Viewpoint

On Transformation

Lucio A. Noto

On June 30 of this year, Arthur D. Little was honored to welcome Mobil Corporation Chairman and Chief Executive Officer Lou Noto to address some 300 senior members of the Arthur D. Little staff at our corporate leadership conference in Charleston, South Carolina. The theme of the meeting was ^Transformation" – a topic on which Mr. Noto has few peers. Since becoming CEO of Mobil in 1994, Mr. Noto has personally overseen the transformation of Mobil. Three years ago he expressed the belief that, to become a great company and to respond to the dramatic rate of change in the market, Mobil needed to significantly increase the pace of divesting non-core assets, reducing overhead costs, and focusing on developing growth opportunities. Toward that end, he set highly ambitious five-year stretch targets – which Mobil has achieved two years ahead of schedule.

Lou Noto spoke to us not only as the leader of one of the world's great international companies and as a leader of change, but as one of our key clients. We at Arthur D. Little are proud to have played a role in Mobil's transformation. Since Mr. Noto took Mobil's helm, we've been privileged to work with Mobil on growth, strategy development, restructuring, and corporate governance issues. In this article, derived from his presentation in Charleston, Mr. Noto offers his personal observations on the experience of transformation.

Good morning. It's a great privilege and an honor to address you today. We at Mobil are proud of the good things the company has done, and we're grateful for Arthur D. Little's contribution to a lot of the changes we've undertaken.

Let me start by saying that „Transformation" – the theme for this meeting – may not be the right word for what Mobil is involved in. „Transformation" implies wholesale change. It doesn't fully contemplate the value of past success and past progress. I use the word „focus" to describe Mobil's activity, because although the changes have been dramatic, we're building on our predecessors' contributions. The successes we enjoy today are a direct result of the good work and efforts of many people who went before us. By the same token, it's part of our job to leave behind for the next generation of management the legacy assets that will continue to propel the company forward in the future.

We certainly don't think we've done everything right during this process, and we approach this with a great deal of humility. But I'd like to share with you a few observations about what I believe has contributed to our success.

Observation 1: The CEO should not throw out the baby with the bathwater – and, in fact, should consider whether the bathwater itself could have some positive value. Translation: value the quality and contributions of your predecessors. Value the culture that you found in place. Build on it. For example, my predecessor, Alien Murray, who took over the company in 1985, worked to re-focus Mobil on our core competencies. We divested businesses such as Montgomery Ward and Container Corporation and went back to doing more of what we do best.

When I had the privilege and honor of becoming CEO in 1994, my greatest advantage was that most of Alien's team was still in place. That gave us the luxury and time to look at our business without feeling that we had to change everything immediately.

Observation 2: The „vision thing" is important. People scoff at this process, but it's important. A vision sets a road map for your company. What's even more important is the process you go through in getting that vision down on paper. It makes you ask a lot of questions about what you do and do not stand for, what your values are, where you're trying to go, and what you're trying to be. It's not easy. It takes time and it takes effort.

In shaping Mobil's vision, we spent a lot of time with our folks around the world. There was a lot of questioning. There was a lot of doubt, a lot of cynicism. But at the end of the day, the process was worth it. It was a unifying and a highly positive thing for Mobil. It sharpened our focus on what we are trying to do and be.

Observation 3: *You don't have to wait until something is broken before trying to improve it.* That's been our approach at Mobil. We felt we inherited a good company – a profitable company that had gotten closer to its roots. But, frankly, we thought we could do better. We quickly came to the conclusion that we had no business being in businesses such as real estate, phosphate mining, and fertilizer production. These weren't our core businesses, and so we brought no value to the table in these areas. We got back down to oil, gas, and chemicals.

Then we took a look at our chemicals business and found it was actually two different businesses for us. One is petrochemicals, a business very close to our core competencies since it requires big, complex plants, multibillion-dollar investments, and close integration with refining activities. It's something we know how to do well. It’s a business we want to grow and nurture.

On the other hand, we also had a big investment in plastics. In this area, many of our competitors were smaller and more nimble. A lot of them didn’t live by the same operating standards that we felt compelled to live by – not just because of laws and regulations, but because of what we stand for as a corporation. In this case, it put us at a disadvantage. So we exited that business.

Observation 4: You have to come to some very rapid conclusions and act on them quickly. If your company is behind the eight ball, you have to be willing to make the investment needed to improve your situation. If others are doing a better job and you can’t compete, get out. Get what you can, but get out. Get back to doing the things you know how to do and can do well. This certainly has paid off for Mobil.

Observation 5: Simplification should be the cornerstone for change. We’re very good at making simple, good concepts almost unintelligible – and, sometimes, so are consultants. We can end up focusing too much on the corporate navel and not enough on our customers and competitors. We start to second-guess things and not use our own good business judgment.

We at Mobil have a lot to learn. We’ve got to learn that once we reach a conclusion and buy into it, we should trust our business judgment and get the job done rather than just keep talking about it. A huge amount of energy is wasted these days in guessing and second-guessing. When I first learned about the KISS principle – Keep It Simple, Stupid – I didn’t really appreciate it. Three years into this job, I now have that message posted on my wall and consider it one of the most important things I need to remember. And you do your clients a great service when you stay focused on this principle, too.

Now let me talk for a minute about goals. I’ve found these to be highly motivating. Simple goals can produce powerful results. Soon after I became Mobil’s CEO in 1994,1 started jotting down notes about what I was going to say at an upcoming Mobil management meeting – my first as CEO. I thought, „I’ve got to give these folks a message, some clear objective – tell them what we’re after.“

I considered what Mobil had done in the previous five years, and thought, „Okay, look. If we do our job right we ought to be able to accomplish three things within the next five years: Earn $3 billion in profits, make at least a 12 percent return on the long-term capital we have in the business, and raise the stock price – then about $70 a share – to $125.“ $o I went to my management meeting and laid this out for my team – with no backup analysis, no input from consultants telling us what was right or wrong about it. My top people had never heard of such a thing. There was total disbelief. My presentation was greeted with an unholy silence.

But I have to tell you that those three simple guide-posts turned out to be an incredibly strong motivator for the corporation – because everyone could understand them, including secretaries, shipping clerks, and even senior executives. And the scorecard was public. We gave this message to our shareholders, our Board of Directors, our executives, our customers, our competitors, and Mobil employees around the world. Then we set out to achieve our goals. It was a wonderfully motivating process for the company.

Going public with our goals wasn’t something Mobil was accustomed to doing. Our approach was, „We know what our job is, so leave us alone and let us do it. When we finish, we’ll tell you about it.“ The world no longer lets us operate like that. $o the goal-setting process itself has been valuable for us.

Let me tell you what else I learned. I knew the goals I was setting were a real stretch. As I said, my management team thought I was crazy. But we achieved those three goals in three years instead of five. The only problem is, we didn’t make sufficient progress versus our competition. We didn’t move ahead of the pack. So we now have a new set of goals, which include becoming a top-quartile performer in the industry. In our business, that means we must be either number one or number two – which, when you’re competing against an Exxon, Shell, BP, Chevron, or a Texaco, is not easy.

We’ve had to ask ourselves, what will it take to do this? We concluded that it will probably take $5 billion of profit for Mobil by 2001. It will take a 14 percent average return on capital employed, instead of a 12 percent return. And, if we do all that right, the stock price, on a pre-split basis, should be at $200. So those are our new goals.

As with the first set of goals, these have been met with disbelief. People ask me, „How did you get there – how did you calculate these goals?“ I tell them, „All I have to know is the destination. It’s up to all of us to find the road map to get us there.“ I say that because if you try to calculate these things, you’ll never do anything. Because what you can calculate is generally inside your „box.“ And if you’re going to stay inside your box, you’re not going to be Number 1 or Number 2 in your business. Somehow you have to force the organization out of the box.

One of our problems is that we are so results/ consequences-oriented that the stretch goals threaten people. Our people are accustomed to being dealt with on a very straightforward basis: *You* accomplish what you're supposed to accomplish, great; you don't accomplish what you're suppose to accomplish, you're out. I've got to tell you, this approach doesn't work. You must keep that responsibility ethic, but at the same time you need to let people know that if they have a stretch goal and they don't achieve it, they won't be thrown out.

We are trying to integrate a lot of things in the company right now. We're working with a new organization whose structure, including 11 separate business units, I would describe as an irregular electron cloud. We used to be a detailed and beautifully aligned functional organization. We had one set of people dealing with the upstream business. We had other people involved in the downstream business. And we had a chemical business.

But that model had problems. For instance, it didn't work well in the developing world, because you end up with three presidents of three different Mobil companies in each country. These countries' representatives want to deal with one person who represents Mobil, not three. So in most developing areas, we now have a geographic organization with one Mobil executive for the whole region.

In other areas that's not the case. In the United States, the upstream and downstream sides are completely separate, so we've kept them separate within Mobil. And we've gone to a worldwide structure with some businesses that we just couldn't pull apart in easy pieces.

We're still in the process of working this structure out, and it isn't easy. What I like about it is that it's giving a lot of our people more responsibility and more authority to do their work faster than they could have under the old structure. I also like the mixed experience it gives our managers. The first time I was responsible for both upstream and downstream parts of the business was when I became President of Mobil Corporation in 1993 – a little late in my career to be dealing with that kind of new experience. So we're restructuring our organization to reflect what's happening in the marketplace, but also to provide for our internal development needs.

Is the process going smoothly? I would have to say we're still in transition. It's a major adjustment for all of us. Some of our people are getting issues thrown at them that they haven't seen before. In the past, they didn't have to deal with some of the „nitty gritty" corporate issues. People could say, „Don't talk to me about whether we should supplement our retirees' pensions, I'm busy building service stations and refineries."

But if you look at the skills you want in your leadership team, it's clear we have to expose emerging managers to corporate affairs. Those of you who lived through the *Exxon Valdez* spill and are looking at today's tobacco settlement know what I mean. These days, the success of large, complex organizations like ours depends on our ability to deal not only with functional and geographical issues, but also with a full range of corporate issues.

Another challenge we're confronting is the need to balance growth and performance. Our business is capital intensive. We spend roughly $5-$6 billion a year on new projects, and our capital base is around $27 billion. Projects that we take on are big and complex, and they take years to reach payout. So some of the things we spend money on today won't have an impact on the company for another five to seven years. In the meantime, we must keep making money for the shareholders and the business, and we must get more out of our existing assets.

In the end, it always comes down to people. That's an area in which we haven't performed brilliantly in the past and aren't performing brilliantly today. Mobil has gone from a maximum of almost 80,000 people – not including Montgomery Ward and Container Corporation – to about 40,000. That's not many people left. Along the way, we've had to worry about a whole gamut of issues. In the process of shrinking our workforce, we took our eye off of getting new people. Our recruiting numbers went way off, and we realized we were jeopardizing the future of the company. We've corrected this, and now have a balanced approach again.

In addition to getting people in from schools, we'd like to attract them from other companies – something unusual in our industry. In the past, the oil industry generally grew its own leaders. You didn't go out and get somebody else's. In recent years, however, we've hired three or four high-level, experienced people, and I think this has opened the eyes of most of my people to the benefits of doing that.

Mobil has never been good at training, though we've spent large amounts of money on it. But if we don't learn to do this well, if we don't give our employees the feeling that being with Mobil will benefit them and their careers, they won't stay. They have to be convinced that they will be better and more valuable in the marketplace because they have worked for us – whether they're with us from cradle to grave or only for a certain number of years. So the process of training people to be better on the job will be more and more important as we go forward.

Compensation systems also will be key. In the United States, we're now all on a salary-at-risk basis. As long as things go well, everyone is happy. But the time will probably come when things aren't going well, and then there's going to be grief. But if you aren't willing to stand firm during the bad times, as well as give out the good news when times are good, you're not doing your job for the shareholders or your management.

Other key issues for us are diversity and internationalization. Diversity speaks for itself in the United States. Notwithstanding certain recent news stories, most companies are really quite good in terms of numbers. That is, if you follow the simple representation rules, most companies look great. But, frankly, that's not the issue. The issue is, how do you get the most out of people? When you are down to a bare minimum of employees, you've got to make sure that everybody comes to the table ready to fight, using all their assets – independent of color, race, creed, religion, or sexual orientation.

An organization's culture should not create obstacles to performance. If one of my people has to set aside 50 percent of his or her talents because they don't think these fit the company, I'm lost. It's not a question of winning awards from *Fortune* or the Clinton White House. It's a question of performance. To get that, you've got to eliminate the obstacles. Everybody's got to feel that this is their hardware store and be willing to put all their skills and talents on the table. That's your only hope.

Internationalization is even tougher. We have a hierarchical structure in our affiliates in most countries – with one general manager and a staff. I've spent 21 of my Mobil years outside the United States. Never once in those years did it cross my mind that I'd have a problem getting a job back home, provided I performed well. That's because there are always high-level jobs in the United States. But imagine the case for an Italian, or a Thai, or a Singaporean, who, as a Mobil employee, may already have the company's top job in that country. If they leave to take on an international assignment, they go off into an abyss, since it's not obvious to that person how they're going to get back home. If that had been the situation for me 20 years ago when I took assignments in Japan, Saudi Arabia, and Italy, I'm not sure I would have taken them.

So we have another set of problems to overcome. We need to be smart enough to run large, worldwide functions outside the United States. In the past, we haven't done this as well as we should have. We haven't taken advantage of the richness of experience and cultural breadth throughout our organization, which does business in more than 125 countries. It's something we're now trying to do much better.

I think another key to success over the next five to ten years in my business will be the ability to do projects and ventures with others. I think the days are over when we could live within the limits of our own companies, in our own cocoons. As you know, Mobil has joined forces with British Petroleum (BP) in Europe. Let me tell you, that was an emotional decision. We had worked hard in Europe to get better. We reduced our manpower by almost 40 percent. We installed common systems. We closed or sold six refineries that were surplus capacity. We did a lot of things right and had finally started to make some money in Europe. But we were making only about a 5 percent return, which doesn't attract growth capital.

Our people in Europe concluded that we couldn't make it on our own. BP went through the same process. Our two major competitors in Europe, Exxon and Shell, have about a 12 percent market share in gasoline and lubricating oils. We had a 4-5 percent share, and BP had about a 7 percent share. So our folks put together a deal. The only thing BP's John Browne and I did was act as cheerleaders. We met only three times in the process, including at the press conference announcing the deal. Otherwise we kept out of it.

As it turned out, combining our assets was the easy part, compared to combining our two corporate cultures into a successful marriage. That's the tough part. For one thing, you have to put your corporate ego on the shelf. The one thing John Browne and I told our respective organizations is that we will not tolerate corporate ego getting in the way of the success of this joint venture. We will not have anybody spending time measuring how many square inches of Mobil's logo you see relative to how many square inches of BP's logo.

Our organizations have worked brilliantly together, creating two joint ventures – a fuels operation run by BP and a lubes operation run by Mobil. The fact that each company heads one of the two parts of the joint venture has facilitated its success. We both feel we have a win-win venture.

You're going to see more of this in the States and more of it worldwide. And it is not going to be a numbers game. It's going to be based on the premise that there are people in this world who do things better than we do. By the same token, there will be more of this thing we call „outsourcing" – hiring others to do certain jobs when it works to your benefit. For instance, Mobil used to run a credit-card processing center in Kansas City. We benchmarked that credit-card center every year against every other oil company credit-card center, and we always ranked among the top quartile. The only trouble is, we didn't benchmark ourselves against companies who do this as a business. When you do something ten times a day and the other guy does it a million times, if he has any kind of sense, he's going to beat the hell out of you. So Mobil is no longer processing credit-card information.

I suspect we'll find a series of activities like this where we cannot be competitive by doing that activity ourselves. If we can't be competitive, we can't attract the best people. If we can't attract the best people, we ought to get out of that activity and start buying those services from somebody else. Of course, that raises the question of how you keep enough skill and technology in these areas to manage the interfaces, and that definitely will be a challenge.

A final area in which we're going to have to do better – and I think Mobil has a good leg up here – is in partnering with governments and national oil companies as opposed to the old „seven sisters." Most countries that are opening up today have more direct control over their own natural resources, so we'll be working with them more and more. Working with governments on a day-to-day basis can be tough. Mobil has done this all over the world. We've learned our lessons, and I believe we have an edge here. We've got more experience relative to our size than any other company. Today Mobil is viewed as an attractive joint-venture partner, and we should be able to continue doing this better than our competitors.

These are some of the things that will be important as we head into the future. They're what will differentiate the winners from the losers in our business. But, at the end of the day, what separates platitudes and preaching from success and performance? Two things: commitment and passion. You've got to love what you do. You've got to be in it. And if you don't feel for it, you should get out and do something else. I started with Mobil 36 years ago, and it seems like yesterday. Time goes by quickly. If you aren't spending it on things that really turn you on, you should find something that does. I get criticized a lot within Mobil because that's what I tell my people. If you're not willing to play, if you're not willing to feel that this is your hardware store, then find a new career. A lot of people find that harsh. But I think it's good advice for living.

Even better advice is, give short speeches – something I'm not very good at. So I'll stop here and say thank you for the opportunity to be with you.

Lucio A. Noto is Chairman of the Board and Chief Executive Officer of Mobil Corporation. In addition, Mr. Noto serves as Chairman of the Executive Committee of Mobil Corporation and Mobil Oil Corporation. His lifelong career at Mobil has spanned the world. He has had significant international experience as President of Mobil Sekiyu and Mobil Oil Italiana and has played a key role in growing Mobiles business in Saudi Arabia, where the company has established a preeminent position in refining, petrochemicals, and lubricants. Mr. Noto is a Director of International Business Machines Corporation and a member of the American Petroleum Instituted Public Policy Committee, the Business Council, the Council on Foreign Relations, and the Business Roundtable.