More often, creativity stems from novel combinations of existing ideas that address a problem in a fresh, new way. Notable examples span quite the gamut–from luxury brand Shanghai Tang's fusion of Chinese culture with Western design aesthetics to China's Haier group developing washing machines for farmers to clean both clothes and potatoes.

As business becomes more global and competitive, it is critical for companies to ensure that such novel combinations come to the fore. However, knowledge and creativity alone may not suffice. They need the support of a third skill in order to thrive–a mental habit that psychologists call *cultural metacognition*. The term refers to a person's reflective thinking about what he or she knows about a given culture. It is analogous to the heightened awareness we have when driving in foreign cities[ii]. We don't take our driving skills for granted and assume they will steer us correctly. We pay close attention to road and traffic signs to guide our skills in its new context. This same heightened awareness of, and reflection about, other cultures lies at the heart of unleashing creativity across borders. They help avoid the pitfall of engrained knowledge resisting novel combinations of ideas. They build trust in cross-cultural interactions which in-turn drives the free flow of ideas that allows these combinations to emerge.

> *Cultural metacognition…* refers to a person's reflective thinking about what he or she knows about a given culture.

When knowledge is too much of a good thing

When charged with responsibilities in different cultures, professionals are often deluged with information on everything from social norms to political and economic issues. Cultural knowledge is inherently complex and can span norms, values, customs, history, and traditions. For any two cultures, there are bound to be both differences and similarities. As a result, the more knowledge one possesses, the more difficult it can be to separate the wheat from the chaff and bring the right knowledge and experience to bear on a given creativity challenge.

"The more you know, the better", however, is the conventional wisdom. But I doubted that this is actually the case. In fact, too much knowledge may actually hamper creativity and limit managers' ability to solve problems.

Cultural knowledge is inherently complex and can span norms, values, customs, history, and traditions. For any two cultures, there are bound to be both differences and similarities.

In a study that my colleague, Kok-Yee Ng of Nanyang Technological University, and I conducted recently[iii], we examined the influence of cultural knowledge and metacognition on cross-cultural creativity. In the study, we worked with 89 business students from around the world who were completing an international organisational behaviour course in Singapore.

At the start of the course, we assigned students to teams of five to seven to work together on the projects. While working on these projects, students had to apply their creative thinking to various challenges including cross-cultural negotiations and solving management problems in a global context. Students also had ample opportunities to observe the creativity of their team members.

After several weeks, three randomly selected classmates evaluated each student in terms of their cultural metacognitive skills, creativity and cultural knowledge. At the end of the course, all team members rated one another's creativity.

The results were illuminating. Contrary to conventional wisdom, more cultural knowledge did not translate into greater creativity unless it was accompanied by the habit of cultural metacognition. Cultural metacognition helps avoid two pitfalls that can stand in the way of effectively leveraging creativity and knowledge–cognitive overload and cognitive entrenchment.

Cognitive overload sets in when individuals acquire such large amounts of factual knowledge that its volume impairs their ability to sieve through all the possible options and arrive at the best choice. Similarly, copious knowledge can result in cognitive entrenchment–when its breadth and depth engrains thinking to the point of resisting ideas that fall outside of what one knows.

Foreign designers at Shanghai Tang, for example, had to overcome their entrenched thinking before they could help the company succeed as a global luxury clothing and accessory brand. Today Shanghai Tang is known for innovative designs that blend Chinese cultural elements with Western clothing styles. But the innovative blend wasn't always the company's hallmark. After opening a large store in New York in 1997, it had to move to a smaller location just 19 months later. Joanne Ooi, who joined as creative director at the time, argued that the company's designs were too "costumey" to have wide appeal[iv].

Although foreign designers spent a great deal of time studying Chinese history, aesthetics and clothes, their designs would often simply mimic iconic Chinese garments such as the *Qipao*, a figure-hugging dress for woman. Ooi's design objectives helped designers move forward by questioning their ingrained assumptions. For example, she felt that some of the company's designs should be comfortably worn with jeans. The objective likely helped designers to open their minds and embrace ideas outside their assumptions about Chinese clothing.

To avoid the trap of cognitive entrenchment, managers can do three things. First, they can take a cue from Ooi and pose questions and ideas that challenge ingrained mental sets. Inquiry is a powerful tool to uncover deeply ingrained assumptions. Second, managers can also help remove knowledge log-jams by making sure employees are actively engaged in activities beyond their specialties. Google, for example, allows employees to devote 20 percent of their time to projects outside their primary responsibilities. That activity provides a constant impetus to think outside the knowledge areas that employees are familiar with[v]. Third, employees should be encouraged to build social networks involving people from diverse cultural and functional backgrounds. Doing so ensures that one does not get entrenched in one world view. What underlies these three approaches is the development of metacognitive skills in employees, a mental habit that is paramount to breaking down cognitive barriers (See "Putting it to work" below).

Trust and creativity

Although professionals must solve creative problems on their own, more often than not they need to work with others. In cross-cultural creative collaboration, trust is a key ingredient. People must feel comfortable opening up and sharing insights if they are to develop novel combinations of ideas.

Is cultural metacognition also a critical ingredient for creative solutions when people from different cultures collaborate? Does it foster levels of trust needed for creativity to flourish? To find out, my colleagues (Michael Morris and Shira Mor of Columbia University) and I asked a group of executives attending an executive MBA programme in the U.S. to provide lists of associates from other cultures with whom they had worked[vi]. The executives rated their own level of cultural metacognition: the extent to which they refined cultural knowledge based on their experiences and then made use of those refinements to begin anew. Their associates assessed whether the executives developed win-win solutions when working with people from other cultures and if their work was marked by creativity.

I also examined two types of trust. The first is what we call trust from the

head (cognitive trust). This type of trust emanates from the confidence one has in a person's accomplishments, skills, and reliability. The second type of trust—trust from the heart (affective trust)—arises from feelings of emotional closeness, empathy, and rapport. Most friendships and personal relationships are based on this type of trust. It is also critical to cross-border creative collaboration. How comfortably someone freely shares ideas has much to do with how much affective trust they have in the people with whom they are collaborating. Professionals must be willing to make themselves vulnerable to others. New ideas, after all, can be easily ridiculed, or even stolen.

Our study found a significant relationship between the habit of cultural metacognition, affective trust, and the creative fruits of collaboration. High levels of cultural metacognitive skills create stronger affective trust, which, in turn, drives the free sharing of ideas needed for creativity. The study demonstrates that people feel more comfortable when they have developed the multiple dimensions of a personal relationship. In fact, the affective trust that comes from a personal relationship can be very difficult to achieve in intercultural collaborations without cultural metacognitive skill.

Often, the advice to improve intercultural collaboration hovers on the surface and targets symptoms instead of causes. When it comes to debating or discussion style, for example, managers are advised to explicitly set norms for collaboration and, if necessary, make accommodations.

The heart of the matter, however, goes much deeper. Demographic characteristics such as nationality or ethnic background correspond to significant differences in people's views of the world, motivations, and behavioral tendencies. If we don't thoroughly understand these differences and interact with foreign counterparts in a conscious meaningful way, we can derail any creative collaboration. We end up reinforcing people's sense of "otherness", making them feel misunderstood or stereotyped. When that happens, people won't open up and share ideas.

The importance of affective trust and how to develop it can't be underestimated. Imagine an American manager working for Chinese company Haier. He or she is leading a team of Chinese and Americans to address call centre complaints that washing machines are breaking down because farmers are putting potatoes in them. The Americans might challenge the Chinese to come up with better ways to explain to customers what a washing machine should be used for. Without a significant level of affective trust, it is hard to imagine a Chinese team member comfortably advocating what Haier ultimately did—retooling a clothes washer to handle potatoes too. Such a provocative idea wouldn't be aired if the Chinese team members don't feel genuine rapport with the Americans.

The proof of the pudding

The studies discussed above focus on individuals evaluating others. It was important to test these assumptions in a situation that simulates real life. I also wanted to know if trust is as important as innate creative ability when it comes to the creative fruits of multicultural collaboration.

To find out, I conducted a laboratory experiment, tasking participants with creating a new chicken dish for a soon-to-open restaurant. I recruited 236 students at Harvard with different cultural backgrounds—European-American, African-American, and Asian-American.

To assess the creativity of each participant as a baseline for evaluating the impact of trust on creativity, I asked each participant individually to develop a chicken recipe using a list of ingredients from different cultures—American, Indian, Chinese, and Thai. I then paired each

participant with someone from a different cultural background than their own. Half were asked to immediately develop a recipe together. The other half had an informal conversation before they started to work. The conversation topics provided a chance to build affective trust by sharing personal experiences in their cultural contexts: significant events they experienced during school and how those would have an impact on their careers and lives.

Professional chefs judged the dishes, evaluating the recipes for their creativity. The results were telling. Irrespective of participants' baseline creative ability, there was a clear relationship between cultural metacognitive skill, development of trust and the creativity that ensued. Pairs that had one individual with high cultural metacognitive ability collaborated well. And their dishes scored higher marks from judges when they were able to get to know each other first. This effect was the same even after accounting for the individual's baseline creativity assessed in the first step.

The proof was in the pudding. An individual's creativity *of and in itself* doesn't always guarantee the most creative collaboration outcome. When working with a partner from a different culture, high levels of cultural metacognition on the part of at least one of the individuals is needed to build the type of trust that fosters the sharing of ideas that produce creative results.

Putting it to work

To build trust in intercultural business relationships, it is important to understand the barriers. The first is mind-set. People from different cultures don't always share the same norms, mental approaches and assumptions. East Asians, for example, tend to see issues in a more holistic fashion than do Westerners who focus on specific issues. The resulting dissonance reduces trust, which in turn impedes the effective exchange of information.

The second is behavioural differences that define appropriate conduct. These are often taken for granted by individuals in their own cultures. For example, recent studies by researchers at INSEAD and the University of California at Berkeley found that if a negotiator perceives anger on the part of his or her counterpart, that perception affected European-Americans and Asian-Americans differently[vii]. Because the blatant expression of anger and negative emotions is considered inappropriate in Asian cultures, when dealing with an angry negotiating counterpart, Asian-Americans were less likely to make concessions than were European-Americans. This study implies that any mismatch in behavioural and communication style in cross-cultural interactions can easily erode trust.

Finally, vacillating motivation can be an issue. The difficulty in achieving a shared understanding with partners from another culture can drain energy and tempt someone to walk away. Perseverance is critical to building trust and confidence that all participants are committed to finding a solution[viii].

To ensure that employees have the ability to build affective trust with their counterparts from other cultures, companies should expand their training programmes beyond what they typically offer. Often, cross-cultural training focuses on social customs, etiquette and negotiation strategies. The focus should, however, expand to include deep cultural knowledge such as learning the local language—language can be a powerful tool in navigating foreign cultures. Knowing the other person's language enables one to better take perspective and understand his or her true motivations and interests, a prerequisite for building rapport and trust.

As our research demonstrates, however, overcoming these barriers is not only a matter of cultural knowledge. It also requires skilful cultural metacognition to shape that knowledge by testing it in actual experiences. Executives who have mastered this habit do four things[ix]. They consistently:

- Build awareness of their own cultural assumptions
- Challenge these assumptions—i.e. to what extent do they help predict how people will behave and react?
- Modify assumptions that don't apply
- Plan to use the new knowledge in upcoming interactions

To build this skill, professionals need to carve out time to reflect on their intercultural

> As business becomes increasingly global, creativity and cultural knowledge are central to developing innovative solutions that will work in vastly different cultures. Individuals also need to develop the mental habit of cultural metacognition.

encounters. They should view each experience in the context of these questions:

- What cultural assumptions am I making? What assumptions are people from other cultures making about mine?
- Do my assumptions and knowledge apply to a given situation such as a negotiation? Or do they reflect a different setting such as a social gathering?
- What challenges could arise? How can I address them? What do I need to know to avoid misunderstanding?

In addition, individuals should actively observe any interaction and realise that their assumptions might not be accurate or applicable in a given context. For example, it is common to assume that Chinese are concerned about losing face and will avoid expressing opinions candidly. However, instead of simply making such an assumption, professionals should observe how their counterparts interact with one another and see if it always fits with the assumption. Although face-saving is important in China, the degree of that importance can vary. Without that understanding, it is easy to erode trust and avoid frank and useful criticism out of a desire to save face for the partner. For example, an American executive who is concerned about saving face for his Chinese counterpart might avoid voicing his true opinion about the Chinese partner's numerous ideas, only to later find themselves in a project quagmire.

This less-than-desirable outcome might lead the two partners to question whether they could work effectively together. Had one of them exercised cultural metacognition during the collaboration, the outcome might be different. Engaging in cultural metacognition habits when giving feedback during cross-cultural collaborations would make individuals from face-saving cultures, such as China, Japan and India, feel understood rather than offended, which can pave the way for more candid discussions, a critical process for successful creative collaborations.

Conclusion

As business becomes increasingly global, creativity and cultural knowledge are central to developing innovative solutions that will work in vastly different cultures. However, the combination of cultural knowledge and individual creativity alone may not suffice; individuals need to develop the mental habit of cultural metacognition. Mastering that habit assures that they can effectively bring their knowledge to bear on cross-cultural creative challenges and build the trust needed for a free sharing of ideas when working with people from different cultures.

Roy Chua
is assistant professor in the Organizational Behavior unit at Harvard Business School

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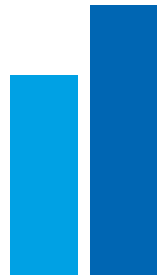
Surviving beyond a third generation

Family-owned businesses' continued survival is unsure. Research indicates the most likely cause is their pursuit of professionalisation.

By Andreas Raharso

Family-owned businesses (FOBs) are the backbone of the economic systems in most countries. A 2012 Ernst and Young report disclosed that family businesses make up more than 60 percent of all companies in Europe and the Americas, and account for about 50 percent of total employment. In Asia, the situation is similar. According to a 2012 report by Credit Suisse across 10 Asian markets, more than 70 percent of Asian firms are family-owned, accounting for nearly half of all listed companies and 32 percent of total market capitalisation. These businesses also employ 57 percent and 32 percent of all listed companies' employees in South Asia and North Asia respectively. Thus, their role in the Asian economy is of tremendous importance.

However, their continued survival is uncertain. The global, multidisciplinary professional association for family enterprise, Family Firm Institute, reports that around 70 percent of FOBs will not survive into the second generation, and 90 percent will not make it to the third generation. The



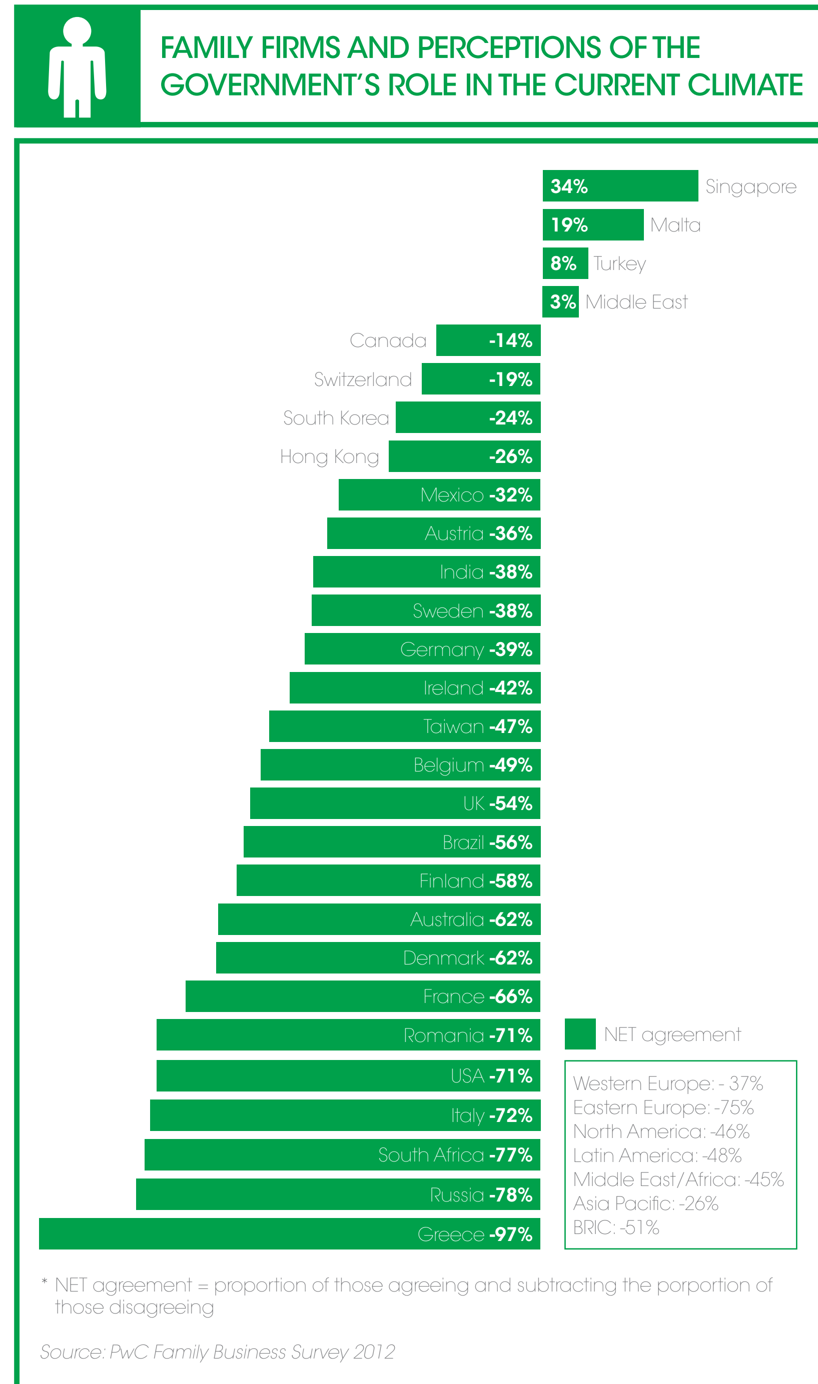
70% will not survive into the second generation and **90%** will not make it to the third generation.

question is why? Hay Group research indicates that FOBs view the lack of government support as the major factor threatening their survivability, whereas in reality the most likely cause is their pursuit of professionalisation. Professionalisation can often lead to the deterioration of family relationships if it is not set firmly within a basis of mature family capital. Thus those that focus on developing rich family capital are better prepared for the risks associated with professionalisation.

Over-reliance on government support

Many of today's top Asian FOBs have had significant support from their government, a fact best illustrated by South Korea's FOBs or *chaebols* that emerged in the 1950s and marked the rise of protectionism. The chaebols were then some of the world's largest FOBs and appeared after the departure of the Japanese in 1945 when the newly formed government entrusted a handful of Korean businessmen with the assets of several Japanese firms. Fast-forward to the 1990s and several had grown into household names, such as Samsung, Hyundai and LG. Similarly, many Asian countries adopted protectionist policies to develop their domestic industries while defending themselves from foreign competition.

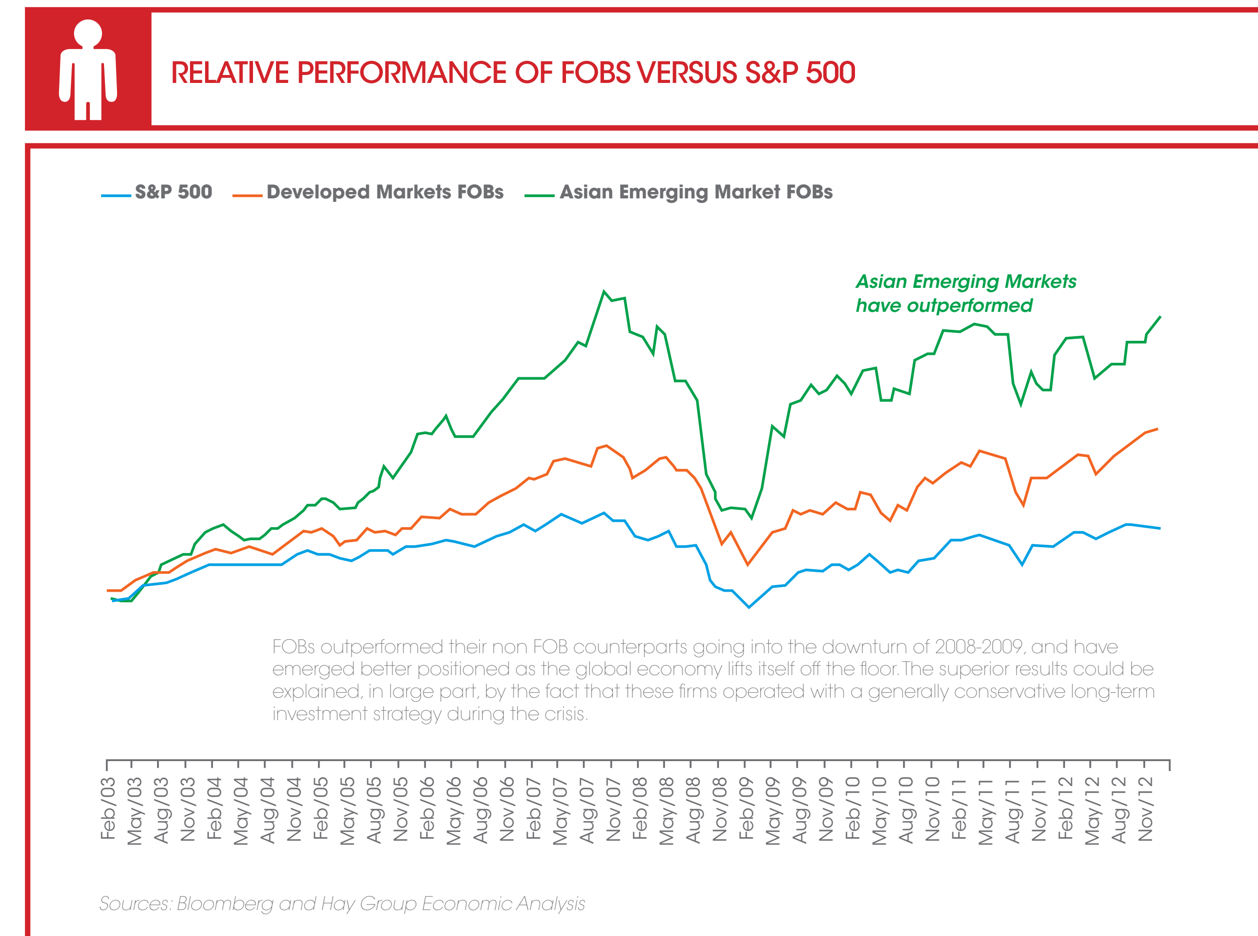
However, rapid globalisation over the last few decades has changed the business climate drastically. This is even more apparent in countries like China, where post-1998 economic reform have relaxed protectionist policies. It is therefore not surprising that a PwC 2012 report on global family business indicates that approximately 26 percent of FOBs in the Asia-Pacific region feel negatively about the government's role in helping them survive in the current business climate.



According to a report by the Conway Centre for Family Business, the life span of family firms has reduced significantly over the past few decades. In the 1990s, firms would typically last 50 to 60 years (equivalent to two to three generations) compared to their current average span of about 24 years (about one-and-a-half generations). We therefore ask to what extent is the shortened life span a result of the lack of government support?

> These businesses also employ 57 percent and 32 percent of all listed companies' employees in South Asia and North Asia respectively. Thus, their role in the Asian economy is of tremendous importance.

Our analysis shows that their performance is not as heavily dependent on government protectionist policies as they think it is. This view is substantiated by their performance during the financial crisis. During an economic downturn, most governments struggle to find the perfect mix of interventionist policies, and are thus unlikely to give preferential treatment to particular industries. However, notwithstanding the Asian and global financial crises in 1998 and 2008, FOBs all over the world, including Asian ones, outperformed their non-family controlled counterparts in the period 2003-2012.



Professionalising the FOB: A lethal threat

Hay Group research believes that the greatest threat to a FOB's life span is not the lack of government support, but the pursuit of professionalising the business. This requires the company to clearly distinguish family and business interests, and entails them tapping into essential external resources, such as recruiting and retaining talented non-family employees. In reality, professionalising can be both a blessing and a curse–it can provide family enterprises with the necessary tools for business evolution, but may also see less priority placed on those family relationships that supported the business during its early days.

FOBs face many unique challenges that need to be resolved using the strength of family ties and relationships. Pursuing professionalisation should see them being able to tap into the strength of the family capital–and by not doing so, problems can be accentuated, as most of their attention is diverted to efforts to achieve professionalisation rather than resolving the problems.

Moreover, mismanaged professionalisation attempts can make matters worse. Many FOBs are faced with an inherent conflict that typically arises from their inability to separate business and personal affairs. Sometimes the feuding is due to the varying interests of each family member, or a combination of personal egos and rivalries that spill into the business environment.

Keeping it in the family is one thing, but forcefully involving family members who do not fit the needs of the business is another. There are numerous occasions in which FOBs have family members on their payroll holding top-level positions, not because of the expertise they lend or the merits of their professional experience, but by virtue of them being related to another family member. This form of special treatment ends up dividing employees by creating different classes among them. It can also be a great demotivating factor for non-family member employees. One of the biggest criticisms of growing family-owned businesses is that they do not provide opportunities for non-family members to advance into leadership positions. Without the opportunity to advance or take on a leadership role, many talented and ambitious employees will move on to better opportunities outside. FOBs need to recognise that their employees should not be discriminated against based on their ties to the family, as they cannot survive without talented employees who represent the lifeblood of the business.

> Pursuing professionalisation should see them being able to tap into the strength of the family capital – and by not doing so, problems can be accentuated, as most of their attention is diverted to efforts to achieve professionalisation rather than resolving the problems.

> The biggest challenge that remains is succession planning.

The biggest challenge that remains is succession planning. Although not a difficult decision for a non-family business, it can be a daunting task for FOBs, which have two objectives that are of equal weighting; one, to ensure sustainability of the business, and second, to ensure the family has a controlling interest in the business. It is the latter that gives rise to the difficulties in succession planning. In an interview with the *Financial Times*, Yupana Wiwattanakantang, associate professor of finance and corporate governance at the National University of Singapore Business School shared that the reason succession planning is difficult for Asian FOBs is because leaders of family businesses in Asia tend to be patriarchs rather than matriarchs, and these men want to continue to remain at the helm of the organisation until their dying day. This mentality prevents them from training or selecting a proper successor, resulting in a void that cannot be filled when the need arises. FOBs thus need to have a clear succession plan, or they are setting their business up for failure.

> …the reason succession planning is difficult for Asian FOBs is because leaders of family businesses in Asia tend to be patriarchs rather than matriarchs.

THE AMBANIS' POWER OF WILL

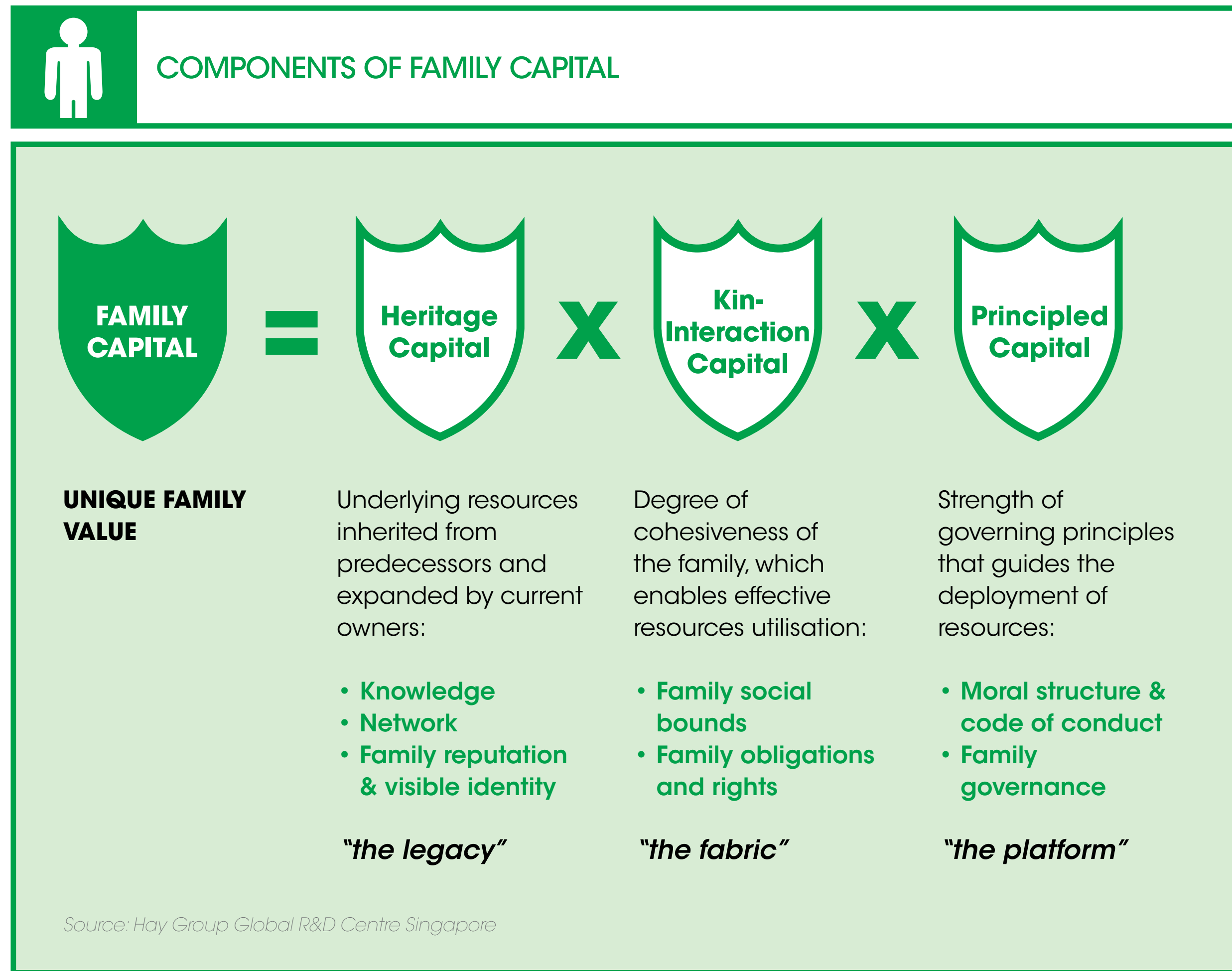
The famous Ambani brothers' feud is well-known throughout Asia. However, what was most alarming is the lack of succession planning by their father Dhirubhai Ambani that led to the situation. In July 2002, the founder of Reliance Industries in India passed away without leaving behind a will or a formal succession plan for his empire. Since then, the brothers have been involved in a series of constant struggles for power that eventually led to the demerger of the company, brokered by their mother in 2005. These struggles gave Mukesh Ambani control of oil and gas, petrochemicals, refining and manufacturing while the younger brother, Anil Ambani took control of electricity, telecommunications and financial services.

Business Insider: The Full Story Of The Massive Feud Between The Billionaire Ambani Brothers (http://www.businessinsider.com/ambani-brothers-feud-reliance-2011-05?op=1#ixzz2Vte2tuw5)

Prescribing *Family Capital* as a cure

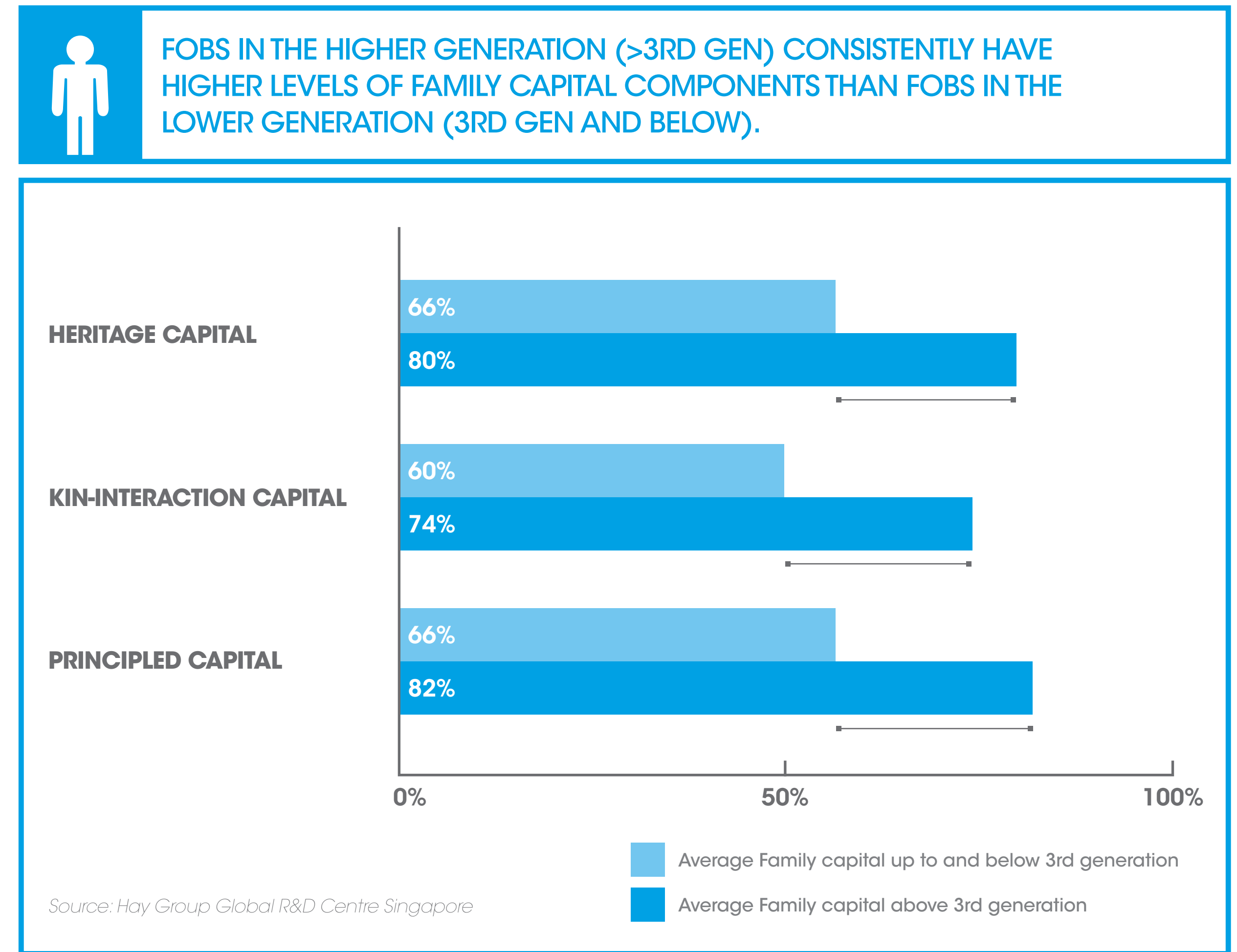
An extensive global survey in 2012 of 160 family businesses (including 35 Asian firms) allowed the Hay Group to identify the critical key strength that can make the transition to successful professionalisation smoother – and the answer was high levels of "family capital", which enables FOBs to respond more positively to the continuation of their business into the next generation. Three key components of family capital were uncovered: heritage, kin-interaction and principled capital, each of which can be developed individually to create a multiplier effect that increases the overall family capital to support the business.

Heritage capital is the legacy inherited from previous generations. The implications for heritage are important to survival. It plays a guiding and stabilising role in allowing family-owned businesses to promote their uniqueness and competitive strengths to external stakeholders. The next generation of family members is able to tap into the wealth of knowledge and networks created by their forefathers, ensuring that corporate values are interwoven into the family heritage. Family members thus do not suffer any disconnect between business objectives and family legacy.



Preserving and enhancing quality kin-interaction within FOBs by focusing on the family member's rights and obligations is the second component that can enhance family capital. Though commonly confused with one another, rights and obligations possess distinct differences. Rights refer to the privileges that family members enjoy in making decisions regarding the family business. These privileges should not displace or override obligations that family members have towards their family and the business. Too many family-owned businesses disappear as a consequence of not paying attention to the quality of the bonds that hold the family together, and connect it to their enterprise. In such a context, detached or uncommitted family members exploit to exhaustion the assets they have received, until little is left for the following generation.

Finally, family moral infrastructure and governance policies are of instrumental importance in preparing future generations to run the family business. This is something that external employees will not be able to bring to the company, and has to be a practice that is passed on within the family. This authenticity is the essence of principled capital. Equipping the next generation with the tools of the trade is not a simple task. One step that older generations can take is to create a strong civic structure encouraging younger members to act in a manner that is consistent with the workplace while incorporating family values. This can be done by actively governing the way family members interact with the business, ensuring that its conduct is compliant with the law while being in line with the family vision for the business.



Putting together the sum of the parts

Combining the three integral variables allows FOBs to maintain long-term financial and social stability. They are able to attain sustained growth through identifying the unique resources and networks created by their forefathers (heritage), fully utilising and developing those resources (kin-interaction) and guiding their optimal use (principled capital). Lessons from those FOBs that have made the leap beyond the third generation prove that family capital can help them be better prepared for family feuds as well as utilise formal structures to create a succession plan. Feuds are most likely to occur during the attempt to professionalise. Our analysis has also identified that FOBs who survive beyond the third generation have higher levels of family capital when compared to those who do not survive as long. For this reason, it is important to have a sound mix of guiding principles, rights and obligations, and moral infrastructure.

FOBs are unique because their objectives are two-fold: sustaining the business and keeping the family together as a cohesive unit. For many years, FOBs have operated with the idea that a trade-off between the objectives becomes essential after the third generation. However, as we have argued in this article, these objectives can support each other if FOBs learn to manage the balance of their family capital and professionalisation of the business. Yet the trick is to be able to develop the family capital as a foundation for professionalisation. Developing family capital before professionalisation, or the lack of either one, will result in the demise of the FOB.

Developing family capital before professionalisation, or the lack of either one, will result in the demise of the FOB.

Andreas Raharso

is global director at Hay Group Global R&D Centre for Strategy Execution, in Singapore. He wrote this article together with his researchers, Shakifur Chowdhury and Witansa Angwidjaja

THE NEW Capitalism

By Ann Florini and Bindu Sharma

Asia and the future of business, government and society

Capitalism as we have known it is not fit for the 21st century. What is to take its place?

To have a conversation, the appropriate language is needed. The language is just starting to emerge in both Asia and the West for one of the most important conversations the world is now having—the discussion about the future of business and capitalism. Thailand's King Bhumibol refers to the sufficiency economy. Harvard's Michael Porter speaks of shared value. Ellen MacArthur's eponymous foundation supports the transition to the circular economy. John Elkington proposes breakthrough capitalism. Bhutan's call to measure progress by gross national happiness (GNH), rather than the narrow metric of gross domestic product (GDP), is now attracting attention around the globe.

The explosion of terms, concepts and practices takes us far beyond the familiar corporate social responsibility. All are efforts to grapple with the same issue: capitalism as we have known it is not fit for the 21st century. What is to take its place?

The old equation

The ideology of free-market capitalism assumes a simple but powerful equation: Profit maximisation plus government regulation equals maximum social value. If people in the business sector strive to make as much profit as they legally can, and government regulates business activity as needed to protect the public interest, everyone ends up in the best of all possible worlds—wealth grows, jobs abound, and consumers get the best possible goods and services at the lowest possible prices. This is the idealised essence of the Western capitalist model. Like all ideals, it never really existed, but it came close enough to generate the extraordinary wealth of the Western world. But every part of the equation is now breaking down.

Profit maximisation has degenerated into casino capitalism. Roger Martin's brilliant 2011 book *Fixing the Game* points out that the West went wrong when it adopted the belief that a corporation exists to maximise shareholder value. That misguided notion led firms far afield from their real value to society—the efficient design, production, and distribution of goods and services that people want to buy. The game of guiding "expectations" for quarterly earnings reports and trading stocks, options and complex derivatives, Martin shows, is the wrong game. He uses the metaphor of American football's Super Bowl, but the metaphor works as well (and more globally) for the World Cup—in the new casino capitalism, teams aim not to win the World Cup but to win a *bet* on the World Cup. And even firms that are not gambling in the casino (such as family or state-owned firms) still often see the siren call of profits as excusing them from taking any responsibility for social and

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environmental well-being beyond what government can make them do.

Government regulation is needed to set and enforce property rights (so that business can be transacted at all), enforce contracts, and make business–or someone–deal with the nastier side effects of business activities, such as pollution or exploitation. The thought leader behind the U.N.'s new Principles on Business and Human Rights, Harvard's John Ruggie, has long argued that free market capitalism is only socially bearable when it is "embedded" in a set of rules, norms, and social protections that buffer people from the disruptions of capitalism's drive for efficiency. As business has gone global, regulation and embeddedness need to operate at the same scale, but government is still national, with no prospective world government in sight. And within countries, many governments fail to regulate effectively in the public interest, due to lack of capacity, regulatory capture, the absence or breakdown of countervailing powers such as unions, and the effects of the past few decades' prevailing ideology that government is the problem and markets the solution.

And the "maximum social value" side of the equation is not what it used to be. Societies are no longer satisfied by businesses that provide desired goods and services in private markets at acceptable prices. Now, corporations must satisfy new standards for how they *conduct* their business, even when government fails to effectively regulate that conduct. As firms from Apple, Nike and Shell in the Western MNC world to Olympus, Sanlu and Satyam in Asia have found in recent years, business cannot so easily escape responsibility for the social and environmental side effects of their activities. In addition, society is increasingly turning to business models to find financially sustainable ways to provide public goods, from education to water to environmental protection.

The new equation

The single-minded pursuit of short-term profit maximisation now lies discredited with the advent and persistence of the Great Recession. Although this time it was a Western-based disaster, Asia has been an equal partner to the relentless pursuit of profit–the 1997 economic crisis served as a costly reminder of unbalanced and unstable growth via single-minded pursuit of profits without much thought to the wider economic, environmental, and social development process. Now, both Asia and the West are experimenting with new equations for capitalism.

In the West, some of the experiments date back decades, with codes of corporate conduct that attempted to achieve on a voluntary basis what governments were failing to require legally. Driven primarily by the demands and effective pressure tactics of civil society organisations, codes have appeared everywhere: the Sullivan Principles to set standards for fair labour practices by western multinationals in the apartheid era of South Africa; the numerous codes to improve labour and environmental practices throughout the global supply chains of MNCs; the Equator Principles to set social and environmental standards for banks to use in determining which projects they will fund; the U.N.'s Principles on Business and Human Rights that provide guidance for firms as to how they should go about respecting human rights and avoiding complicity in violations of those rights; and many, many more.

Although for the most part firms have been pushed into adopting such codes and practices, some have put themselves out in front. Unilever's Sustainable Living Plan, adopted in 2010, has publicly established very ambitious goals for transforming the company's operations, based on the view that the profits of the future will not come from the practices of the past. Not incidentally, the company no longer provides quarterly earnings guidance, freeing itself from the worst of the casino-capitalist mentality. City Development Limited (CDL) of Singapore proudly notes its inclusion in several of the world's top sustainability benchmarks: FTSE4 Good Index Series (since 2002), the Global 100 Most Sustainable Corporations in the World (every year since 2010) and the Dow Jones Sustainability Indexes (World & Asia Pacific – since 2011).

> The 1997 economic crisis served as a costly reminder of unbalanced and unstable growth via single-minded pursuit of profits without much thought to the wider economic, environmental, and social development process.

As the CDL example suggests, stock exchanges can be powerful mechanisms for holding business to higher standards of governance, operational accountability and disclosure, thus creating institutional structures for oversight that governments lack. In several Asian countries, stock exchanges are demanding such standards at the outset in their listing requirements by mandating disclosure on corporate governance, independent directors, and ESG reporting.

Collaborating for success

Individual businesses have found, however, that leadership is lonely and requires new kinds of partnerships. As they in the private sector try to grapple with taking on roles that traditionally had fallen to the public and people sectors, they find that they must work closely with those other sectors to figure out what to do and how to do it. Unilever has reached out to Oxfam to conduct public and critical assessments of such matters as Unilever's impacts on poverty in Indonesia and labour practices in Vietnam. Codes of conduct and other experiments in new business practices usually involve a plethora of stakeholders, from NGOs to community groups to local and national governments.

Such collaboration across the three sectors is essential. If we leave it to business to regulate and transform itself, market forces may drive even the best of intentions to socially sub-optimal outcomes. But we cannot rely solely on government, which often lacks the knowledge, institutional forms and capacity to respond quickly to complex challenges, even leaving aside the problems of corruption. Civil society organisations are the means by which voices are heard, but by itself the sector has too little power – it can only persuade or influence the other two sectors. Although the revolutions in communication technology and social media may be transforming civil society's capacity to influence and insert itself into the decision-making process, the sector is rarely properly organised to manage representation at the table. Only together can today's non-linear, dynamic, interactive and fast-paced challenges be met.

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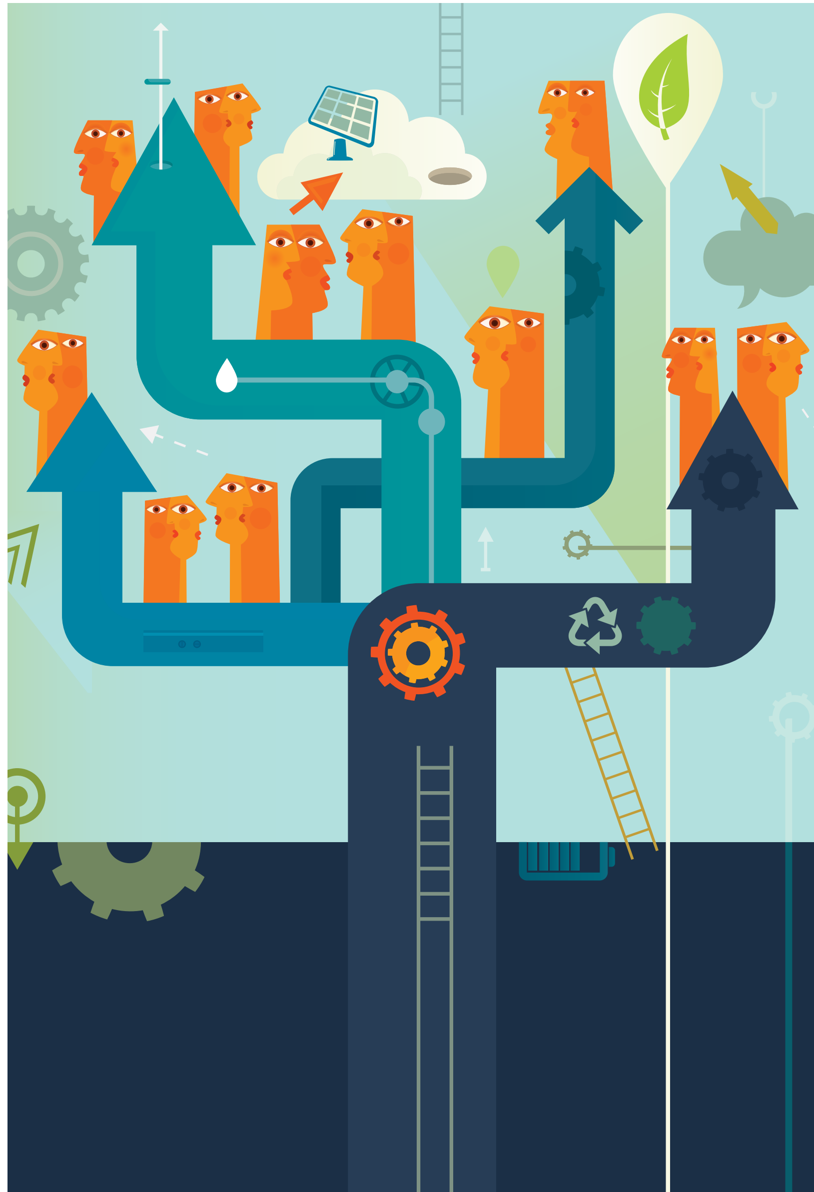
Ideally, these are mutually collaborative partnerships between partners of equal standing, but partners' respective development is mixed in Asia. Civil society organisations are growing, but in certain constrained ways. Elsewhere, SOEs and family-owned businesses operating with differing priorities can also dominate the markets. This is a critical issue. These companies enjoy the freedom to determine their priorities without worrying about the demands of shareholders seeking short-term profits, but it is also more difficult for civil society actors to influence firms' policy. How do you get the attention of a state-owned enterprise or a family-owned business?

Values for the future

The explosion of experiments in new business and governance practices offers hope for a world trying to find ways to provide for the material well-being of a global population heading toward nine billion, while facing major shortfalls of readily available water, land, and energy, and dealing with the destabilising impacts of technologies from social media to 3D printing. Yet without a truly coherent global debate over the roles of business vis-à-vis government and society, this hopeful moment could simply result in a cacophony of uncoordinated efforts that fail to add up to anything that can truly address the world's great challenges. Beyond the new training and new mindsets needed for tri-sector collaboration, we also need a global debate about what values should underlie a reinvigorated and responsible capitalism of the future.



This is a debate to which Asia has much to contribute. For example, in Thailand, the 1997 financial crisis prompted the King to put forth the "sufficiency economy philosophy" emphasising the optimisation of profits, balancing the social, environmental and other stakeholder interests as against maximising profits at the expense of all. The sufficiency economy construct sets the bar for new thinking in redefining the relationship across sectors, with the government's goals going beyond GDP growth to pursue the reduction of poverty and social inequality, developing indicators to capture wellbeing and happiness. The increasingly obvious costs of China's mad dash for economic growth led President Hu Jintao to call in 2005 for a "harmonious society" that would incorporate social and environmental ends into the developmental strategy. Almost immediately, new guiding principles and regulations began to issue from China's governing institutions. Events soon crystallised public attention, in the form of the 2008 Sichuan earthquake and the Sanlu milk scandal, both of which put product quality and the ethical/moral compass of business in the spotlight.

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What next?

Globalisation, the intense competition for limited global resources and the continued financial crisis are moving the discourse on the "new capitalism" front and centre in all sectors–civil society, governments and the business community itself. The West is where most of the conversation has been happening, focused largely around ever-expanding ideas of corporate social responsibility. But Asia may be where the question of "what next" finds its most compelling answers.

Asia is no stranger to close collaboration between business and government. Japan, Korea, and the "tiger" economies (Hong Kong, South Korea, Singapore and Taiwan) enjoyed tremendous growth through such partnering. The early 1990s saw newly industrialising economies (Indonesia, Malaysia and Thailand) emerge, each with its own variant of cross-sector partnerships. State-owned enterprises and sovereign wealth funds remain notable features of the region.

But those earlier partnerships generally excluded the crucial third partner–civil society. And they aimed at addressing mostly local problems without much connection to the wider world, except insofar as that wider world provided useful trade and financing systems. Now, Asian businesses, governments, and civil society organisations have both motive and opportunity to think and act bigger.

Already, Asia abounds in successful experiments in "social enterprises" that combine profit-seeking with social/environmental goals, such as Grameen Bank and BRAC in Bangladesh, the Self-Employed Women's Association (SEWA) in India, and the Population and Community Development Association in Thailand. Many of Asia's social enterprises started as non-profit ventures and are now operating in the business space. These initiatives transcend current parochial business practices and have perhaps

established the ethos of responsible social enterprises still to come. Today's emergent social enterprise may become tomorrow's leading corporation, especially as governments develop the legal and regulatory systems that enable and perhaps even favor such practices.

Now may be the time to combine the thinking behind tri-sector collaboration and social enterprise with a global goal-setting process that is happening under the aegis of the U.N. In 2000, the world's governments collectively agreed upon a set of Millennium Development Goals, concrete targets in such areas as poverty reduction, health, and education to be achieved around the world by 2015. As we approach that deadline, the poverty goal (which specifically aimed to halve, between 1990 and 2015, the proportion of people whose income is less than the international absolute poverty line of US$1.25 a day) has already been achieved. That stunning accomplishment represents the kind of achievement any business, government, or NGO could be proud to help to bring about. (Other MDG targets, particularly on such issues as maternal health and child mortality, will not be met despite some progress.)

Because 2015 is nearly upon us, an international debate is raging about what goals should come next. A leading candidate is the elimination of extreme poverty by 2030, a very challenging goal, especially as it must be coupled with the need to make industrial systems and land use practices sustainable in a world already severely threatened by climate change and ecosystem collapse. There is wide agreement that whatever the goals are, they should be accompanied by concrete and specific implementation plans. Those plans can and must involve not only governments and the plethora of NGOs active in development. They can and must involve business and the new capitalism. We must incorporate the private sector's genius at efficient resource use and innovation to have any hope of achieving such goals. That requires a new and better kind of capitalism.

Ann Florini
is professor of Public Policy, School of Social Sciences, Singapore Management University; academic director of the SMU Masters in Tri-Sector Collaboration, and non-resident senior fellow, Brookings Institution

Bindu Sharma
heads the Asia office of the International Centre for Missing and Exploited Children, a global NGO headquartered in the U.S.; author of Contextualising CSR in Asia, a Lien Centre for Social Innovation, Singapore Management University publication; and on the Advisory Council of the International Centre for Not-for-Profit Law in Washington D.C.

EXECUTIVE BRIEF

WHAT KEEPS talent managers AWAKE AT NIGHT?

As the talent acquisition landscape undergoes dramatic change and the lines between the disciplines of recruiting and marketing continue to blur, how can talent leaders stay ahead of their game?

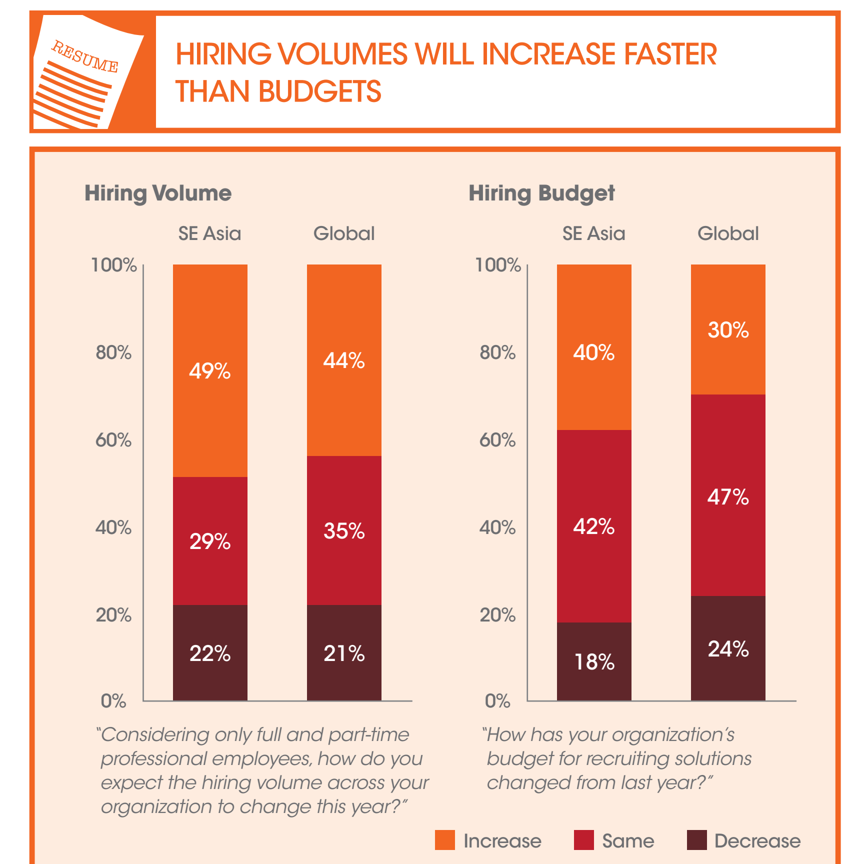
By Hari Krishnan

The talent agenda remains a top priority for business leaders in an increasingly competitive business environment—even for employers not facing an immediate talent crunch. The Asia Pacific region, one of the world's key growth engines, is no exception and leaders are under greater pressure to hire the best talent as a strategic competitive differentiator.

LinkedIn recently surveyed over 3,300 senior recruitment professionals worldwide, including 141 in Southeast Asia, to better understand the global talent landscape and the challenges in store for these senior executives. Specifically, the survey sought to gain insights based on answers to two key questions: "What keeps you up at night?" and "What are you doing to attract and retain the best talent?" The results of LinkedIn's Global Recruitment Trends 2013 survey point to a talent acquisition landscape currently undergoing dramatic change and offers five key insights that are set to shape the future of recruiting.

Like their peers in other disciplines, recruitment professionals are being challenged to achieve better results with fewer resources. Close to half of the executives surveyed in Southeast Asia expect hiring volumes in their companies to increase, while 60 percent expect budgets to stay the same or decrease. This challenge is by no means new or unique, but it does underscore the need to be even more focused on getting the basics of talent recruitment right: ensuring talent sourcing, pipelining and hiring are executed in the most efficient manner, without compromising quality.

In line with global trends, it should come as no surprise that sourcing and recruiting the right talent for Southeast Asia's talent leaders remains the top priority. However with so many companies—from established multi-nationals to enterprising start-ups—all going after the best talent, a key question is how can companies differentiate themselves if they are to win the battle for the best talent?



Source: LinkedIn 2013 Global Recruiting Trends

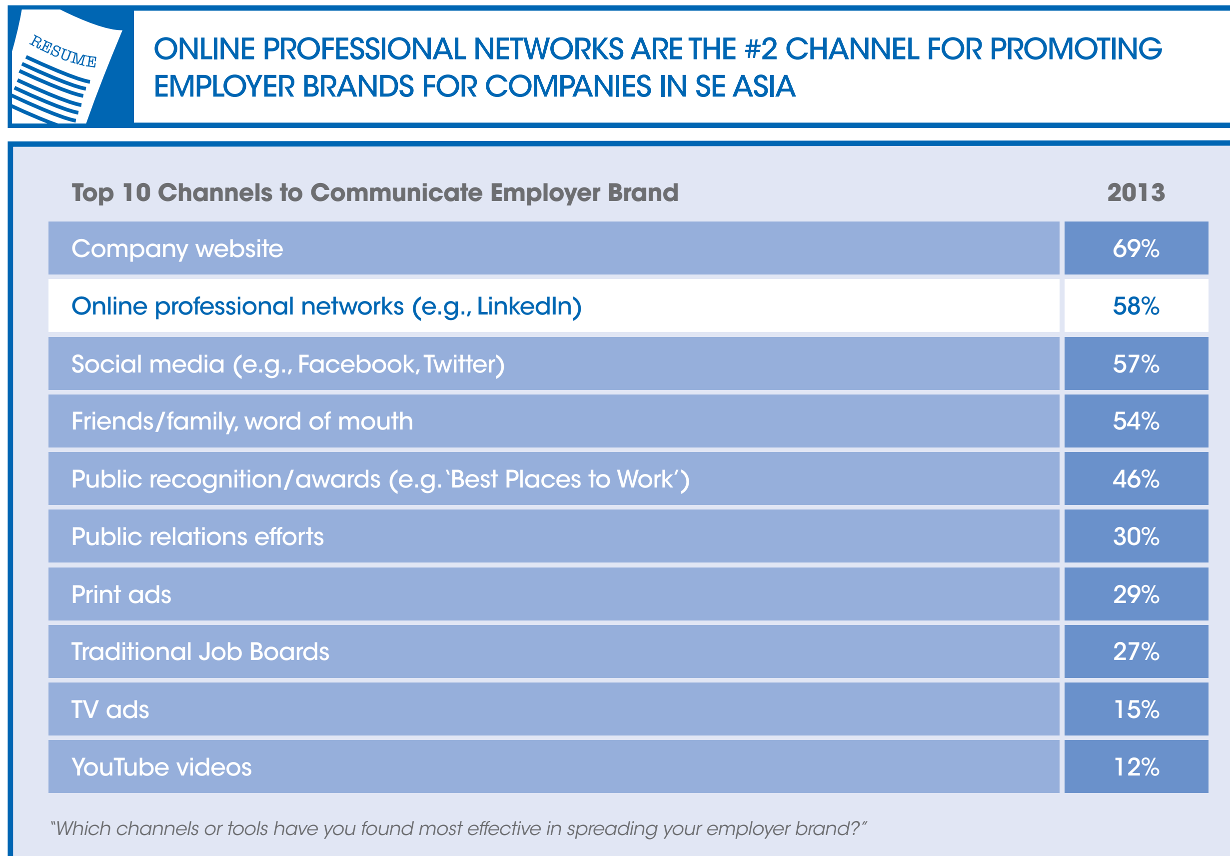
Leveraging social professional networks

The survey shows that social professional networks as a category, is currently the number two source of quality hires in Southeast Asia, right behind recruitment agencies. Moreover, the survey indicates that recruitment professionals expect to rely more and more on social professional networks to source and engage top talent in future.

To understand why the world's talent leaders believe social professional networks will play an expanded role in shaping the dynamics of recruiting in the long run, one need only look at one potent combination: social networks and "passive talent". Recruitment, the search for attracting and retaining the best people, is being transformed by the advent of online professional networks and the rising awareness of passive talent. Passive talent comprises professionals who are not actively looking for a new position, but are open to new opportunities. According to LinkedIn research, this group makes up approximately 80 percent of the fully-employed workforce. If anything, passive talent is happy where they are and continue to create value for their current employers. In Singapore, passive talent makes up about 73 percent of the workforce, which is not noticeably different compared to the rest of the world. Companies thus must find ways to engage this group, even though it may mean having to expend greater effort to "find" them, compared to simply focusing on talent currently "in the market".

> Companies must find ways to engage passive talent, instead of simply focusing on talent currently "in the market".

The Adidas Group has already started to change the game and is putting the concept of passive recruiting into practice. Through LinkedIn, its recruiters were able to find and reach out to passive candidates directly, and get them interested about opportunities within the Group. This approach helped reduced the company's average time-to-fill for vacant positions from 70 days in 2011 to 52 days in 2012.



ONLINE PROFESSIONAL NETWORKS ARE THE #2 CHANNEL FOR PROMOTING EMPLOYER BRANDS FOR COMPANIES IN SE ASIA

Top 10 Channels to Communicate Employer Brand	2013
Company website	69%
Online professional networks (e.g., LinkedIn)	58%
Social media (e.g., Facebook, Twitter)	57%
Friends/family, word of mouth	54%
Public recognition/awards (e.g. 'Best Places to Work')	46%
Public relations efforts	30%
Print ads	29%
Traditional Job Boards	27%
TV ads	15%
YouTube videos	12%

"Which channels or tools have you found most effective in spreading your employer brand?"

Source: LinkedIn 2013 Global Recruiting Trends

There is little doubt that passive talent recruitment will gather even more momentum going forward. In Southeast Asia, 62 percent of recruitment professionals surveyed by LinkedIn see it as one of their top hiring tactics, while a savvy minority (28 percent) says it went so far as to maintain a list of potential candidates who have not yet applied for any positions. Essentially, these recruitment professionals are taking a proactive approach to talent sourcing. Rather than responding reactively to fill positions on an ad hoc basis, they are taking a forward-looking approach by building strong talent pipelines that will ultimately enable them to better meet their company's future talent needs.

Yet, to be more successful at engaging passive talent, recruiters should seek to better understand the subtle differences between passive and active talent. On the one hand, passive talent seems more likely to want to make an impact, and work within a corporate culture that fits his/her personality. But on the other hand, one could argue, active talent generally wants rapid career advancements, and wants to be recognised for his or her contributions.

Employer branding, a competitive advantage and a threat

Businesses have long understood the returns from marketing their products and brands to customers to develop customer awareness and capture market share. Attracting talent should not be any different. And as the lines between the disciplines of recruiting and marketing continue to blur, more recruiting teams are starting to adopt marketing tactics that are more commonly used by their marketing colleagues.

> As the lines between the recruiting and marketing disciplines continue to blur, more recruiting teams are adopting tactics that are more commonly used in marketing.

Employer branding is at the core of the marketing tactics used in recruiting. For most companies, investing to boost their respective employer brands can be an effective way to attract and influence top tier talent. While prominent brand names would have an easier time attracting top candidates, recruiters at these companies may still sometimes struggle to recruit for certain specific functions, business units or geographies. The problem becomes more acute when an employer does not have the luxury of a strong brand, such as a start-up company or one operating in a Business-to-Business context. In some situations, a company's brand could change overnight due to mergers and acquisitions.

A particularly revealing insight from LinkedIn's survey is that employer branding can potentially place a company at a competitive disadvantage. While the majority (88 percent) of recruitment professionals surveyed by LinkedIn see employer branding as a competitive advantage that has a significant impact on their abilities to hire great talent, they are also aware of it as a competitive threat. Globally, recruiters rank the action of competitors investing in employer brands amongst their top three threats.

Notwithstanding its impact on convincing potential candidates to explore career opportunities in an organisation, an employer brand can improve bottom lines and productivity as well. LinkedIn's research points to the fact that a strong employer brand can halve a company's cost per hire, and that companies with stronger employer brands have a 28 percent lower turnover rate than companies with weaker employer brands. These reasons should be compelling enough to convince any company to start investing in boosting their employer brands if they have not already done so.

Leverage data insights

As the amount of data in business continues to explode, effectively leveraging insights from data will become a strong basis of competition. Some of the most effective and successful employers are already using rich data sets to obtain a more analytical and strategic approach to recruitment. Well ahead of the global average of 23 percent, 37 percent of respondents surveyed in Southeast Asia say they believe their organisations utilise data effectively to make hiring decisions. While this is encouraging, it also means that about two-thirds of companies are missing out on the many opportunities to make strategic, evidence-based talent management decisions.

To complete the picture, employers should also be surveying their new hires regularly to get a qualitative review of their employer brands, which will complement the data that can be mined from online recruitment efforts such as click-through-rates, candidate response times etc.

Investment

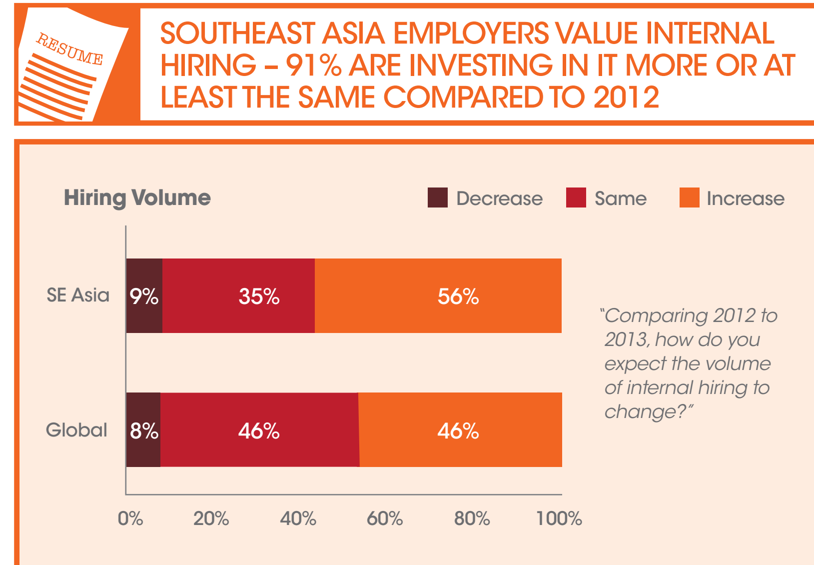
A business leader who runs a successful business knows that acquiring a new customer can be more costly compared to keeping existing, satisfied clients. This applies to talent acquisition as well. A good talent strategy is not only about hiring the best external candidates but also about keeping existing top talent from walking out the door to the closest competitor. LinkedIn's survey results support this view, with best-in-class employers saying

internal hiring and internal mobility are their priorities.

A structured internal hiring process and supportive culture helps companies keep their best people engaged and motivated—and it can work out to be one of the smartest things an employer can do, especially with hiring budgets stagnating. This also means that a company that is not investing sufficiently into providing internal career opportunities for its employees will become an easier target for the poaching of existing talent.

In Southeast Asia, nine out of 10 employers surveyed by LinkedIn say they are making at least the same level of investment for internal hiring, with 56 percent saying they expect internal hiring volumes to increase in 2014. These companies are clearly seeing the advantages of internal hiring. While retaining top talent was the number one advantage cited in the survey, the gains from employee productivity due to a reduced ramp-up time as well as the lower cost per hire were amongst the top reasons why companies continue to invest in internal hiring processes and employee engagement.

SOUTHEAST ASIA EMPLOYERS VALUE INTERNAL HIRING – 91% ARE INVESTING IN IT MORE OR AT LEAST THE SAME COMPARED TO 2012



Source: LinkedIn 2013 Global Recruiting Trends

Mobility

Few people would dispute the fact that smart mobile devices have forever changed the way people live and work. According to Deloitte's latest Technology, Media and Telecommunications study[i], the combined sales of tablets and smartphones have grown from over 350 million units in 2010 to around one billion in 2012. As the web is increasingly accessed via mobile devices, recruiting teams will need strategies that work both on the desktop and on smaller mobile screens. Just like the marketers, recruiters should also be reaching out to engage their target audiences on multiple devices.

It is therefore curious that many organisations are not investing sufficiently to meet candidate demand, especially those candidates who are "on-the-go". For candidates who want the flexibility of searching for jobs on mobile devices, there has thus far been limited investment on a global basis by companies and recruiters to introduce such mobile-friendly channels that would enable such candidates to discover them.

> A company not investing sufficiently into internal career opportunities will become an easier target for the poaching of its talent.

While some companies have already built mobile websites and apps to reach candidates on their phones, it is unclear how successful these efforts will be in reaching passive talent. By their very nature, passive talent is unlikely to be interested in downloading apps or visiting websites. If a company is intent on reaching out to a broader group, including passive talent, they should look to "fish" in a professional ecosystem where many are engaging with one other and sharing business content and insights.

The next frontier

Niccolo Machiavelli observed more than 500 years ago "the first method for estimating the intelligence of a ruler is to look at the men he has around him". This axiom continues to apply today, and given that people make the organisation, one of the keys to a company's success is having and retaining the best talent. Intelligence begets intelligence, and the only way to win this talent war is to employ smart tactics—reach out to passive candidates, build a compelling employer brand, leverage big data, prioritise talent retention and tap into possibilities of mobile recruitment as the next frontier.

Hari Krishnan
is LinkedIn's managing director for Asia Pacific and Japan

Reference
i Deloitte Touche Tohmatsu Ltd., 2013, "Technology, media and telecommunications predictions 2013".

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AN Oreo WITH CHINESE CHARACTERISTICS

By Srinivas K. Reddy

Shawn Warren reflects on Kraft's glocalisation transformation

In late 2005, Shawn Warren, head of biscuits, Asia Pacific for Kraft, was in desperate need of a quick turnaround strategy. Oreo, after nearly 10 years in the China market was facing the imminent disaster of being completely pulled from the shelves. Local retail channels, along with company headquarters near Chicago, had finally grown impatient of the iconic product's lacklustre sales.

When Warren described the turnaround in March 2012, he said, "The first step to solving a problem is to admit you have one. We are committed to have this brand and put resources behind it."

Framing the context

Oreo, first sold by Nabisco in Hoboken, New Jersey in 1912, had become a classic fixture of Americana. Over time, Nabisco built an international presence with Oreo and increased the size of that product's packaging as demand for it grew in both the United States and overseas markets.

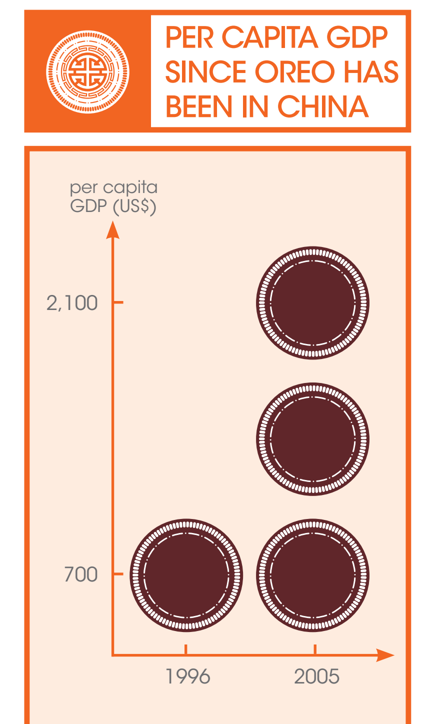
In 1996, Nabisco entered into the increasingly liberalised and rapidly-growing China market. Four years later, Phillip Morris, a U.S. based tobacco company, acquired Nabisco and merged it with several other food companies under the Kraft banner. The merged company had a diverse product portfolio of some of the most well-known brands in the world. At that time, Mary Chun, the brand manager at Oreo China, commented to Warren about the merger, "One big difference was that Kraft operated at a different pace than Nabisco. At that time, Kraft had a portfolio of products considered *back-of-the-shelf–grocery*. Nabisco had more of a fast-paced distribution model, with a product shelf life of around 12 months. Kraft products had a shelf life of more like two years. So once you changed to the Kraft pace to sell Nabisco products, it wouldn't work."

In terms of decision-making for Oreo, this was consolidated in the senior management team at company headquarters, which dictated central policy based on what worked well in established core markets. In 2004, Kraft had global revenues of US$32.2 billion, with Oreo sales accounting for some US$900 million. Impressive as these figures were, the company had experienced steadily declining profits since 2001–with the most severe drops coming from Latin America and Asia Pacific operations. A key manager at Kraft headquarters once commented, "I am not sure why the Oreo has not been a success in China. It is the most successful biscuit in the world. It has gone from a regional favourite to the number one biscuit in so many markets; surely the winning combination of taste and brand will work in China if we just give it some time."

The China market

In the nearly 10 years that Oreo had been in China, per capita GDP had risen from US$700 per person to US$2,100–a threefold increase. This rapid economic expansion was due largely to export driven growth.

PER CAPITA GDP SINCE OREO HAS BEEN IN CHINA



32%
lived in cities (1996)
50%
lived in cities (2005)
60%
living in cities (by 2020)

URBANISATION IN CHINA

Favourable improvements in import policy were also occurring. Market-oriented reforms hit a milestone in 2001 when China was admitted into the World Trade Organization. A strong growing economy and the rise of the Chinese consumer in the world's most populous country had become an enticing opportunity for foreign companies.

Several foreign companies had impressive successes early on. Hypermarkets, first introduced in 1995, were well suited to take advantage of upwardly mobile Chinese consumers. More and more of these stores were opening in cities across the country. Between 1999 and 2004, their sales increased by 147 percent. This growth was expected to continue as China became more urbanised. For instance, in 1996 only 32 percent of China's population lived in cities, but by 2005 this number had reached 50 percent of the country's 1.2 billion people. By 2020, urbanisation was projected to reach 60 percent. Prospects for hypermarkets, and by extension, the packaged food category looked bright.

The issues at hand

THE MERGER

In 2005, bakery goods were the number one packaged food in China. As a bakery good, biscuits had done well—having grown by 8.4 percent annually between 1999 and 2004, with sandwiched biscuits like Oreo growing at 7.5 percent. But as the market matured, this growth had slowed down.

Oreo had a successful initial launch in China and within three years, by 1999, had established a strong foothold. After Kraft acquired Nabisco, the merged company with its expanded product line had become the largest biscuit company in China, with a 10 percent market share in the category. Warren commented, "There was a fair amount of integration that happened pretty quickly, which created a fairly unwieldy brand portfolio." It soon became apparent that the expanded portfolio was a collection of distinct brands, with non-complementary sales efforts.

> There was a fair amount of integration that happened pretty quickly, which created a fairly unwieldy brand portfolio.

Warren worried that this larger portfolio was not being branded and distributed effectively. The company lacked the focus and sufficient spend on any one brand, and by attempting to concentrate on all brands they ended up concentrating on none.

After the merger, sales of Oreo had been flat–growing at just over four percent annually. Warren recalled, "When it was launched, we used the U.S. product, the U.S. formulation, and the U.S. advertising strategy, which was very much the global practice. But growth between 2000-2004 was stagnant. Four percent is not good enough in China; anything below 10 percent is not growing at all."

This was extremely frustrating for the local office, which felt they had little say in major decisions about Oreo. In particular, decisions about pricing and product innovation were completely centralised.

A UNIVERSAL PACKAGE

From 1996 to 2005, Oreo's primary sales channel in China continued to be the medium-size grocery stores and foreign-chained hypermarkets such as Tesco and Carrefour. The biscuits came in the standard packaging that was used in other geographies—which was based on the U.S. packaging that contained three partitioned rows of 12 Oreos. Chun discussed the package size with Warren, "The current production is manufacturer-driven as they prefer producing packaged rows of all the same length, since it gave better efficiency and output. But if we need to satisfy the customer, we might need to change."

Kraft would also run bonus pack promotions with extra Oreos in the standard package size. This had been a highly successful strategy in the U.S., where having additional Oreos in the package strengthened the consumers' perceived value.

COMPETING COOKIES

Across China, competition in the biscuit market was strong. Despite Kraft's overall number one position, the company was trailing behind the competition in regions outside the north. Oreo's sales began to erode as competing biscuit sales grew. Chun remarked, "When Oreo was first introduced in China, the types of biscuits in the Chinese market were limited. The majority of the market was in sweet or savoury plain crackers. At its launch, Oreo was considered a good innovation as it was in a sandwich cookie format. But as we got into the later years, we started to see all different forms of biscuits appearing on the market. Some of these products did quite well, like sandwich biscuits introduced by Taiwanese companies."

Taiwan-based Master Kong led the sandwich biscuit category with two brands that together held a national share of 32 percent of the market, well ahead of Oreo's 19 percent. Master Kong brands were less sweet than Oreo, and more to the taste of the average Chinese consumer's palate. It was also offered in smaller packaging than Oreo, and contained just three biscuits. However, since most packaging in China contained only two biscuits, Master Kong packages were perceived by consumers to be of good value.

SELLING AT A PREMIUM

Oreo was priced at a premium and noticeably more expensive than competing brands on a per biscuit basis. On a per package basis, the absolute price of buying Oreo was dramatically higher because of the large package size. Distributors believed that the higher price and larger package size was a key factor behind the poor sales. There were other concerns too.

DISTRIBUTION

Premium biscuits, like Oreo, generally contributed a smaller share of the final sale to the distribution partner. Kraft estimated that 60 percent of Oreo's final sale price went to the distributor, whereas value biscuits, such as Master Kong brands, gave 70 percent of the final sale price to the distributor.

In stores, Oreo was given shelf space in proportion to how well it sold. Unlike the U.S., where companies could pay for more favourable shelf space, most grocery stores and hypermarkets in China would arrange their shelves based on their own sales data. Although they would sell end-cap space or prominent one-time displays, the most desirable shelf space in the aisles was reserved for best sellers – which did not include Oreo.

In 2004, 50 percent of all biscuit sales came from super/hypermarkets. Although corner stores were the fastest growing sales channel for biscuits, nonetheless, internationally-chained hypermarkets were very important to Kraft's distribution strategy as they maintained an expansive network of locations. Whereas 65 percent of locally owned grocers had only one location, 60 percent of foreign chains had locations in at least five cities, with 30 percent present in more than 16 cities.

INVENTORY WOES

Kraft was not sitting idly as their biscuit sales tanked. In 2003, the company increased marketing and communications spend by 40 percent in China–but the consumers did not respond. By 2004, shipments for their entire biscuit line were down 12 percent. Moreover, higher than expected inventories were driving up storage costs, and much of the stock had to be thrown out.

In late 2005, while Warren was wondering how to salvage the Oreo in China, he went back to a market research study that had been completed earlier that year in July. The study tested a new Oreo product, LightSweet Oreo against the regular Oreo, and it revealed what the local team members already knew – that Chinese consumers preferred a less-sweet biscuit.

32%
Master Kong's share
19%
Oreo's share

SANDWICH BISCUIT CATEGORY

CUSTOMER WANTS

The study, however, could only estimate a preference for LightSweet at a 90 percent confidence interval. Policy at Kraft required a 95 percent confidence to launch a new product line, and several new product launches had recently already been cancelled. Convincing headquarters to go ahead with LightSweet Oreo would be difficult. Warren elaborated on the company's reluctance, "If you look back at it from 1912 to 1975, we did not have a single variant of the Oreo, just the black and white cookie. Even in 1975, when the Double Stuffed came out, the only change was the extra amount of crème. The next actual flavour took almost 100 years and came out in 2001, which was chocolate. The original Oreo is what got us here."

Regardless, something had to be done quickly if the Oreo was to stay in China. A debate ensued–should the company

focus on the core brands that had been underperforming, or spend a lot of time and money on launching new flavours and varieties? Warren recalled Chun's comment, "We need a mind-set shift and to place a foundation for future success. We have to decide what we want to achieve as the Oreo brand in China and how we can reset our strategies to get there."

Recognising the problem

The Oreo was too sweet for most Chinese consumers and the packaging too large to appeal to purchase occasions. The promotional strategy was no-good either. The Oreo was still a new product for many people in China, and they were not interested in buying a month's worth of Oreos, having never tried them. Yet, the large size of the Oreo package presented exactly this dilemma.

The problem, as Warren put it, "was that we were looking for American consumers in China". The Oreo in China simply focused too much on the global market, and not enough on the local market. It essentially had its name translated into the local language and dropped into China. Market research may have helped address these problems early on, but by no means would it have guaranteed the biscuit's success.

By 2005, it was apparent that there were so many challenges that needed to be addressed, that for a turnaround to work, a number of interrelated problems had to be solved at the same time. Addressing only a few of these would not yield the dramatic results that the company needed.

Many of the issues that Kraft experienced in China originated from central policy and decision-making that took place in the U.S. Senior managers, who had never even visited the countries where Kraft was operating, were the ones developing strategy for those places. This was, in fact, a Kraft-wide problem. Moreover, the team in China too was not very local, and comprised many expatriates and Westerners.

There was also a strong culture in place that felt the formulation of Oreo was untouchable.

Oreo in China needed a vision shift, but these factors made for a hard sell. Nonetheless, it was becoming evident that a change in Oreo in China's marketing and communication strategy, along with an adaptation of product innovations to the local market, was the need of the hour.

A transformative solution... nothing is sacred

In 2006, the CEO and Chairman of Kraft were replaced and a new management team was brought in. This, along with the poor sales in China, helped Warren convince central leadership to give him enough leeway to make changes. He said, "Giving empowerment to local managers made a big difference... If you looked at the board of management for Kraft China in 2006, there were a lot of expatriates and western folk around. If you look at the organisation today, almost 99 percent of our staff is Chinese, which makes sense. The brand was at risk of elimination, and in the face of that, we were humble enough to listen to the consumer, put resources around it, and change."

Kraft China refocused on six core brands in their biscuit line, including Oreo. The vision for Oreo was adjusted from the number one sandwich biscuit to the number one sweet snack in China. This paved the way for improved product innovation that catered to local tastes, which included an expansion of the Oreo brand into the wafer category and the launch of LightSweet Oreo.

Distribution was also expanded beyond Kraft's limited network in northern China. This would enable Oreo sales to grow alongside the booming hypermarkets. As Warren said, "[The Oreo] was too expensive... we didn't have the right distribution capacity and the manufacturing and cost structure were not very attractive."

Packaging decisions were shifted from the manufacturer's prerogative to local offices that understood customer wants and perceived value. In addition, customer trials were boosted by a subtle campaign around in-store samples.

Looking back

Oreo in China became a huge success. After the changes, the brand took off. Warren looked back, "When I first came to China in 2005, Oreo sales were US$20 million in China, and today (March 2012), seven years later, it's almost US$400 million–growing nearly 20 times in that time."

GROWTH OF OREO SALES

US$20m
in 2005

US$400m
in Mar 2012

He added, "We changed the business from the ground up, to move away from headquarters. The price point, for example, was being decided from Chicago. The company also made a significant change, and now key decisions are being made from managers who are closest to the company."

These experiences changed the way Kraft operated as a company into a truly Glo-Cal (global-local) enterprise.

Srinivas K. Reddy
is professor of Marketing at Singapore Management University's Lee Kong Chian School of Business where is he also the director of the Centre for Marketing Excellence

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Digital canaries
IN AN URBAN DATA MINE

Technology-based sensors and data analytics have created unprecedented levels of informedness for consumers, corporations, the public and government agencies. The information they generate provides a basis for smarter cities and more sustainable urban living.

By Robert J. Kauffman

Two centuries ago in Great Britain, coal miners took caged canaries down into a mineshaft, along with equipment, gas lamps, food and water. The canaries acted as environmental sensors for threats from poison gases. They reacted quickly to adverse conditions. And if a canary fell from its perch, this signalled it was time for the miners to get out.

Today, technology-based sensors, acting as "digital canaries", make us more informed than ever before. We learn about social sentiments from social media. We obtain online news via mobile devices. We get frequent micro-locational weather reports. And we receive updates on traffic and transit delays, stream flooding, and other problems. We also obtain news of air pollution through environmental sensing and crime downtown through public safety monitoring. Business managers, meanwhile, learn about and leverage data streams that cover logistics, supply chain management and product movement from store shelves to consumers, while government agencies and officials track political opinions of citizens and social programme effectiveness. At the 2013 Wimbledon Tennis Championships, the organisers even appointed a "Twitter Chief" to inform people who were queueing for stadium entry about when they would no longer be able to see the men's final.

There are sensors everywhere now. Through them and the informedness they create, it is possible to do better planning, risk management and public communication, and pre-empt problems-in-the-making.

Digital canaries

Having data to create relevant information supports an understanding of the rich tapestry of urban life in ways never before possible. Sensors in the city act as "digital canaries in an urban data mine", with so much information to be revealed and leveraged for smarter living. Urban data analytics tell us things we need to know so sustainability becomes possible—for consumers, corporations, the public and government agencies—in contemporary city life.

As large-scale data have become available, so have emerging analytics methods based on multidisciplinary knowledge: machine learning, text mining, Bayesian statistics, randomised closed-loop network experiments, social networks methods, and more. These are elements of a new *computational social science* coming together for an understanding of how urban activities can be understood. This will support the emergence of a new *e-social science.*

Data to information

Information is valuable. However, *data* captured in smart city analytics processes only have potential value. Their value will be unlocked though a process of *transformation*—the mapping of data facts to useful information for decisions and actions.

The *value of information* for data analytics applied in urban settings is the value of a decision made in the presence of the information minus the value of the same decision made without it—adjusted for the acquisition and analytics process costs. Fortunately, the costs of its acquisition have dropped dramatically of late.

> The *value of information* for data analytics applied in urban settings is the value of a decision made in the presence of the information minus the value of the same decision made without it—adjusted for the acquisition and analytics process costs.

Working with big data supports efforts to achieve smart city life. We can capture data in large *stocks*, based on their storage in data warehouses as transactions, sales records, inquiries, taxi pick-ups, inventory levels, water drain gauge levels, airline fares, and housing starts. We also can acquire data in near-to and real-time *flows:* social sentiments, financial market prices, and seller inventories in transparent Internet markets. Flow data are used for electronic road pricing for highway access, and online reservations at our favourite restaurants.

Contextual information is important too. Examples are stock prices and parking in different areas of the city. Individual data points only have meaning when we know their means, variances, maxima and minima, and the stability of the readings we obtain about them over time. We want to know what causes them to change, for example, announcements of changes in interest rates or big-draw sporting events.

This is true for collections of large time-series data sets as well. For example, the social sentiments that emerge in different issue areas involving quality of urban life-related issues–the availability of housing for young families, the effectiveness of healthcare outreach and services for senior citizens, and the reliability of public transit services. Are the social sentiments trending up or down? Influenced by recent governmental actions? Or stable?

Obtaining useful information requires knowledge of data in a context before it can be used to formulate strategies and actions to make desirable impacts. Information makes people and decision-makers informed. This can be about whether it makes sense for rail transit planners to experiment with differential prices during peak hours. Or whether the timing is right for a young couple to buy a home. It also includes something so simple as gauging if it makes sense for a commuter to carry an umbrella to work.

Informedness is key to the operation of smart future cities. It arises as: *consumer informedness, firm informedness, citizen or social informedness, and government informedness.* In a smart city, informedness has diverse facets–as an understanding of consumer choices, knowledge of regulatory impacts, awareness of service effectiveness, and assessment of how actions to promote change need to be implemented for impact. So it is critical to identify the kinds of data to acquire, to provide the greatest fidelity for the analysis of the problems in the bull's eye.

Strategic data analytics process

Researchers at the Living Analytics Research Centre (LARC) at Singapore Management University are studying settings in business, consumer and social insights research that involve the "digital traces" of urban living. Data in corporate, public and social domains can be tracked, mapped and understood as a basis for improving strategy and taking appropriate actions. For example, investigating urban rail transit and hospitality services, retail telecoms and digital entertainment, financial services and e-commerce, and public safety and election campaigns have all become commonplace. Some data occur as sentiments expressed in social media, others as transactions in ATM networks and bank branches, and still others as consumer purchases in shops, restaurants, and online.

Considering these settings–and the role of data, the costs to transform it into meaningful information, and the value it produces for organisational strategy and informed action–I see a common *strategic data analytics process.* It involves data, information, strategy, action and evaluation, and can be iteratively implemented, so the most value can be achieved by organisations that use this process (refer to Figure 1).

Dr. Jamshid Vayghan, chief technology officer for IBM's Global Business Services in Latin America, echoed this view in a speech at Singapore Management University in August

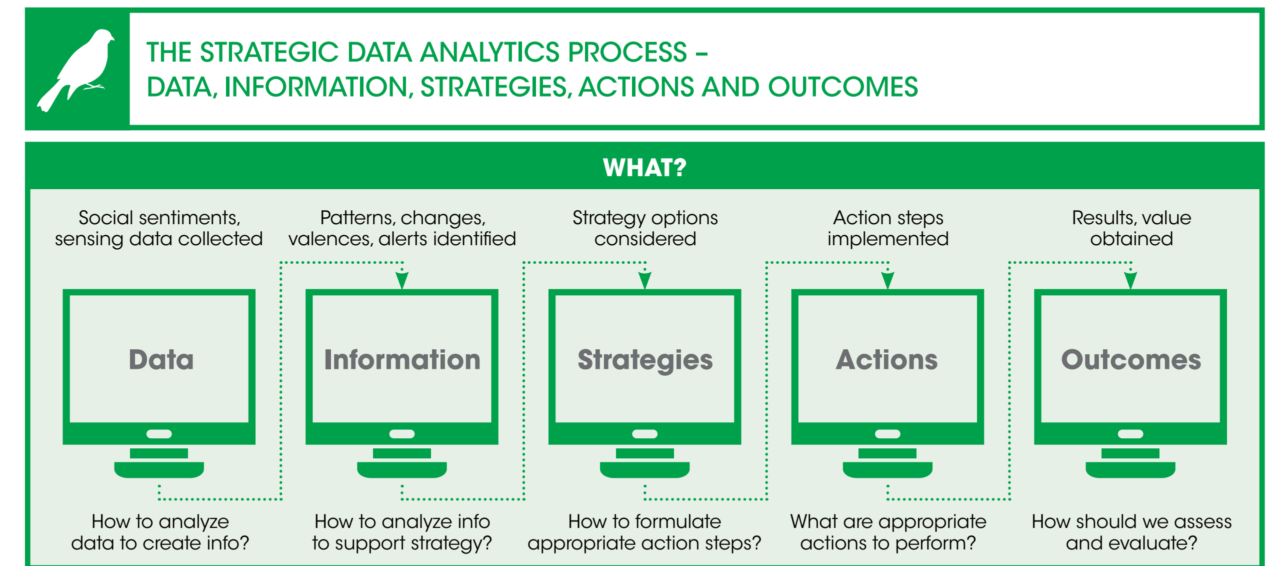

FIGURE 1

Source: Kauffman and Lim-Wavde (2013)

2012. Data analytics, he argued, should be managed as a business process–and one that reflects repeatable best practices. Appropriate requirements analysis, functionality and usability design, cost-effective and action-relevant data capture, and maintenance and updating of data and algorithms that constitute the data analytics must be undertaken. Building strong data analytics capabilities requires human, process and technology capital investments. And they all need to be focused on building best practices for the organisational processes that produce strategic business, consumer and social insights. This allows goals to be targeted so that current products and services can be refined, new ones can be designed, adjusted business and social processes can be introduced, and new programs can be launched. Better strategy formulation is the main driver of data analytics.

Formulating effective data analytics strategies requires an understanding of how value is created for a targeted set of stakeholders. Value takes on many guises in different urban contexts: as healthy profit margins achieved in business by local firms; as effective risk management protocols for contagious disease control in public health; as citizens' well-being with clean indoor and outdoor air; and as knowledge-based trust and understanding through the public's informedness regarding government policy actions. This goes beyond business value to citizen and social welfare.

Strategies to actions

Big data analytics support organisational programmes for a range of strategic objectives. An example is *observational micro-segmentation of consumers.* No longer is it necessary for organisations to employ high-priced consultants and generic market-wide segmentation templates to establish their market segments.

In LARC, my research group has analysed societal-scale data related to the density of household cable TV viewing in different segments. The analysis work showed enormous flexibility in identifying channel and programme viewership micro-segments based on 30-second data from two-way TV set-top boxes. We also explored the extent to which households efficiently use the spectrum of channels to which they subscribe, and learned that viewing time is a key determinant of the outcome (refer to Figures 2 and 3).

> The formulation of effective data analytics strategies requires an understanding of how value is created for the targeted set of stakeholders.

THE STRATEGIC DATA ANALYTICS PROCESS – DATA, INFORMATION, STRATEGIES, ACTIONS AND OUTCOMES

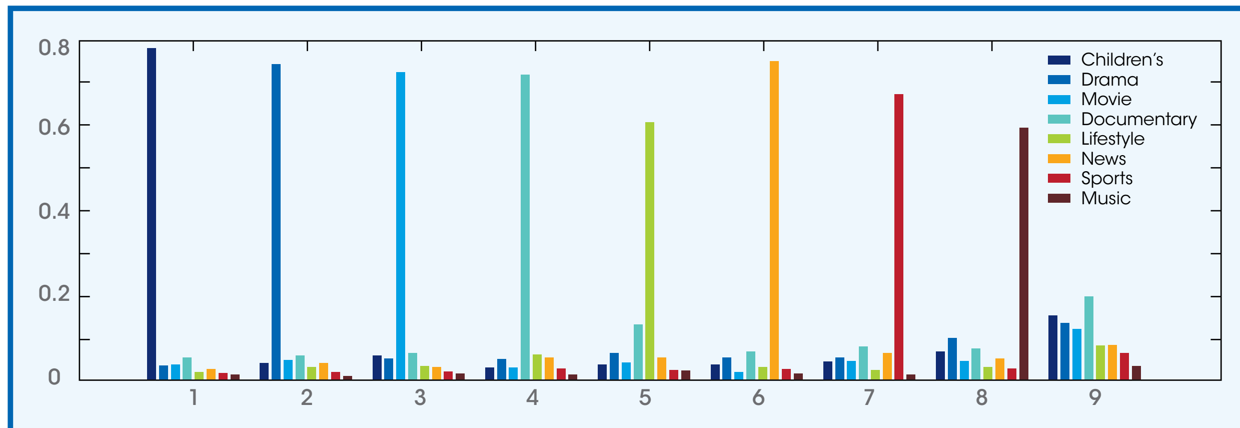

FIGURE 2 *Source: Living Analytics Research Centre, 2014*

SPLINE REGRESSION FOR CHANNEL VIEWING EFFICIENCY

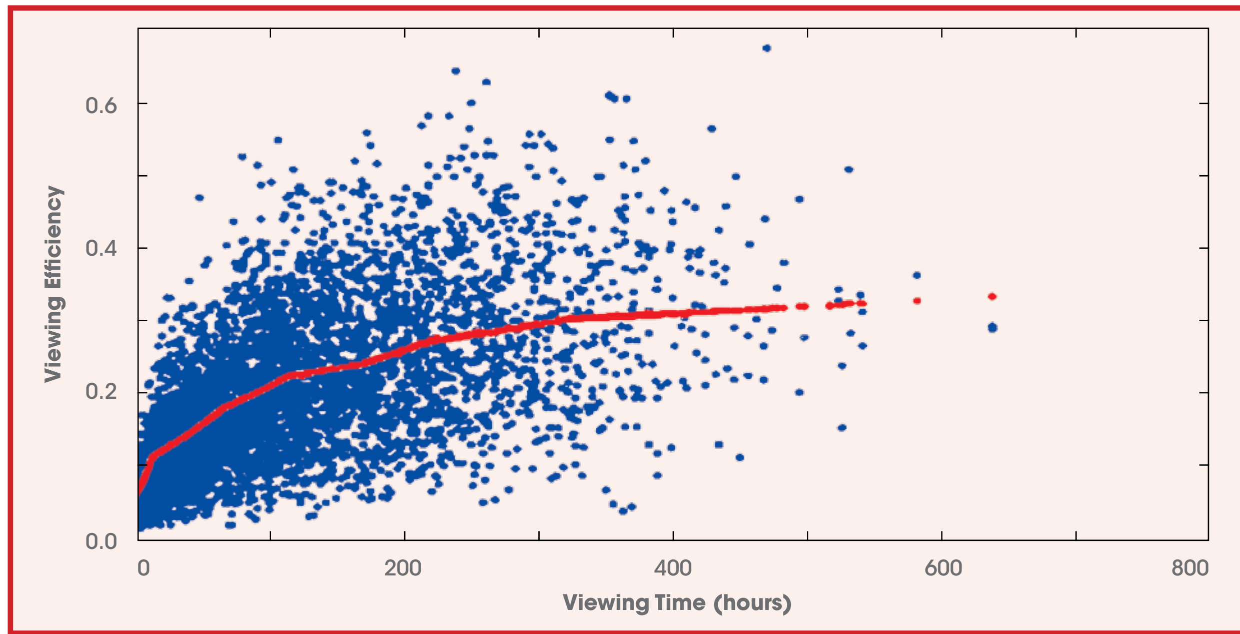

FIGURE 3 *Source: Living Analytics Research Centre, 2014*

Public information and communication. Another context for the application of urban data analytics is *strategic public information and communication enhancement* in social media. Analytics help public organisation and government agency communications to be effectively constructed, targeted and timed to have beneficial effects. In joint research that I have been conducting with computational and behavioural science research scientists at Singapore's Agency for Science, Technology and Research (A*STAR), we are studying the tie-in between tweet volumes, and positive and negative social sentiments from Twitter users related to the city's MRT (Mass Rapid Transit), and other current social issues (refer to Figures 4, 5 and 6).

TWEETS FOR "MRT" JANUARY 1 TO FEBRUARY 7, 2013

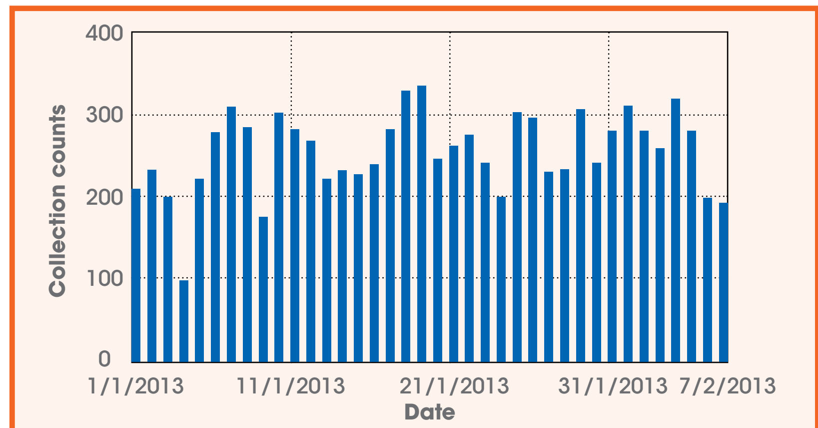

FIGURE 4 *Source: Wang, Kauffman, Goh, Yang and Chin (2014)*

POSITIVE AND NEGATIVE TWEET DENSITIES

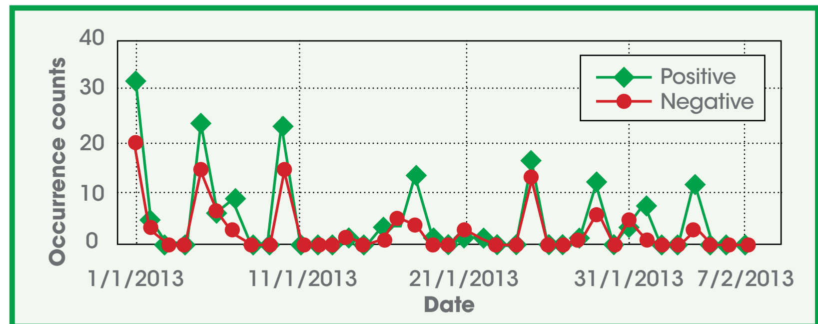

FIGURE 5 *Source: Wang, Kauffman, Goh, Yang and Chin (2014)*

POSITIVE AND NEGATIVE TWEET TRENDS

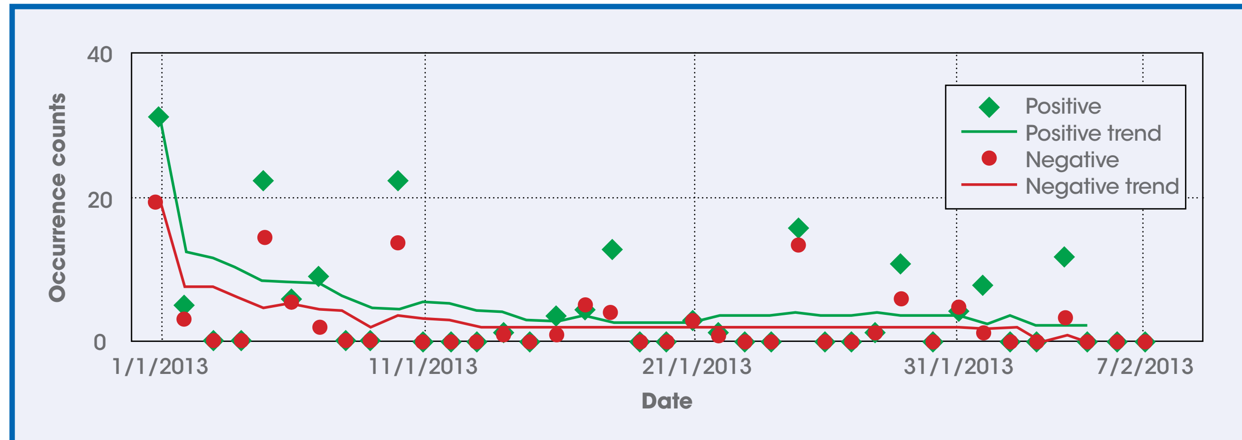

FIGURE 6 *Source: Wang, Kauffman, Goh, Yang and Chin (2014)*

We have attempted to connect the social sentiments to news in Singapore's *The Straits Times*, as well as social media news and announcements that act as stimuli for social reactions. We use various approaches to identify the evolving density of social expression, while controlling for prevailing baseline levels of tweet activities, and recognising the sentiment valence patterns (positive, neutral, negative), and the sub-negative categories of anger, anxiety and disappointment.

Geolocation and contextual awareness. Another application area for city analytics is the use of mobile phone tracking, GPS, and location-based marketing, to maximise the benefits consumers experience while they shop. The goal is to create *contextual awareness* for sales and service that goes beyond what a consumer knows herself.

In the past, many different kinds of stores–department stores and even bookstores–were "information deserts" for the consumer. Like water in the desert, little information was available to a customer in most stores. If you happened to have a mobile phone, you could obtain more product information than most store employees typically knew, and make well-informed price comparisons and purchases. New in-store and in-mall applications have emerged, making it possible for consumers to receive micro-location-based recommendations, coupons, discounts, and promotions.

Key sensors of consumer behaviour in the city are the many credit and debit cards that we carry in our purses and wallets. Card products from financial services firms are ubiquitous and soon our mobile phones will support card-free, contactless mobile payments. They all have the capability to track what we buy and where we buy it. Our daily transactions will become the digital traces of our lives as consumers.

The cards offer "15% off at ESPRIT", for example, co-branding incentives with airlines, malls and merchants, and micro-segment focused loyalty vehicles. This might be successful and independent women, as is the case with DBS Bank's recent "DBS Women's Mastercard". Another is Standard Chartered Bank's card use-focused mobile recommendation application, "Breeze", for location-based promotions, categories and merchant recommendations.

All these provide searchstream and consumer purchase data, with time, merchant and location stamps, and spend amounts. These create the basis for new and valuable insights on *consumer spatial transaction trajectory* over time for the firms that effectively data-mine the relevant digital traces. This will yield business value that the merchant and consumer can share: higher firm profitability via greater consumer willingness-to-pay levels. Value-sharing in all kinds of social settings is desirable.

Data analytics: limits to value?

Tropical rainforests showcase the complexity and interrelatedness of ecosystem life, with many species competing for the available resources. Cities are like that too. The challenge of making life in cities comfortable for people is a matter of managing the complexities and the interdependencies among the inhabitants.

Integrated data analytics that bring together the point-of-service or the point-of-sale with an organisation's data warehouse and operational systems can create enormous value for consumers, business partners, and citizens and public services providers. They can build new levels of informedness to support customer and user-focused product and service delivery. This is true for the operation of taxi fleets, city buses, rail transit, tourist attractions, and other urban services. Hospital emergency rooms, and water and electrical utility services are all subject to high demand at different times too.

Data analytics, no matter their level of sophistication, will be based on economic models of human behaviour in the urban environment. Nobel Prize-winning economist, Herbert Simon, has reminded us: "Human beings, viewed as behaving systems, are quite simple. The apparent complexity of our behaviour over time is largely a reflection of the complexity of the environment in which we find ourselves."[i]

Indeed, cities are the ultimate in complex human systems. It will be challenging for data scientists, business analysts and policy-makers to address the problems that arise due to the human complexities in city life. The decisions that city dwellers make–where they shop for food, whether they own a car, how much energy they use, when they commute to work, to what entertainment services they consume–can be modelled (if imperfectly) with data analytics that support predictions.

Difficulties will arise, of course: not all consumers make rational choices–even with "perfect" information about products and services. What's more likely? That decisions based on bounded rationality still will abound. And although such decisions may be "good enough" in some sense–for the individual perhaps, they still may not truly be good in the social sense. In many settings, "one person's music is another person's noise".

Thus, one can expect that business and social systems built on data analytics still will have "hits and misses" in their predictions about consumers, firms, citizens, government agencies, and societal processes. But the smart money should be on their having impacts that involve greater pleasure for most, with a modicum of pain for some.

So it makes sense to raise a caution flag... at least to half-mast height. What are the potential limits to value for data analytics in support of smarter city life? Can the "digital canaries" be our sentinels and saviours in different issue and policy areas? Will they help us to organise systems that make sustainable urban living more achievable?

Due to the burgeoning populations, limited land and increasing industrialisation of Asian cities, we must assess the issue areas in which the new sensor mechanisms will provide the greatest societal return on investment. Will they become strategic necessities, but still not sufficient to deliver desired levels of social welfare in different settings? In what settings will they offer more complete solutions: mass transit, healthcare and housing? Business or social services?

Herbert Simon offered some hints in a newspaper interview in 2000, "I don't care how big and fast computers are, they're not as big and fast as the world."[ii] Cities, especially Asian cities are ever bigger, ever faster-paced, and ever more complex. Yet other sage advice from the British statistician, George Box, suggested that "some models are useful" for many problems. He admonished us: we must "[r]emember that all models are wrong; the practical question is how wrong do they have to be to not be useful?" [iii] Still, data analytics for business, consumer and social insights have a bright future. They have the potential to improve urban social welfare through the greater informedness they create, and smarter cities will be better places to live in as a result.

"Human beings, viewed as behaving systems, are quite simple. The apparent complexity of our behaviour over time is largely a reflection of the complexity of the environment in which we find ourselves."
– Herbert Simon, Nobel Prize-winning economist.

Robert J. Kauffman
is associate dean (Research, School of IS), Deputy Director (Living Analytics Research Centre), and Professor of IS at Singapore Management University. He was the Lee Kuan Yew Faculty Fellow for Research Excellence in 2012-2013

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Sourcing Hub

By Anupam Agrawal, Luk N. Van Wassenhove and Arnoud De Meyer

Managing the suppliers of your suppliers may be a lot of work, but there is plenty of value in unlocking the supply chain

Active management of upstream sourcing is often said to add great value to a firm's supply chain. When a firm brings its suppliers and suppliers' suppliers together, value is created by pooling knowledge: information about demand, process improvements, raw material sourcing, and design complexity reduction is exchanged.

In most firms, there is a tendency to focus only on the immediate suppliers, as reducing the number of suppliers with whom they conduct business would result in less coordination with fewer companies, and hence reduce costs and improve profitability. Moreover, an increased focus on core business activities and the outsourcing of non-core activities has also resulted in firms slowly distancing themselves from some of the value in their supply network. However that may not be the best approach as TDV[i], a South Korean commercial vehicle manufacturer discovered.

Known in the industry as an automotive original equipment manufacturer (OEM), TDV manufactures products or components that are purchased by another company and retailed under that purchasing company's brand name. Because of the nature of its business, TDV has to coordinate with a large number of direct suppliers for items such as spark plugs, tyres, chassis, and hundreds of other parts that make up a motor vehicle. These direct suppliers in turn deal with their own raw material suppliers, giving rise to a fairly complex upstream supply network.

> When a firm brings its suppliers and suppliers' suppliers together, value is created by pooling knowledge.

In a four-year empirical investigation into the raw material supply chain practices of TDV conducted by Arnoud De Meyer of Singapore Management University, Luk Van Wassenhove of INSEAD, and Anupam Agrawal of the University of Illinois[ii], it was found that TDV had developed relationships with its suppliers and suppliers' suppliers, and was actively managing its raw material supply chain.

But is such management of the raw material supply chain necessarily beneficial for firms? And if there are two options available to a firm for upstream sourcing–either to supply raw material directly to their suppliers, or else to build a systematic collaborative process that brought the direct suppliers and the raw material suppliers together–which one would be most beneficial for all, the OEM, the component suppliers and the raw material supplier?

Benefits of direct raw material procurement

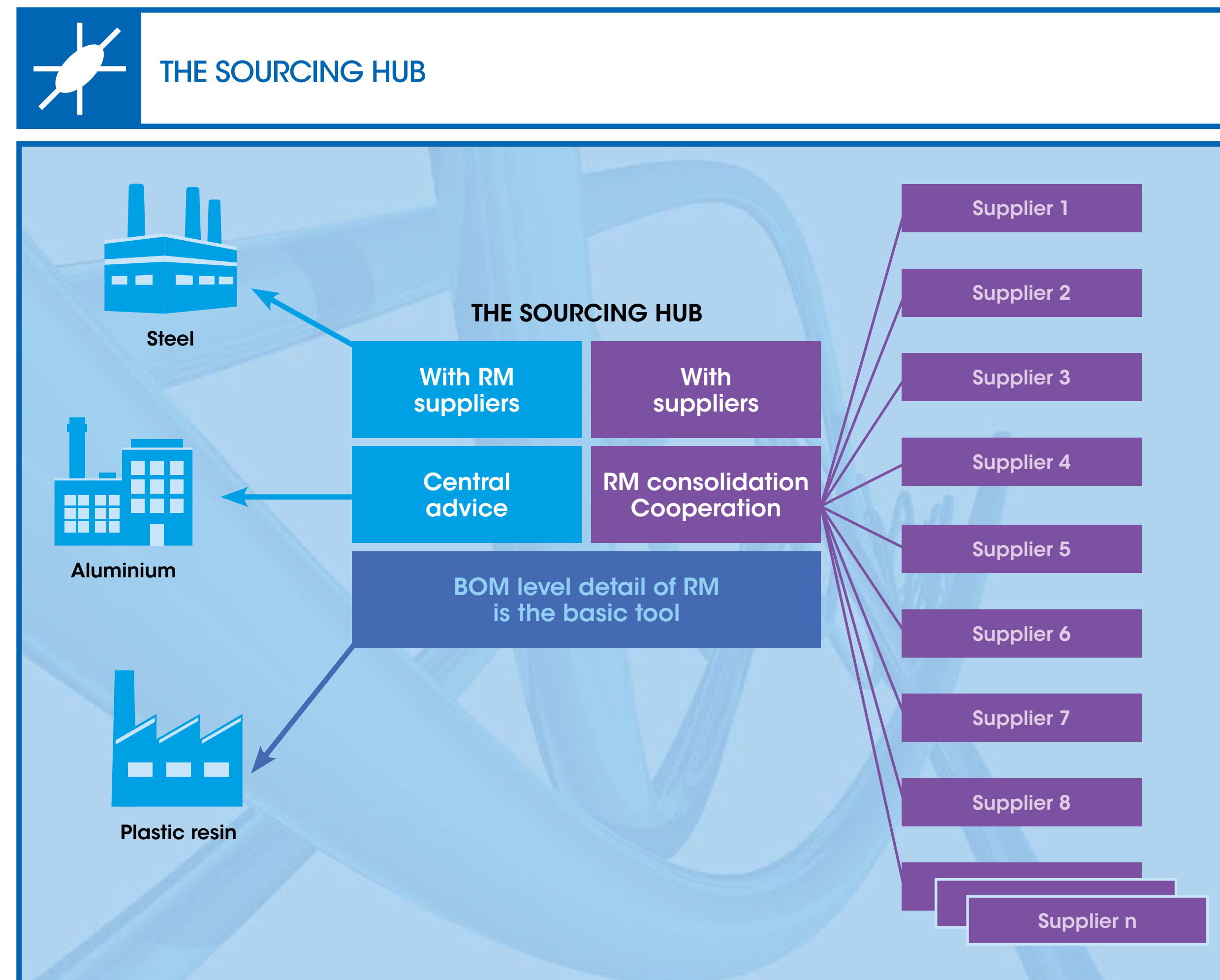
TDV has 23 suppliers supplying components for which steel is the major raw material. Instead of letting these 23 suppliers source for steel individually through the typical traditional decentralised raw material procurement and sourcing set-up, TDV purchased steel as a single buyer from the steel mill and supplies the metal to all 23. It also managed the logistics, physical supply, inventories of

raw materials, and disposal of scrap/offcuts of steel generated in the manufacturing process at these component suppliers.

TDV's contracts with its component suppliers stipulate that suppliers do not make any profit from raw materials, even if they buy the materials themselves and do not use the steel provided by TDV. Therefore, there is no financial incentive for component suppliers to manage raw material transactions via the addition of a profit margin; and given the additional benefit of not having their capital locked up in raw material procurement, it makes more sense for them to let TDV deal with such issues.

On the other hand, there is a seven percent difference between the supply prices of steel to OEMs and to other buyers. Interestingly, it was expected that the difference would be due to the standard volume purchasing benefit, where the OEM buys more and gets a lower price – however, this was not the case. The authors compared the price of steel provided to TDV, and another firm Hyundai, which produced cars in much higher volumes; and found that there was in reality very little difference in the price both firms paid for steel. It appeared that lower volumes did not matter—what appeared to be important was the fact that TDV was an OEM. When asked to explain the seven percent price difference, steel supplier executives emphasised the importance of long-term relationships and managing a stable production schedule over a price premium. One executive said, "Costs are not dependent on individual customer volumes after a base level. As long as firms procure standard products from us, our costs are really the same for TDV as for Hyundai... Costs are reduced by having a detailed plan and levelled production—that only comes from our OEM customers, because their plans do not vary too much for the next few months."

Moreover, by having a relationship with the OEM, or rather the direct customer's customer, the steel company is able to reduce many of the complications that routinely occur due to derived demand and its effect on the supply chain. That is, for the raw material supplier, steel in this case, having greater visibility of demand further down the supply chain reduces the opportunity for bullwhip demand problems.



The Sourcing Hub

In the initial years TDV managed its supply chain set-up through the direct raw material procurement system mentioned above—which helped the firm run its supply chain at lower costs, but it was very much a transactional relationship. However, over time, the firm developed a far more collaborative process, focused on developing relationships with its suppliers and raw material supplier. TDV now manages raw material prices, logistics, and other related transactions via a Web-based system in a department the authors refer to as the "sourcing hub". Physically, the sourcing hub is deployed as a separate department within TDV, and focuses on raw material sourcing and management. This helps in developing upstream relationships with both raw material suppliers and direct component suppliers. It also enables building cooperation between suppliers by increasing the understanding of raw materials sourcing, and further appreciating the complexity of the entire supply chain. This Web-based information is used by component suppliers as well as raw material suppliers, and is continually updated.

On an annual basis, TDV and its suppliers come together and develop the annual production plan. From this meeting, a detailed raw material plan is produced, from which quarterly and monthly plans are drawn on a rolling basis.

On a day-to-day operating level, plenty of information is shared between the firm, the suppliers, and the suppliers' suppliers. TDV manages all the information on the sourcing hub, which has the kinds of information necessary to help keep its suppliers up to speed about the production schedule: a production plan for the coming months, new models, changes in drawings, quantity of components required, and the quantity and grades of raw materials required. This information is used by component suppliers as well as raw material suppliers, and is continually updated. Moreover, as a result of managing all this information, the sourcing hub has details of raw materials required for each component as well as details of current pricing between TDV and its raw materials suppliers. Information at the bill of material (BOM) level includes complete information about the raw materials, components, and assemblies, as well as their respective quantities to manufacture an end product. This enables the company to have a clear picture of what raw materials are needed, the quantity and grade of raw materials required, as well as changes to the production schedule.

There are, of course, costs involved in setting up and running a system such as the sourcing hub: both start-up and on-going. Start-up costs relate to the detailing of raw material at the component level and establishing a material database so that the raw material supply is streamlined. To do so, the OEM has to collate accurate raw material information for each component. Most OEMs do not have such information since it takes time and money to build the necessary database—but once in place, the database is an invaluable source of raw material-related knowledge. On-going costs consist of managing the sourcing hub—linking supply with the payment cycle to the raw material and component suppliers, auditing the inventory etc. At TDV, the sourcing hub requires only two full-time employees and part-time support from one person in the finance department for a single raw material, for a single country.

Managing raw material sourcing is more beneficial for firms that have higher raw material content in their costs, as well as a large number of suppliers.

When does the Sourcing Hub work?

Using these empirical observations of TDV as assumptions for modelling a setup with a single buyer (in this case TDV), many component suppliers, and a single raw material supplier—the authors' explored two options: first, the buyer procures the raw material and supplies it to the component suppliers; and second, the buyer creates a sourcing hub.

It was found that managing raw material sourcing through the latter option of a sourcing hub setup is more beneficial for firms that have higher raw material content in their costs, as well as a large number of component suppliers – just like TDV does.

Moreover, as raw materials become more and more important in sourcing, building cooperative relationships with component suppliers and the raw material supplier via a sourcing hub also becomes increasingly beneficial for all the agents. Furthermore, the agents would benefit more from a sourcing hub as information asymmetry increases in the supply chain.

The authors' empirical research suggests that firms can achieve between three to six percent savings in their cost of goods by deploying initiatives such as the sourcing hub. This can be a source of great competitive advantage, considering that raw material costs amount to over 50 percent of the cost of goods sold for automotive OEMs, and the margins on the auto products are very low—the industry-level net profit estimate for auto industry is 3.5 percent (Damodaran 2013[iii]). While the automobile industry is an obvious potential beneficiary, other industries such as footwear, furniture, aerospace

and appliances could also extract value by lending themselves to the sourcing models described earlier. On the other hand, sourcing hubs may not be very useful for industries such as electronics, information technology, chemicals, or entertainment.

Overall, it is those scenarios where raw material supplies are monopolistic (or oligopolistic) and relatively stable, and where buyers have a larger dependency on raw materials in their cost of goods sold, that the deployment of a sourcing hub can help firms create value from upstream sourcing and recapture some of the value that has been lost in the race to become a lean manufacturer. By building a relationship with raw materials suppliers, the OEM encourages sharing of demand, production, and design information. This leads to improved sourcing processes thereby lowering costs and boosting profitability.

> Firms can achieve between three to six percent savings in their cost of goods by deploying initiatives such as the sourcing hub.

So why then are these models not more widely practiced? One answer could be that when an OEM procures raw materials directly for its suppliers, such an arrangement benefits the component suppliers. However the OEM will only benefit if it keeps the transaction costs of procuring the raw material supplies lower than the potential benefit arising from such a direct purchase. Otherwise, the OEM loses. Additionally, when there are many possible raw material suppliers or the choice of suppliers is subject to significant change over time, the return to the OEM of developing the infrastructure and relationships required to deploy a sourcing hub might not be sufficient to justify the investment. But perhaps most of all, an OEM needs to invest time and money to create a material database at the component level. This entails revisiting the bill of material for all components–a gruelling task for any organisation.

"If a new material grade has to be established for a new component", TDV sourcing engineers told the authors, "the process is longer, since TDV and the steel supplier need to agree on the new requirement and its price, as well as supplies. Additional IT work is also involved. Since this additional work is cumbersome, there is therefore an inherent pushback to any frivolous increase in the number of basic raw material grades being used."

However, revisiting the bill of material is the only way to find out answers to questions such as: (a) which current products of an OEM require a particular raw material? (b) what quantities of this raw material are needed at the firm level? (c) what is the grade of the most important raw materials needed at the firm level? While this is an exhaustive and time-consuming exercise, it is one that better enables management to holistically plan the needs of the sourcing hub and understand potential opportunities as well as vulnerabilities.

Moreover, while other firms may not follow the approach taken by TDV saying that this is not their core competency or core process–which is to build/assemble products – the reality is that such a sourcing model would enable the firm to insulate its core competency by extending beyond the immediate suppliers and ensuring that there are no disruptions to their core process.

How do managers go about this?

To begin with, managers need to focus on the key raw materials only. It would not be wise to manage the above process for *all* raw materials. Instead, they should perform some kind of a 20/80 analysis, and decide where it would be the most cost-efficient to do so.

The OEM firms should also analyse its bill of materials in detail, to see who are the main first-line suppliers. These are the ones that then need to be convinced about the value that is added by being supplied to by the sourcing hub. The OEM managers would need to get some alignment from these first-line suppliers on the concept.

They would need to engage in a negotiation with the supplier of the raw materials, in order to show them the non-financial benefits of stability in demand. It is only at this stage that the process will culminate in creating a sourcing hub.

In the case of TDV, its management of relationships with direct suppliers and upstream raw materials suppliers resulted in a far more efficient supply chain. Bringing their suppliers together at the sourcing hub, and the resulting cooperation between them, was clearly beneficial for not only TDV, but also its suppliers and the raw material suppliers.

Anupam Agrawal
is assistant professor at the College of Business, University of Illinois at Urbana–Champaign

Luk N. Van Wassenhove
is professor of Technology and Operations Management and the Henry Ford Chaired Professor of Manufacturing at INSEAD, France

Arnoud De Meyer
is president of Singapore Management University

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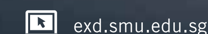 exd.smu.edu.sg
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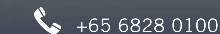 +65 6828 0100

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THE CUSTOMER INSIGHT JOURNEY OF Amazing Grace

How do you put consumer-centric marketing into action? Make it personal!

By Pradeep Pant

Mondelēz International is one of the world's largest snack manufacturers and distributors and makes some of the world's favourite brands such as Cadbury Dairy Milk chocolates, Oreo biscuits and Halls candies. Its current consumer-centric approach to the market originated in 2009 in the Philippines. As I recall, those were tough times; family budgets were stretched thin. Our products weren't even present in most *sari-sari* shops–the small neighbourhood convenience stores that met ordinary people's everyday shopping needs. It seemed hardly ideal for my company, with its portfolio of leading international brands, to capture local hearts and pesos. We had to do something.

To address this, we developed the Amazing Consumer Journey Programme, which was designed to enable the company to access the innermost thoughts and behaviours of its consumers, and get to know them better. As it turned out, that journey unlocked the power of our brands, and our employees. The Programme took our staff out of the office and into the shoes of ordinary people to see how they think, and how they feel. Through that initiative we learned all about our customer's wants, needs and desires. We discovered what they valued, how they lived their lives and thought about the future. A pattern began to emerge, from which we generated our model archetypical customer. We named her "Grace".

The teams then came up with a profile for their target customer: a woman, someone in their mid-30s, with three children. Her name was Grace.

By getting to know her… to relate to her… we embarked on a consumer-centric journey that would unlock the power of our brands, and the creativity and passion of our employees.

PROGRAMME'S 1ST SEASON

4 months

48 employee volunteers

6 cross-functional teams

RESULTING IN

659 insights

22 new product development ideas

Grace is a fictitious representation that personifies everything our staff learned through the Programme. This gave us a lot of insight. Not only did we better understand customer behaviour in the context of where our products were sold, but where our products should be sold, like a *sari-sari* store. This led us to an important realisation.

Prior to 2009, we acted only as a global player that skimmed the top of the market with our international offerings. We had never really gotten to know the consumer, and because of that, we had never committed to localising our offerings. Grace inspired and transformed our Philippines business. By getting to know her... to relate to her... we embarked on a consumer-centric journey that would unlock the power of our brands, and the creativity and passion of our employees.

Plotting the journey

The Programme was the brainchild of Elaine Limbaco, the consumer insights manager at Mondelēz Philippines. She knew that the company had to go beyond "desk marketing", where market research teams relied heavily on data analysis and reports. Rather, these teams should be engaged in field research. They needed to experience the lifestyle habits and spending choices of a typical consumer. This was a significant organisational innovation—as it was the first-ever attempt to rally our organisation into leaving the office and talking to consumers face-to-face.

In 2009, we began rolling out the Programme. This occurred over three phases, which we called "seasons". The first season lasted for four months, with 48 employees volunteering to take part. They were placed into six cross-functional teams that addressed specific category questions. It was quite a competitive environment with requirements to complete certain tasks under a clear deadline. In addition, it was extremely immersive. The teams listened diligently to our consumer hotline for feedback. They carefully profiled their target customer and went through all the touch-points of their life: daily routines, shopping habits, who they visited and the places they frequented.

The teams then came up with a profile for their target customer: a woman, someone in their mid-30s, with three children. Her name was Grace. She became a living part of the Mondelēz world—and the team soon began referring to this consumer-centric journey as "Amazing Grace". The name stuck. Her picture now hangs in our hallways and meeting rooms. When we make decisions, we ask ourselves, how does this make Grace's life better?

Amazing Grace was a real break from the past. It used to be that we approached consumer insights globally and then applied knowledge from those insights locally. Amazing Grace is a much more personalised approach, where we identify and connect with the local consumer. We've given her a name and face; she celebrates birthdays and attends family gatherings. That's what the first season was all about: establishing the Grace persona and relating to the consumer on a personal level. It gave us some real insight.

Results garnered included 659 insights and 22 new product development ideas with top scoring concept test results. These provided actionable outcomes to be activated within the next six to 12 months to apply consumer centricity to business outcomes.

Season Two went on to expand our emphasis on catering to low-income consumers, and in Season Three we shifted from a consumer insight focus to a focus on shopper insights. This empowered our employees and put the customer at the heart of everything they did. Mondelēz was transformed into a truly consumer-centric organisation.

WHERE IT ALL STARTED: THE PHILIPPINES' AMAZING CONSUMER, GRACE

Name: Grace
Age: 34
Children: Jennifer, 11, Michael, 8, and Ryan, 4

Her husband Ronald was recently laid off from his job at a law firm and is now taking care of the kids during weekdays while Grace works. Family is the most important thing in Grace's world. She shops not only for food, but also for good nutrition. **She is practical and always looks for best value products.** On weekends, her family is happy going to Mass and then visiting the mall and eating at Jollibee. These small moments with the kids help bring them closer together. She feels she can guide her children on the right path when she's part of their lives, and that they will grow up to be good people.

Consumers are not static—they are always changing and if your product stays the same, you lose.

Employee engagement soars

As employees became involved in the Programme, they gained a better sense of purpose about their role within the organisation. Sudip Mall, the general manager for the Philippines, expressed it best when he said,

> Everyone began to understand that their basic purpose here was to work for their boss, Grace. Every meeting would be about Grace. People now had a sense of purpose about who they were, and that purpose was to make today delicious for Grace. If you knew Grace, then you would have an idea that would make her life better. And that meant everyone who worked here could influence the business.

The cross-functionality aspect of the programme also strengthened employee morale. Staff came to realise the importance of their own role and the roles of others. It became apparent that each and every member of staff had the ability, and potential, to influence the business. This catalysed greater collaboration and synergies that brought about new opportunities, not just for the individuals, but for Mondelēz as a whole.

Suddenly, all functions and levels of the organisation began to contribute to the innovation process. It was no longer about the marketing people pitching for a new product and arguing over the validity of their ideas. Now manufacturing, logistics, finance, etc., were all working on product solutions together. The process had become about collaboration and consensus between peers and there was tremendous team energy.

Rudi Ramin, regional marketing manager for biscuits in APAC, commented on how refreshing the new cross-functional team approach was,

> People who don't do consumer work day in day out are now doing consumer work—finance, corporate affairs, supply chain, etc.—and this gives them a different experience, they all really feel there's a better purpose in what they do now... It was a marketing journey with a specific goal.

For example, when the packaging team began to understand the living conditions of Grace and the Filipino consumer, they came up with ideas about package shape, size, and how to better ensure freshness and quality. Product development teams

ELAINE RODRIGO'S FIVE INSIGHTS

Elaine Rodrigo joined the organisation in 2007 as consumer insights director for Asia Pacific. In the past, the company's approach to consumer insights was to take a global insight and apply it locally. That changed after "Amazing Grace". The Philippines was first in line to try the new approach, which has since become a blueprint for innovation in corporations throughout the world.

Elaine points to **five insights** that led to the success of the Amazing Grace Programme:

01 Find a name and a face for the consumer – to enhance consumer "relatability" and help employees relate to her on a personal level. Grace and her picture helped to unify the mission of the organisation. We made her tangible and that made her real in the eyes of the team. Sometimes we work best when we know who we are working for.

02 Design the programme as a cross-functional activity, with cross-functional representation on the insights team – to introduce fresh perspectives from people less immersed in the brand and to build esprit de corps throughout the company.

03 Secure strong senior management endorsement as well as participation from the regional leadership team and the country general manager – to underscore the strategic significance of being consumer-centric and keep the focus on actionable insights. Initiatives that are started at the top have an easier time gaining traction.

04 Create buzz and excitement through the spirit of friendly competition – to increase the fun, recognition and team-building aspects of the journey. Borrowing from the Amazing Race made the process of gathering consumer research fun and exciting. It was not a task but often a release.

05 Activate insights and measure results – because this is not a feel-good programme; it's a critical lynchpin of the company's growth strategy.

began to create flavours, textures, and preservatives that could withstand the warm, moist and often erratic tropical climate. In turn, the Manufacturing team began to understand not just how, but why, we needed to produce and deliver products that might be different from our other global products. And marketers–well they began to understand where Grace was, and where she was not; what she said and what she wanted. These marketing insights changed the way in which we communicated with the market. We had to constantly think about where, and how, to reach Grace.

Innovation became another key outcome of getting to know Grace so intimately. For instance, we produced winning concepts such as the Eden CookSarap Cheese, the world's first shelf-stable pre-grated cheese meant for cooking–which met its sales targets within one month. And as a business, we went from single-digit growth in 2007 to double-digit growth in 2009, which has continued in the Philippines until today.

Tasting success

The Amazing Consumer Journey remains just that, amazing. All of Asia Pacific had been watching as the Philippines executed the programme in 2009 and the enormous success of this programme riveted the Philippines business.

In 2010, The Amazing Consumer Journey Programme was rolled out across the Asia Pacific. Transposed to culturally relevant names–the Programme was dubbed, "Amazing Xiao Fang" in China, "Amazing Su in Malaysia", and "Amazing Budi' in Indonesia"... the names go on. In 2011 the Programme was further replicated in Australia, India, Japan, Malaysia, New Zealand, Singapore and Thailand. By the end of that year, across Asia Pacific, 750 employees from nine markets had participated in the Programme for over 450 days, generating 300 new insights, and 600 new ideas.

Inspired by the success of the Programme in Asia Pacific, other emerging markets across Mondelēz set out on their own Amazing Consumer Journeys, including: Czech, Dubai, Egypt, Poland, Romania, Russia, South Africa, Turkey and Ukraine. In 2013, the Programme was adopted throughout Latin America. The countries were diverse, but the objective remained the same: to observe and understand consumers at a deeper, more intuitive level.

In the Philippines, Amazing Grace is now into its fourth year. The Programme continues to be a great source of innovation, transformation and engagement. Staff have a greater appreciation for their roles and are contributing to the company in new and different ways–one can really feel the momentum and excitement as their ideas contend for acceptance and implementation. We no longer need to muddle through the time-consuming research reports of the past. Our intuition has become an invaluable tool as we've transformed into a consumer-centric organisation. However, this intuition is more than a gut feeling. The Programme helps us to reveal actionable insights that are incubated through a competitive, cross-functional team-based approach to innovation. In addition to their ability to enable multi-functional teams to connect with consumers at a deep level, the campaigns also fully utilise people's curiosity and creativity to unearth fresh insights that inspire breakthrough marketing and sales. Our employees become better utilised and feel empowered. The results are visible and quantifiable in corporate performance dimensions.

Innovation, then engagement, has been central to the organisation's transformation. Indeed, the Amazing Consumer [Grace] Journey has fundamentally changed our perception of the company's consumer insights and strategy function itself, which previously wasn't rated highly in the organisation. Moreover, by adopting a consumer-centric approach throughout the whole organisation, we have become more agile and more competitive.

PROGRAMME IN ASIA PACIFIC

9 markets

750 employee volunteers

450 days

GENERATING

300 new insights

600 new ideas

Final thoughts

There are two moments of truth for marketing executives: first, when the consumer confronts the product, does she take it home? And second, when the product is consumed, does she like it? If both outcomes are met, a virtuous cycle of brand equity commences. To achieve sustainable product growth, I believe these two moments of truth need to be mastered so that they are consistently met. But consumers are not static – they are always changing and if your product stays the same, you lose. The consumer has ever changing needs. For products to adapt, companies must have a strong emphasis on knowing their customer and recognise when they are ready for a change.

The Management team in the Philippines demonstrated better intuition and gained new perspectives on our product offerings through Amazing Grace, our consumer-centric journey. They also displayed greater expertise in generating fresh ideas and, more confidence in their ability to implement such ideas in the marketplace. They could anticipate the latent, yet hidden desires of consumers, even before those consumers could conceive of such unknown desires themselves. These abilities are the crux of innovation. When consumer-centric strategies are in place, and the faces and personalities of consumers are understood–innovations become more powerful and create a sense of engagement far beyond the company's income statement.

Innovation, then engagement, has been central to the organisation's transformation. Indeed, the Amazing Consumer [Grace] Journey has fundamentally changed our perception of the strategy function itself.

Pradeep Pant

is the former executive vice president of Mondelēz International (previously Kraft Foods) and president Asia Pacific and Eastern Europe, Middle East & Africa

Commodity super cycles

A reality check

By Maureen DeRooij

Do commodity super cycles exist, or are we simply seeing patterns in randomness? More importantly, are we in the middle of one that is showing signs of going bust?

Super cycles, or those much observed and quantifiable phases in economic activity, where waves of expansion and growth are followed by a slowdown and recession[i], continue to pique the interests of investors and the media alike. In fact, the possible demise of the current commodity super cycle has spawned many eye-catching headlines, ranging from mere predictions[ii] to the dire "death bells" for the commodities super cycle in 2013.[iii]

Yet in any analysis of the waxing and waning of super cycles and their impact on commodity prices, one question seems to have been overlooked: Is there clear evidence that they exist in the first place or are they simply patterns in randomness?

Depending on who you are or who you represent, there are a number of reasons to be concerned about super cycles and their impact on commodity price trends.

At a national or government level, for example, super cycles can be an issue of critical importance for commodity-dependent economies and commodity-exporting countries looking to steer policy decisions on inflation, currency, and balance of payments, with serious implications for the size and type of economy being developed.

At a corporate level, movements in commodity prices will drive decisions for capital investment to fund expansion of capacity. These decisions are often dependent on how the current price of a commodity relates to the expected future price. If you run an oil or mining company and know that it can take as long as 15 years for a project to be completed and start producing, you need to know if and what kind of return you can expect on that investment before you invest.

And given the increased popularity of commodity indexes since the late 1990s, where a wrong "bet" can have significant impact on one's investment returns, reputation and personal wealth, others with a stake in the game also include individual investors or hedge funds.

History and the super cycle

Theorists, prominent economists and policy makers have studied business cycles for at least the last 200 years; and there is some evidence that cycles were of interest even before that. Coherent analytical frameworks were in place by the early 20th century, including the one developed by Nikolai Kondratiev that was later further developed by the well-known economist, Joseph Schumpeter.

> The latest cycle, the one that we are supposedly in now, is caused by the emergence of China.

In 1925, Kondratiev, a prominent Russian economist, identified three phases of the business cycle – expansion, stagnation and recession.[iv] His basic premise was that the capitalist system would actually not

collapse as a result of a great depression but instead would self-regenerate. Kondratiev analysed 21 statistical series consisting of economic indicators such as interest rates, commodity prices, wages, rents, production and employment. Using data from the French, British, German and U.S. economies, he applied a nine-year moving average to reduce the noise from shorter cycles. He found strong evidence of a long wave cycle in the price level and interest rate series, and only in 6 of the 21 series was he unable to confirm the long wave presence all together. Kondratiev concluded that these capitalist economies exhibited a long wave economic cycle with an average duration of 54 years.

The notion that capitalism could be self-regulating and that it would not suffer an inevitable collapse was extremely unwelcome with the Soviet government under Stalin and Kondratiev was sent to a gulag in Siberia. Later sentenced to a further 10 years, he was actually executed by firing squad on the same day as the sentencing in September 1938. In the 1930s, Schumpeter further endorsed the concept of cycle theory, calling it the "Kondratiev Waves" in honour of the economist.

Many prominent economics and finance professionals have endorsed their findings, and several very detailed studies focused on commodity price cycles have come to light in the last few years.

One of these is Bilge Erten and Jose Antonio Ocampo's "Super-cycles of Commodity Prices Since the Mid-19th Century"[v], which examines the contributing factors behind the start of commodity super cycles, as well as the possible causes for its ending. The authors reason that the key component for the start of a cycle is a sudden rise in demand, often caused by technological innovation such as had occurred during the industrial revolution, or the impulse resulting from industrialisation, urbanisation and increasing population.

Erten and Ocampo identified four super cycles that have occurred since the end of the 19th century, with characteristics differing for each analysed commodity. Each cycle starts with one of the above-mentioned conditions. The first was triggered by the rapid industrialisation of the U.S. driven by, amongst other factors, the emergence of the internal combustion engine and large-scale electrification. The second cycle was initiated after World War II with the rebuilding of Europe and the third was driven by Japan's remarkable manufacturing prowess. The latest cycle, the one that we are supposedly in now, is caused by the emergence of China.

> Are we to sit back and enjoy the ride on the upswing or should we hold on tight as global commodity prices reach a tipping point and start to nosedive?

Erten and Ocampo estimate the length of each cycle to be approximately 30 to 40 years, half of which consists of rising prices, followed by falling prices. Energy, and to a lesser extent metals, exhibit real-commodity cycle price peaks that are higher than the peaks of previous cycles. Non-energy commodities, primarily agricultural products, exhibit the opposite behaviour, with each cycle resulting in peak real-commodity prices that are below the peak of the previous cycle. This behaviour can be explained by the supply side innovations in agricultural efficiency and the growing urbanisation of the world's population.

David S. Jacks in "From Boom to Bust: A Typology of Real Commodity Prices in the Long Run"[vi] uses the data of real commodity prices over 160 years (from 1850 to 2010) for 30 commodities. His typology has real commodity price series consisting of long-run trends, medium-run cycles and short-run boom/bust episodes, which yield some interesting findings related to commodity super-cycles. First, Jacks concludes that indeed, commodity price super cycles have existed in the past, and do exist in the present. He begins by establishing a long-term upward trend in commodity prices but then detects deviations from this trend that last up to 70 years, with upswings of about 10 to 35 years. These upswings are demand-driven, which seem closely related to historical periods of mass industrialisation and urbanisation, combined with acute capacity constraints in many product categories. Second, Jacks' research shows that there are short-term booms and busts within each cycle and that these booms and busts seem to have become exacerbated in recent times. According to Jacks, 15 of the 30 commodities studied are currently in the midst of a super cycle.

Interestingly, and similar to Erten and Ocampo, Jacks observes that although real commodity prices of both energy and non-energy commodities have been on the rise since 1950 across all weighting schemes, over the full duration of his study (160 years) commodities "to be grown" show long-term declines in real prices versus commodities "in the ground" (energy, metals, minerals), which show long-term increases in real prices.

Where are we today?

Research, both old and new, seems to demonstrate that commodity super cycles do exist. And there is a general consensus among experts that we are currently within a commodity super cycle that started in the late 1990s.

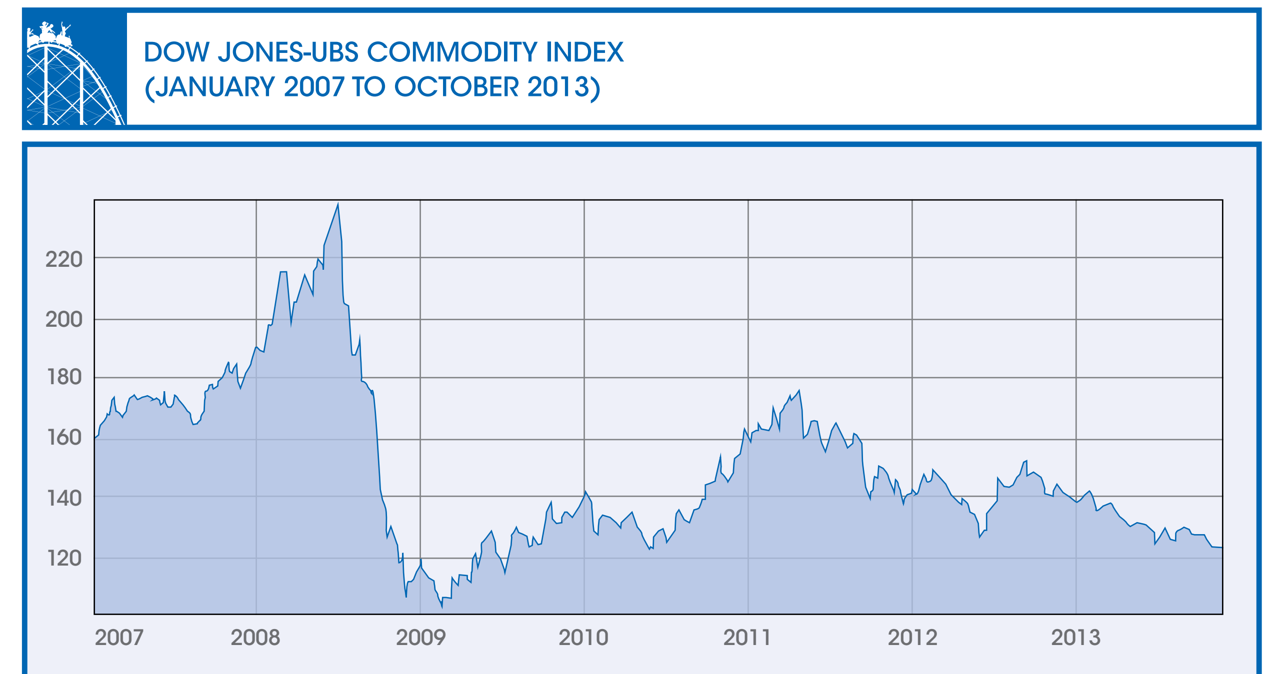

EXHIBIT 1

Source: Dow Jones-UBS Commodity Index

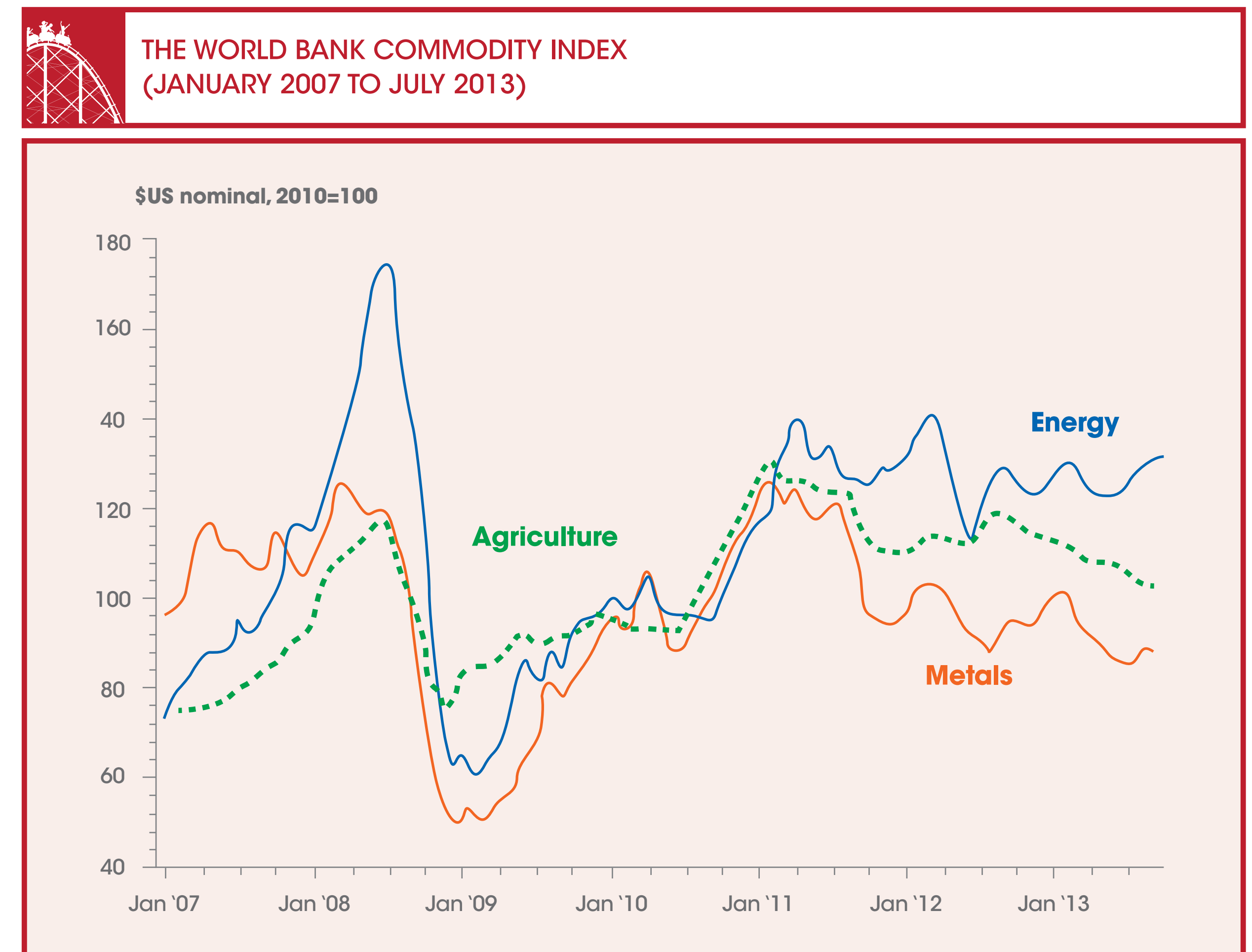

EXHIBIT 2

Source: The World Bank Commodity Markets Outlook, 2013

If we accept this, then the question arises—at which point are we on this commodity price roller coaster? And are we to sit back and enjoy the ride on the upswing or should we hold on tight as global commodity prices reach a tipping point and start to nosedive? Although some surmise we have passed the peak, there is no clear agreement on this issue.

1998 TO 2008: REAPING THE BENEFITS OF THE UPSWING

Between 1998 and 2008, commodity prices nearly doubled, as indicated by the Dow Jones Commodity Index; with certain components, such as oil and gold, increasing by 700 percent during the same time period.[vii] Institutions and individual investors have poured more than US$440 billion into commodity funds since 2004.[viii] Erten and Ocampo attribute this upswing to, "the strong global growth performance by the BRIC economies, and especially China, which is particularly metal- and energy-intensive"[ix]. Undoubtedly, recent growth in these countries is leading to an insatiable demand for food, fuels and metals, feeding into construction of infrastructure facilities to support economic growth as well as demand for consumer goods from the rapid accumulation of wealth.

2008 TO 2011: A DIP FROM A BLIP

The collapse of Lehman Brothers in September 2008 and the global economic crisis that followed led to a sharp, albeit temporary, dip in commodity prices. The Dow Jones Commodity Index fell by over 50 percent between July 2008 and March 2009; picking up again from the second quarter of 2009 (refer to **Exhibit 1**). By early 2011, metals and agriculture prices recovered to their peak of 2008, with energy prices following closely behind (refer to **Exhibit 2**).

2011 TO 2013: A SLOW FALL?

Commodity prices have been trending downward since the second half of 2011, leading many analysts to predict the end of the current super cycle. A comment from Citigroup, for example, states that slowing economic growth in China will be a key factor responsible for declining commodity prices:

> Economic growth in China, the biggest user of everything from copper to cotton to coal, slowed to 7.4 percent in the third quarter [of 2012], from as much as 12 percent in 2010... China has reached a new phase, less focused on infrastructure and urbanisation, both of which are highly commodity intensive.[x]

Looking ahead — are we at a tipping point?

When examining the upswing phase of a super cycle, for example, factors to consider include industrialisation, urbanisation and demographic changes resulting from population growth and economic prosperity. Most often, these factors are symbiotic and simultaneous.

Rapid industrial growth and population pressures have traditionally fuelled the demand for raw materials. The current super cycle owes its origins primarily to the accelerated investment-led growth in China, with contribution from growth spurts in India, Russia, Brazil and smaller yet dynamic economies in Southeast Asia. Since the turn of the century, rapid urbanisation in these countries has called for greater investment in housing and utilities, transportation networks and other infrastructure. Population pressures have also led to a multi-fold demand for food.

Growing wealth and increasing affluence have contributed to the insatiable demand for consumer products and luxury goods, globally. Gold has culturally been an important asset for the increasing middle class and wealthier Indians, while the rich in China are indulging in everything from fine wines to watches.

Modern agriculture has helped many of these countries achieve efficiency in food production, but the simultaneous surge in demand for energy commodities and mining products has helped maintain global prices for these commodities.

Although China and India have achieved tremendous growth, there are still hundreds of millions of people, mostly in rural areas, that are relatively poor compared to Western standards. And whilst perhaps not as spectacular as in China and India, population growth and the associated development and urban migration in other countries in Southeast Asia should also be considered. According to the United Nations, the world population will touch 7.72 billion in 2020[xi], with most of the growth coming from the developing nations. These masses will not stop and sit back, they will work hard to achieve further economic growth and this will require massive amounts of natural resources. I think that all these factors will continue to support commodity prices in the coming decades.

Adding to this are the developments on the supply side. The question here is whether or not this will become increasingly constrained. There has definitely been a slowdown these past few years in new capability coming on line, especially in the mining sector. There is also evidence of resource nationalism as well as social unrest, as recently seen in the mines of South Africa. There are concerns about water, soil and even genetically modified agricultural products that are limiting supply side gains. Even though the threats of short-term supply bottlenecks are a possibility, I do not subscribe to the view that supply constraints can impact prices in the long run. Eventually, supply steps up to fulfil demand—through new resources and/or new technologies—albeit with a lag.

It is another story when it comes to the possibility of an eventual demise in commodity prices. Erten and Ocampo quote Joseph Schumpeter who, in 1939, reasoned that, "demand for raw materials will decline as eventually any industry will attract competition, leading to decreasing profits and hence reducing derived demand for commodities".[xii] This point of view alludes to supply side factors; claiming that capacity increases and over-production (in response to higher prices) play a hand in the declining commodity prices. For example, the discovery and production of natural gas from shale has shifted supply from shortage to glut, and has had a subsequent dampening effect on oil prices.

Another opinion that is of interest is from Alan Heap, former head of Commodities Research at Citibank. In a 2005 report titled "China: The Engine of a Commodities Super Cycle"[xiii] he states that a decline in commodity prices is observed only when developing economies become services-oriented economies and have less demand for raw materials:

> In the U.S., intensity rose strongly during the early 1900s, then plateaued and declined from around 1940 as its economy evolved. The highly materials intensive growth phase came to an end, as the economy became increasingly services-based.

Needless to say, a large number of emerging economies are still behind on the industrialisation curve. Many still rely on the agriculture sector and most are still far from transitioning into service economies.

Conclusion

The simple question of "have we passed the peak of the current cycle?" turns out to be not so simple at all, with proponents and opponents each making convincing arguments. The uncertainty stems from a number of sources, such as firstly, disagreement over the future prospects of big commodity consumers such as China and India, and the potential future rise of other developing economies; secondly, the capricious impact of technological developments on both supply and demand; and thirdly, the occurrence of smaller-scale boom and bust periods within a larger cycle, further exacerbating the difficulty of determining where within a super cycle we find ourselves.

Nevertheless, the simple push of demographic growth and the urge for nations to develop—especially in Asia—means it is unlikely that we are heading into a steep downward phase; even developed nations continue to be sizeable users of both basic commodities (energy, metals) and consumer goods. My expectation is that, as the world's population becomes bigger and wealthier, the demand for all goods, commodities included, will continue to increase. Perhaps this old Chinese proverb says it all: "Do not look for the waves, look for the current."

> It is unlikely that we are heading into a steep downward phase; even developed nations continue to be sizeable users of both basic commodities (energy, metals) and consumer goods.

Maureen DeRooij
is a member of the Advisory Board of Singapore Management University 's Lee Kong Chian School of Business and Country Executive Hong Kong and CEO Asia, Corporate & Merchant Banking at ABN AMRO Bank

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Wealth management IN SINGAPORE

By Francis Koh

Vibrant, growing, challenging

As early as 2015, Singapore may oust Switzerland as the world's top finance hub. But the path forward requires adjustments in the strategic direction of individual firms.

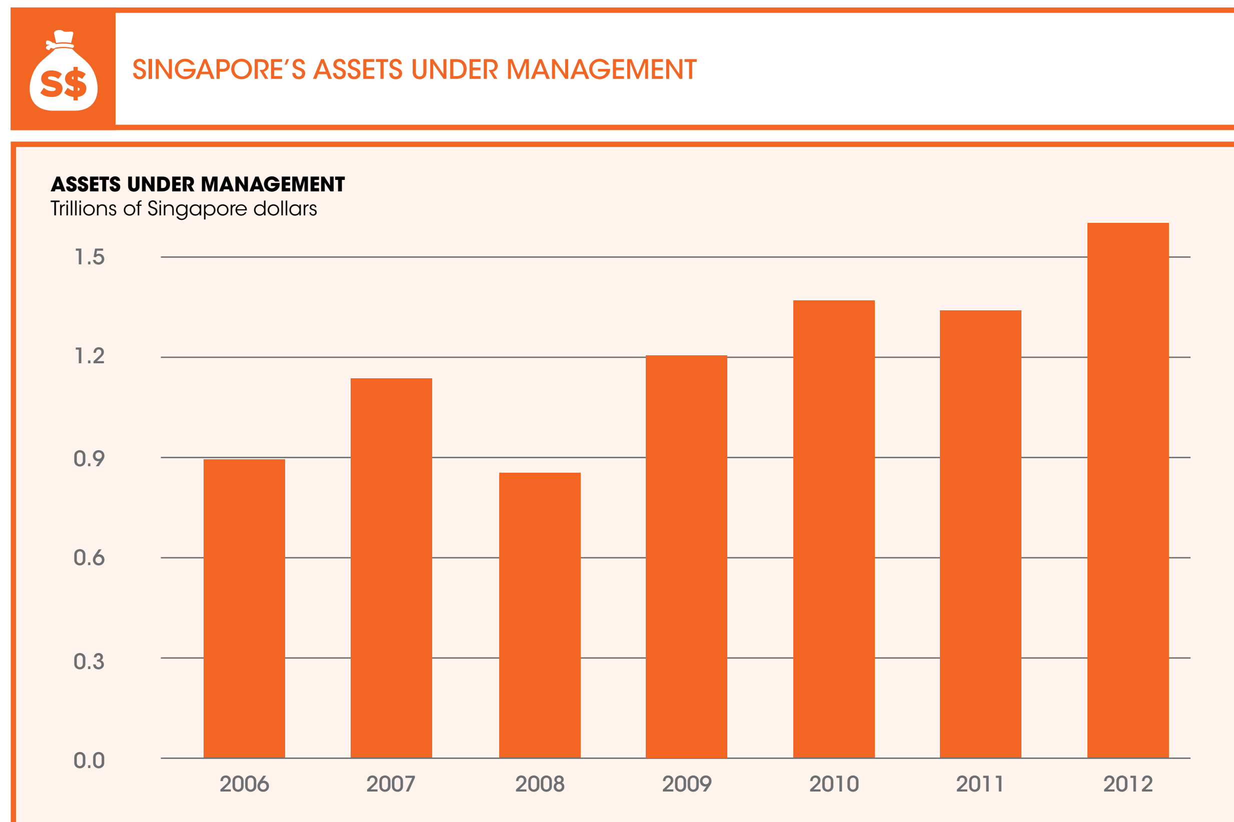
Private wealth continues to grow rapidly across the globe, with 2012 recording new highs in terms of high net worth individuals (HNWI), defined as those with investible wealth over US$1 million, and who now reach a population of 12 million, with aggregate investable wealth totalling US$46.2 trillion.[i] The Boston Consultancy Group reported that private wealth in 2012 grew by around 5.9 percent in the traditional mature economies of North America, Western Europe and Japan, with stronger, double digit growth observed in the new-world regions of Asia-Pacific (excluding Japan), Eastern Europe and Latin America. Thus, in an increasingly complex global environment, wealth managers are looking to aggressively grab a share in the new wealth being created in these new markets, while in the mature markets, the focus will be on retaining existing clients, or wooing them away from competitors.[ii]

In Singapore, the wealth management industry is a buoyant part of the economy. Strategic alliances, mergers and outright new business models are being spawned amid a changing regulatory environment that is employing new technologies and shifting the focus of traditional businesses. Asia's HNWIs are also getting more sophisticated about articulating their needs, passion and direction of investments.

Singapore, with its strong governance and well-developed banking environments, is perfectly placed to meet the increased demand from HNWI clients to provide wealth solutions for their complex needs. The small city-state is challenging the older and more developed wealth management centres, becoming increasingly attractive to investors even from areas outside Asia. "Bright and optimistically vibrant" is how one insider described the future of Singapore as a global financial hub and centre of wealth management services.

In fact, respondents to the PricewaterhouseCoopers 2013 Global Private Banking and Wealth Management Survey believe Singapore will "dethrone Switzerland in the next two years as the world's top centre for managing international funds".[iii] This positive view is supported by the research firm WealthInsight. WealthInsight reported that at the end of 2011, the global private banking industry had Assets under Management (AUM) of US$19.3 trillion. Offshore centres accounted for 42 percent or US$8.3 trillion of this total. Switzerland was the global leader with AUM of US$2.8 trillion, of which over 80 percent of funds were held for foreign clients. Singapore, with a much lower AUM of US$550 billion, was however the fastest growing wealth centre in the world–and WealthInsight believed that it could overtake Switzerland to become the largest global offshore wealth centre by 2020.[iv]

This is not to discount the position of Hong Kong, which continues to compete with Singapore for both clients and market share, though AUM in Hong Kong tend to be more Sino-centric. Whereas Singapore, in tandem with the increased wealth in the region, recorded 22 percent growth during



Source: The Monetary Authority of Singapore, 2012 Singapore Asset Management Industry Survey

2012 in total AUM to reach an all-time high of US$1.33 trillion. Of this, about 80 percent was sourced from outside Singapore, demonstrating the country's important role as a hub serving regional and international investors.[v] Moreover, it is believed that Singapore as a sovereign state would be better placed to manage wealth over many generations.

But despite this enthusiasm, the reality is that wealth management firms in Singapore are grappling with the same challenges that their counterparts across the globe have to deal with—which include managing a host of regulatory complexities that are being imposed by most governments, improving their AUM, generating new revenues, managing increasingly sophisticated customer expectations and battling rising costs. So what is it that will enable the wealth management firms in Singapore to win this global battle for supremacy? How can they ensure that they successfully compete and excel, making Singapore the global hub for wealth management services?

Increased regulatory complexities have changed the landscape

In the recent past, some analysts have been postulating the demise of offshore banking, a key element in wealth management. This is primarily due to a legacy issue involving certain offshore banking centres that had grown to be conduits of undeclared money. These centres prospered with the help of statutory acts providing bank secrecy, which tolerated the acceptance of indiscriminate deposits without rigorous know-your-client processes. Many of these centres were allegedly involved in money laundering and blacklisted by the Organisation for Economic Co-operation and Development (OECD). There is now a broad consensus in the industry that bank secrecy as practised previously will not be an option for banks in the near future. International co-operation against tax evasion and other forms of illicit cross-border fund transfers have made strenuous demands on financial institutions removing bank secrecy as the raison d'être for offshore banking. Consequently, those offshore financial centres that depend on regulatory provisions of bank secrecy as the mainstay of business will decline.

For its part, Singapore is keen to ensure the city-state is not seen as a tax haven for the wealthy from Europe, China, Indonesia, Malaysia and elsewhere, without diminishing its potential for sound financial services to the wealthy. Stringent regulations came into effect in July 2013, and addressed concerns from Europe that, as the veil of bank secrecy in Switzerland is lifted, tax evaders will head to Southeast Asia. Banks in Singapore were asked by the Monetary Authority of Singapore (MAS) to review their account holders, and were forced to decide whether or not they wished to retain them. The tighter rules were intended to fall in line with new global standards announced the previous year, which treat tax crimes as a money-laundering offence.[vi]

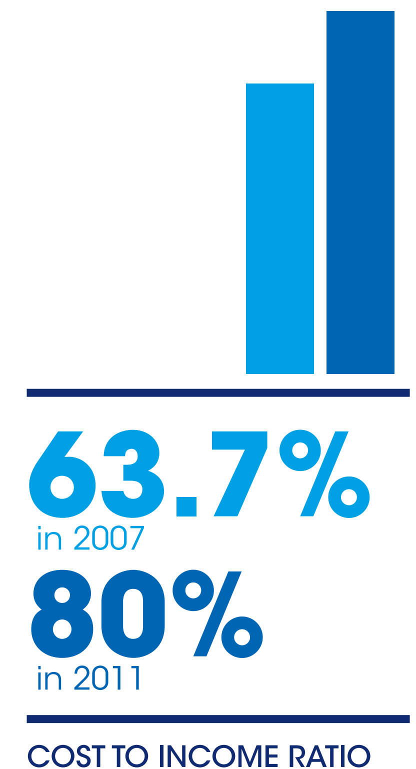
Singapore offers a politically and economically stable jurisdiction, supported by a legally efficient environment, including the Singapore International Arbitration Centre. It is also known for its "competent, clean, and trusted financial sector",[vii] which is particularly attractive to HNWIs from the region. MAS has assiduously introduced regulatory reforms and actively promoted the growth of the banks and encouraged financial innovations. It has urged wealth managers to move away from a transaction-driven approach of pushing products to a client-centred approach, which focuses on customised advice that will meet the financial needs and life-cycle circumstances of their clients. MAS has also repeatedly stressed the need to keep the financial centre "clean", introducing Client Advisor Competency Standards (CACS) examinations in September 2011.

Transforming the business model

But with these added regulations, there is also a dramatic surge in the cost of doing business. The 2013 Capgemini, RBC Wealth Management and Scorpio Partnership Global HNW Insights Survey report states that wealth management firms have seen their cost to income ratio increase to 80 percent in 2011 from 63.7 percent in 2007—and a key driver has been rising costs due to initiatives such as hiring new compliance staff, upgrading platforms and training employees to meet the additional regulatory requirements.

Given this environment, it would not come as a surprise that the industry is expected to go through a period of business consolidation. The bigger banks have a larger balance sheet and the economies of scale to deal with the regulatory challenges, while the smaller boutique players are expected to struggle as their cost-income ratio continues to spiral up. While these small players may decide to develop a business model that is focused on providing specialised services to a small niche of HNWI customers, it is far more likely that they would instead look for mergers to help spread their cost base. This pattern of consolidation has already begun, as seen in Julius Baer's purchase of Merrill Lynch Bank of America's non-U.S. wealth management divisions.

The regulatory pressure has also, in some cases, resulted in a shift in the customer profile, where firms may choose to de-market certain "expensive" clients. For instance, legislation, such as the US government's 2010 Foreign Account Tax Compliance Act (FATCA) requires that wealth managers disclose account details of their U.S. customers to the Internal Revenue Service. Wary of the anticipated increase in cost, and meeting other challenges such as the additional reporting burden and due diligence regulations, several private wealth management firms,



particularly the smaller ones, are limiting or altogether ceasing to offer their services to U.S. citizens.

Finding new customers?

So where can wealth managers in Singapore look to for growing their HNWI customer base and improving top line growth? Singapore is starting to become attractive to investors outside Asia, but the majority of clients are closer to home, with their wealth made in resource-rich countries such as Indonesia, Thailand and Malaysia. This offshore wealth, which is wealth booked in a country where the investor has no legal residence or tax domicile, will remain popular because the HNWI clients need the expertise, service and discretion which may not be offered in their own country.

Offshore wealth, which is wealth booked in a country where the investor has no legal residence or tax domicile, will remain popular because the HNWI clients need the expertise, service and discretion which may not be offered in their own country.

But a new trend appears to be emerging, where growth will come not only from the fact that Singapore is a wealth management hub, but also because it is a flourishing business hub for corporates that wish to set up offices here to deal across the Association of Southeast Asian Nations (ASEAN). Hence, even if the business is, say, dealing in palm oil in Indonesia, it can be expected that there will be significant office space taken up in Singapore, and the entrepreneur/client is more than likely going to keep his family in Singapore and establish a base here for corporate decision making—and this would suggest that that the wealth management industry could grow around these people, servicing their requirements.

Wealth managers therefore need to extract value and deliver services to those corporate owners and principals residing here. They would have to realise that while the off-shore model is not dying, it is definitely morphing to a more hybrid off-shore cum on-shore relationship. This view is supported by the Boston Consulting Group's Global Wealth 2013 report, which believes that new off-shore wealth created in a region would essentially flow to the off-shore centre in that region. Hence, Singapore, along with Hong Kong, is well placed to serve the increasing wealth of HNWIs, particularly from the new wealth created in the fastest growing Asia Pacific region.[viii]

And this trend will also help with managing cross-border issues, because as an on-shore client, there are no issues with banking a resident "foreign" client, and hence even from a regulatory stand point, it makes more sense for assets to be held in Singapore and for clients to have business interests here. Thus, the bulk of the growth will come from the business owners that have significant equity share—either in family-owned businesses or the large corporates that will expand through Singapore—and it is these business owners that the industry needs to focus on.

The off-shore model is not dying, it is morphing to a more hybrid off-shore cum on-shore relationship.

But these business owners are likely to be over-banked, given the highly competitive industry in Singapore. So what is it that would enable a wealth manager to become the leading adviser to a big client? What is the value proposition that HNWIs are looking for?

The evolving customer: meeting client expectations

Hand in hand with the changing wealth environment, the profile of the HNWI is also changing. They are more sophisticated, better educated, more exposed to varied information sources, and demanding a higher level of service. They no longer wish to be passive investors. Evidence that HNWIs have over-invested in real estate and/or passive cash are also signs they will continue to need professional wealth management in the near future and the level of service will need to go beyond such investment. Although there is increased and enhanced demand for lucrative yet trustworthy investment advisory services, Asian clients still want to preserve family wealth and leave a meaningful legacy, or manage their personal family affairs and run active businesses. They may also need to have special structures to manage family wealth and/or intergeneration gifts. And as Asia ages, there will be more "old" wealth to be transferred to the next generation. This inter-generational transfer of wealth will add to the demand by the younger generation for professional wealth management services.

While wealth solutions and products, such as trusts, financial investments and insurance will always remain important, HNWIs are now also looking at investment in "goods of passion" such as art, wines and watches, all of which continue to increase in value with enhanced demand. Shariah investments, which are those investments that comply with the principles articulated for Islamic Banking, are just starting to emerge and will gain popularity with time. The interest to accumulate more wealth in a low interest rate environment is also encouraging HNWIs to overcome "home bias" and invest beyond their own shores.

Thus, to become the leading adviser to a big client, wealth managers will need to offer their clients not only wealth management services—that is a given—but in addition there would be a need to provide other value-added services, be it corporate connections, connectivity to an international global network of say investment bankers, or putting HNWIs in touch with counterparts globally through a solid network that can help their business grow and expand. Hence private banking in an international bank, which was for many

years considered to be aloof and elitist, would now see itself increasingly interacting and relying on other parts of the bank, such as global banking or corporate banking, to further its own business.

THE GROWTH OF DIGITISATION

On another front, there is also an increased demand for digital channels, and it is expected that delivering a quality digital experience to clients will emerge as a key element that sets apart the leaders in the wealth management industry—particularly to those tech-savvy HNWI clients. Big data analytics in client advisory services will become more important. This is an area where we expect to see significant investments being made in the future, as firms ramp up their information technology (IT) networks. It will also have an added benefit in that it would not only offer additional value to their customers, but also meet new regulatory standards with automated risk management and reporting processes, while improving scalability and relieving pressure from rising middle- and back-office operating costs.

There is also an increased demand for digital channels, and it is expected that delivering a quality digital experience to clients will emerge as a key element that sets apart the leaders in the wealth management industry.

The *Financial Times* reported that banks and other financial institutions felt the need to "invest in technologies to respond to changing customer demands, reduce risks and battle cyber crime." It also estimated that in 2014, "large North American financial institutions alone will spend US$73.8 billion on IT improvements, including software, hardware and professional services."[ix]

RAISING COMPETENCIES

HNWI clients are increasingly demanding a one-stop service, to be delivered by highly experienced and knowledgeable staff. There is therefore a heightened demand for skilled and trained staff in the wealth management industry, in particular for the role of a Client Relationship Manager. The fact that competition for talent would increase was identified by MAS several years ago. The Authority has encouraged the industry to train more professionals, and quickly.

Banks and MAS are intent on developing a pipeline of manpower for the industry and thus far, about 1,700 professionals have been certified under the Financial Industry Competency Scheme (FICS).[x] Academic institutions too have started playing their part towards contributing to the pressing need for more competent wealth managers and client relationship managers. The Singapore Management University, in collaboration with the Wealth Management Institute (WMI) and supported by the Swiss Finance Institute (SFI) and Yale University, offers a Master's degree in wealth management to aspiring and incumbent wealth managers. This offers qualified candidates opportunities for internships during their studies. And so far, more than 400 participants have graduated from the programme.

The future of wealth management in Singapore

Are Europe's challenges the same for Singapore's wealth management industry? Essentially yes, as whatever happens in Europe will affect Singapore either now or in the near future. European banks operating in Singapore will also be burdened with the same problems. Regulatory changes are a given in this industry, where compliance impacts reputation. To these challenges, and with Southeast Asia in mind, I would also add the wild card of political uncertainty.

Asia's growth story is still very much intact and it will continue to raise income levels in the region. Amongst the Asian countries, Japan, China, India and Indonesia will continue to grow and be ranked amongst the world's largest economies, and their wealth will grow in tandem. Both Singapore and Hong Kong are well placed to serve the increasing wealth of HNWIs due to their developed financial markets, including infrastructure, human resources, IT and a conducive business environment. Singapore thus stands to play an even bigger role in the region. Hong Kong is near China and will benefit from that proximity, notwithstanding that Shanghai too is a fast-growing centre, and is now poised on the starting blocks in the sprint for the asset-rich or cashed-up.

The close collaboration between industry and regulatory authorities is a key strength of Singapore's wealth management industry and augurs well for its future as a competent and clean wealth management centre for both onshore and offshore banking.

Hand in hand with the positive economic growth recorded in the region, and a greater level of sophistication on the part of the HNWI, the future for Singapore's wealth management industry is thus "optimistically vibrant".

At the same time, the relative positioning of international financial centres is also clearly shifting and as we move forward into an era of greater transparency and shifting wealth creation patterns, "centres located in emerging markets stand to gain increased stature".[xi]

Singapore is well positioned to take advantage of that shift, whether in 2015 or 2020.

Francis Koh
is professor of Finance (Practice) & director, MSc in Wealth Management Programme, Singapore Management University

The close collaboration between industry and regulatory authorities is a key strength of Singapore's wealth management industry and augurs well for its future as a competent and clean wealth management centre for both onshore and offshore banking.

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Managing INNOVATION RISK

By Madhabi Puri Buch

Generating return on innovation without betting the bank

Risk in banks is nearly always considered a dirty word. Yet a handful of simple ideas can help manage innovation risk effectively.

Innovation, almost by definition, is a risky business. But the returns that banks generate are almost exclusively for managing risk (prudently), rather than for staying away from it altogether. A handful of simple ideas can help manage innovation risk. When institutions are alert and see every strong emerging consumer or technology trend as an opportunity to build competitive advantage, there could be significant return on innovation waiting to be harvested.

Back to the future in ancient Babylon

The time was 2000 BC. The high priest of the temple had just finished carrying out his religious duties for the morning and was making his way to the courtyard to supervise the acceptance of grain from the local farmers into the temple's granaries for safe-keeping. As always there were those farmers who were pleased with their harvest. Others grumbled. Suddenly, his young assistant, who was widely touted to succeed the high priest, turned to him to ask a rather provocative question. "What if the temple were to loan seed-grain to farmers who didn't have any, and recover the repayment with interest from the next harvest?"

There were gasps. The buzz in the temple was fast and furious. "Another crazy idea from that young whippersnapper." "Are you out of your mind?" "That would be a foolishly risky thing to do." "How could we be sure we'd get the grain back?" "What if the owners returned early and asked for their grain back?" "What if there is a drought next year?" "Do you want to succeed me as high priest or not?"

But that was how modern banking was born. Credit risk, liquidity risk, and market risk became part of temple life. The assistant's "one bright idea" probably saw him well on the way to becoming high priest.

Innovation and the R word

The world today is abuzz with two strong forces shaping its future. The first is the drive for banking to become even more boring (we have had enough innovation in financial engineering for a while), and the second is the push for technology to do more and more for the common man. We just don't seem to get enough of the latter. In respecting both of these forces, this article focuses on innovation as it relates to consumer and technology trends alone and how innovation in this space can help banks build competitive advantage in the core business of serving their customers.

But innovation, almost by definition, is a risky business. Innovation is about something new and something that is new is usually not proven and is characterised by uncertain outcomes and unknown problems. Something that is new is usually created by new companies, which by definition are those without established track records and with an unpredictable future. As a result, an employee in an organisation can lose his job for doing something new ("Well, that did not go so well") but can rarely lose his job for not doing it—who is to know what opportunity was lost? And while this is true for many organisations, it is particularly true for banks. And perhaps rightly so. Banks deal with their customers' hard-earned money, often their life savings, and all of their financial information is highly confidential. None of this can be treated lightly.

> The returns that banks generate are almost exclusively for managing risk (prudently), rather than for staying away from it altogether.

Naturally, we would all like our bankers to be concerned about taking risks with our money or our data. However, we would

Building an innovation practice is all about learning how to deliver *new* value to the customer, manage the embedded risks prudently, build competitive advantage for the bank and deliver return on innovation to its shareholders.

also like our bankers to think about and work hard at making our lives a lot easier; indeed technology is giving them an opportunity to do so. We would like them to learn to manage innovation risk, just as they learnt to manage credit risk and market risk in order to deliver returns to depositors and shareholders.

Darwin@work in banks

Risk management in banks has evolved. Many would argue not far enough, as the events of 2008 taught us. This is true, and we need to continue to learn and to evolve. The building blocks of effective risk management, while reasonably well understood, are continuing to evolve. There are several models to measure potential risk and potential return for a new initiative. Banks have also developed policies on what kind of risk-return profile they want as well as practices on how to mitigate known risks; and standards have been established on how to provision for residual risks. Over time, regulators have also introduced guidelines to prevent excessive concentration of risk

Fortunately, in some jurisdictions like Singapore, regulators are proactive and forward thinking. They are astute and clearly see the emerging consumer and technology trends, anticipate demand from citizens to adopt any new technology, and proactively issue guidelines[i] as a frame of reference for the banks as they learn to mitigate innovation risk.

So the ball is squarely in the court of the banks. They need to evolve their innovation practice to deliver new value to the customer, manage the embedded risks prudently, build competitive advantage for themselves and deliver return on innovation to their shareholders.

Building the innovation practice

A suggested framework for building a strong innovation practice might include some of the following ideas. They are by no means comprehensive.

1. FROM INSIDE TO OUTSIDE

An interesting thing about the service industry is that before a customer gets served, an employee gets served, either by the system or by another employee. And so, almost any innovation that you would like to serve to the customer can first be served to–and be tested–by employees. This takes place in a very controlled, ring-fenced, risk-mitigated manner. Examples of possibilities include a new mobile application, a new biometric authentication engine, or a new analytics-based advisory service. The possibilities are endless.

So innovate internally and innovate early. As soon as things stabilise, just turn the innovation outward.

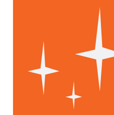
2. FROM THE ICING TO THE CAKE

An interesting thing about icing is that it really does make a difference to the taste of the cake, without ever getting into the cake. There is a good reason why critical systems within a bank are called "critical". They are. And it would be a bad idea to touch them except when the highest level of confidence in doing so is present. But there are a large number of services that can be delivered to the customer, that either don't touch the critical systems, or touch them in a highly controlled manner. For instance, location-based merchant offers to your credit card holders can be offered without ever touching your core credit card system.

So innovate at the edges, innovate early, and as soon as things stabilise, allow the innovation to go in deeper.

3. FROM SMALL TO BIG

An interesting thing about money is its materiality, both for the bank and the customer. And bankers have practised the art of limiting risk by limiting the size of transactions ever since time immemorial. Daily limits on ATM withdrawals, limits on



BUILDING AN INNOVATION PRACTICE

1. FROM INSIDE TO OUTSIDE

In the service industry, almost any innovation that you would like to serve to the customer can first be served to - and be tested - by employees in a very controlled, ring-fenced, risk-mitigated manner. Innovate internally, innovate early.And in the fullness of time, turn the innovation inside out.

2. FROM THE ICING TO THE CAKE

An interesting thing about icing is that it really does make a difference to the taste of the cake, without ever getting into the cake. Innovate at the edges, without touching critical systems, and as soon as things stabilise, allow the innovation to go in deeper.

3. FROM SMALL TO BIG

An interesting thing about money is its materiality, both for the bank and the customer. It is useful to allow innovative transaction modes for small values. And when the technology proves itself, move to bigger things.

4. FROM ONE WAY STREETS TO EIGHT LANE HIGHWAYS

An interesting thing about customer service is that the traffic on the two sides of the communication road is not equally sensitive. Allow infinite innovation for the non-sensitive legs of communication. When the technology evolves enough to provide a high level of comfort, open up the other side of the highway.

5. FROM BETA TO LIVE

Taking a key learning from the tech industry, it's possible to take little or no flak for initial teething troubles. Launch in beta, manage expectations, get valuable customer feedback before going live, and position the bank as a true blue Innovator.

online transfers and alerts for credit card charges beyond a limit have served banks and their customers well in terms of mitigating risk while improving the convenience quotient of a bank's service offerings.

So it's useful to allow innovative transaction modes for small values. Only when the technology proves itself, should you move to bigger things. Chances are Pareto's 80-20 principle will apply and you might never need to move very far from small.

4. FROM ONE-WAY STREETS TO EIGHT-LANE HIGHWAYS

An interesting thing about customer service is that the traffic on the two sides of the communication road is not equally sensitive. Just because data going out from the bank has to be highly protected does not mean that queries coming into the bank have to be highly protected. For instance, a bank might allow any number of channels to integrate with its customer service system to log in a query. So long as the answer to the query goes out only to pre-registered, pre-authenticated channels like the customer's registered phone number, email or postal addresses.

To allow infinite innovation for the non-sensitive legs of communication, innovate early. When the technology evolves enough to provide a high level of comfort, open up the other side of the highway.

5. FROM BETA TO LIVE

An interesting thing about customers is that they are not all alike. They have completely different responses to innovation and in their personal capacity, could be early adopters or laggards, or any group in between. Somehow we assume that we need to cater to the least common denominator when we do something new for our customers...

Taking a key learning from the tech industry: If we were to launch every new service in beta mode, we would clearly signal to our customers that not every crease in the offering has been ironed out (barring security, of course, where required, as this is non-negotiable for bankers), and, that "in the interest of getting constructive feedback from our customers, we are making a beta version available".

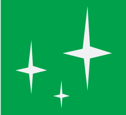
Not only would we be able to move nimbly on innovation, and take little or no flak for initial teething troubles, but also we would also genuinely obtain valuable customer feedback that would actually help us refine our offering and make it more valuable to the customer.

So launch in beta, manage expectations, get valuable customer feedback before going live, and position the bank as a true blue Innovator, able to ride those trends that seem to be firmly entrenched in the world.

The big four trends

So where is the pot of gold in innovation? Many trends emerge and many die out as well, sometimes fairly quickly too. But the good news for banks is that they need only ride the reasonably established trends and not invent the next big one. And that brings us to SMAC. These are the big four trends that look like they are here to stay and are growing bigger and bigger by the day.

S: SOCIAL MEDIA. When people stop thinking of Facebook as cool and start thinking of it as a necessary utility like electricity or water, then it looks like its here to stay. The facts are that there are one billion active Facebook users every month, with 50 percent of them logging in on any



INNOVATION, THE BIG FOUR AND THE BIG O

S: SOCIAL MEDIA. When people stop thinking of Facebook as cool and start thinking of it as a necessary utility like electricity or water then it looks like its here to stay.

M: MOBILE. When mobile internet access in China (75%) surpasses PC internet access (71%) and penetration of smart phones grows at 52 % per annum in India, mobile has indeed arrived.

A: ANALYTICS. When 92 percent of all the data in the world has been created over the last two years, and McKinsey estimates that Big Data could generate over US$1 trillion in revenue/savings per year, it is very much a part of the future

C: CLOUD. When Gartner estimates that 60 percent of all server workloads will be virtualised by 2014, it looks like it deserves a serious look.

O: OPEN INNOVATION. When hundreds of entrepreneurs and angel investors across the globe want to build innovative services for your customers for free, maybe you should let them!

given day. Around 48 percent of 18-34 year olds check Facebook when they wake up, while 28 percent of them check the social media site before they get out of bed.

M: MOBILE. When China declares that mobile Internet access (75 percent) has surpassed PC Internet access (71 percent) and India declares that smartphone penetration is only six percent of the total subscriber base of 1.1 billion but growing at 52 percent, it looks like it is becoming serious.

A: ANALYTICS. When 92 percent of all the data in the world has been created over the last two years, and machine-to-machine data hasn't even begun, and when McKinsey estimates that Big Data could generate over US$1 trillion in revenue/savings per year, it looks like this is very much a part of the future.

C: CLOUD. When Gartner estimates that the size of the cloud computing market could reach US$150 billion in 2013 and that 60 percent of all server workloads will be virtualised by 2014, it looks like it deserves a serious look.

The mega trend: The big O, open innovation

To my mind, the most interesting thing about innovation today is that organisations don't need to drive it internally alone. There are a large number of innovators out there who are willing to innovate for your customers free–if only you would let them. There is a huge and growing ecosystem of entrepreneurs and angel investors who will passionately pursue the development of value added services for your customers, if only they could speak to you and your systems.

As a bank, even if it is only in line with the spirit of "One Way Streets", if you were to permit them just one way access, you could open up a huge opportunity for innovation and value addition for your customers. All of it for free!

This then is the power of Open Innovation.

Rewinding to the future, imagine that you are the assistant to the high priest at the Great Temple of Babylon in 2014. What would you want to say to the high priest? "Is it possible to generate Return on Innovation without betting the bank?"

> Building a low risk innovation practice: innovate inside, innovate on not-so-critical systems, innovate small, innovate on non-sensitive legs of communication, induct your customers into your innovation.

Madhabi Puri Buch

is a director at Agora Partners Pte. Ltd.

Reference

[i] Monetary Authority of Singapore (MAS) Technology Risk Management Notice and Guidelines, June 2013: In recent years, various technology innovations in areas such as card payment, mobile technology and system virtualisation have helped to expand financial institutions' (FIs) business offerings and customer reach. Information technology (IT) outsourcing has also become more attractive to FIs due to the abundance of outsourcing services. Against the backdrop of an increased reliance on complex IT systems and operations in the financial sector is the heightened risk of cyber attacks and system disruptions. In this regard, FIs are expected to continue to deepen their technology risk management capabilities and be ready to handle IT security incidents and system failures.

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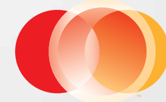

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