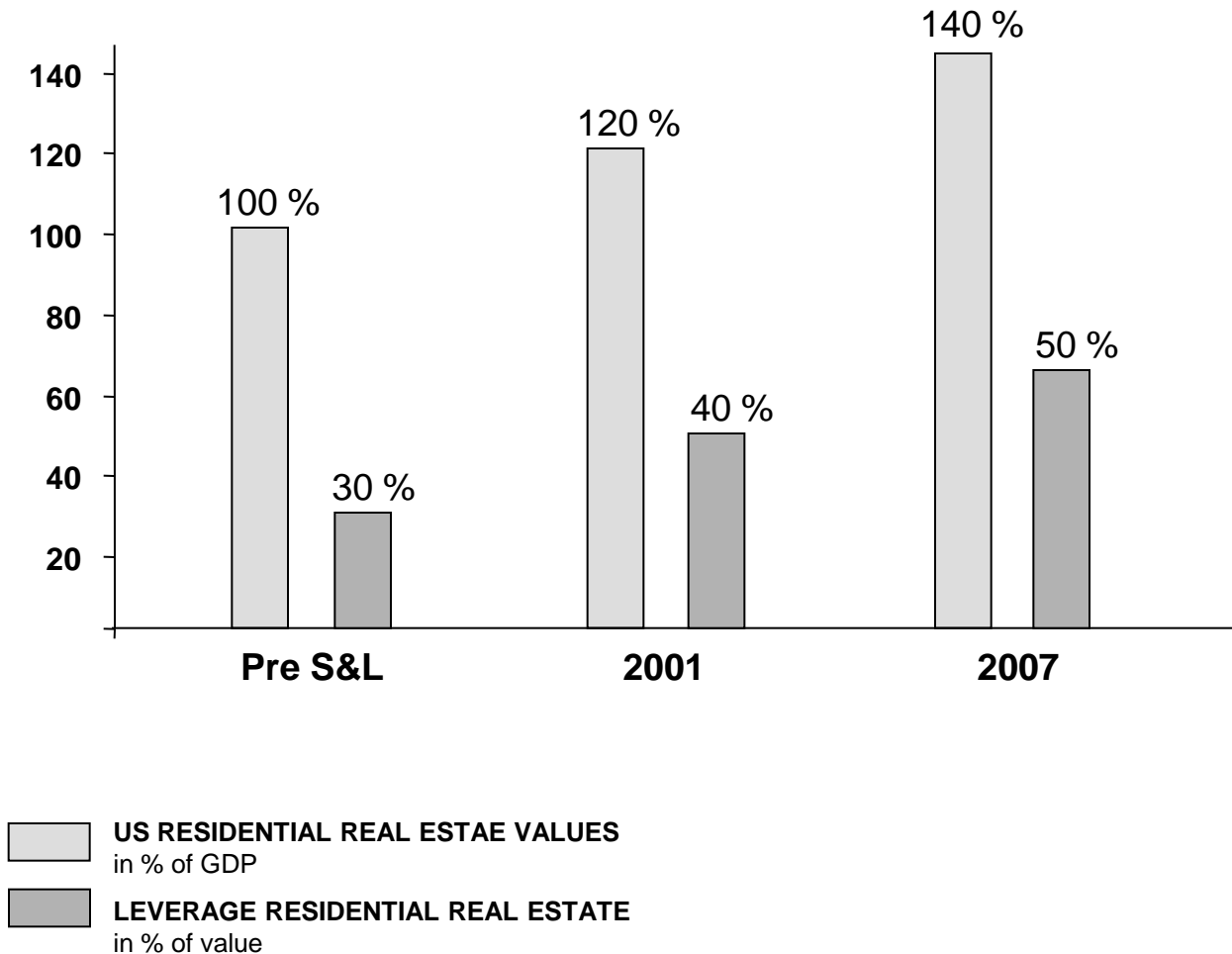


Managing uncertainty: handling the economic crisis

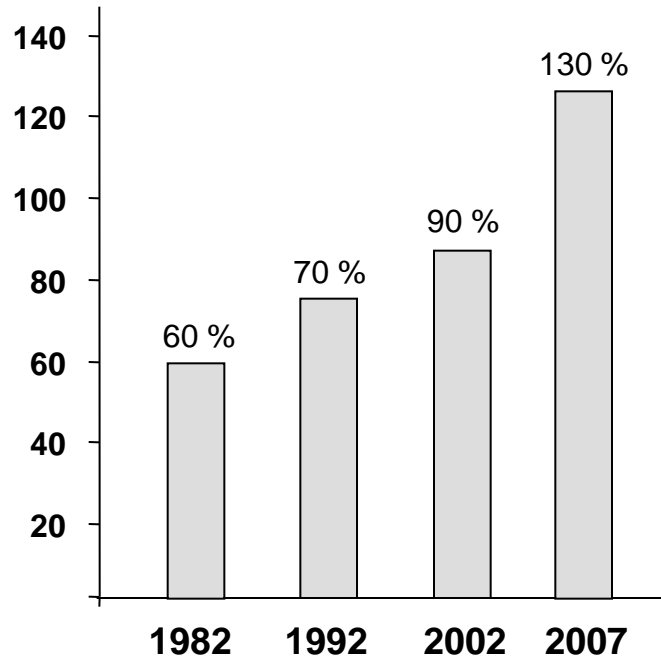
Dirk Schneider, D'92
Darden Roundtable
Frankfurt, March 21, 2009


- **Uncertainty about course of recession**
- Uncertainty about subsequent recovery
- Four directional scenarios
- Non-regret moves

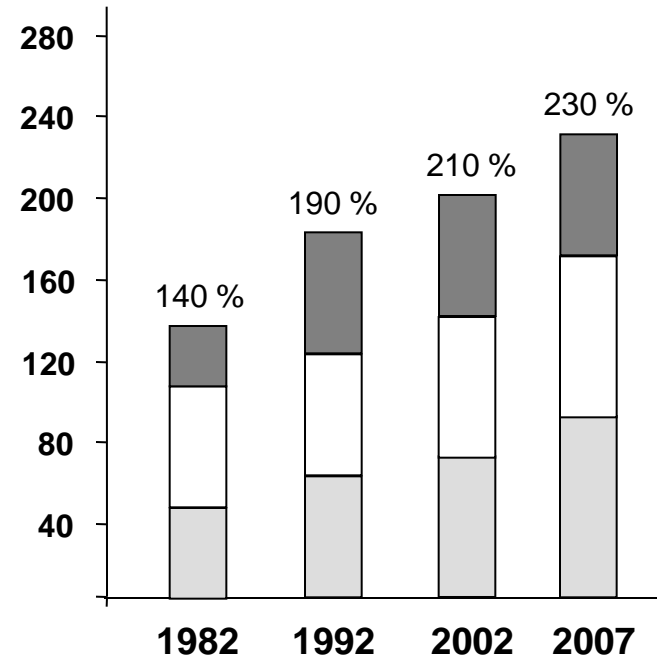
Excessive real estate valuations and leverage in the US triggered recession



High leverage across all sectors worsened impact

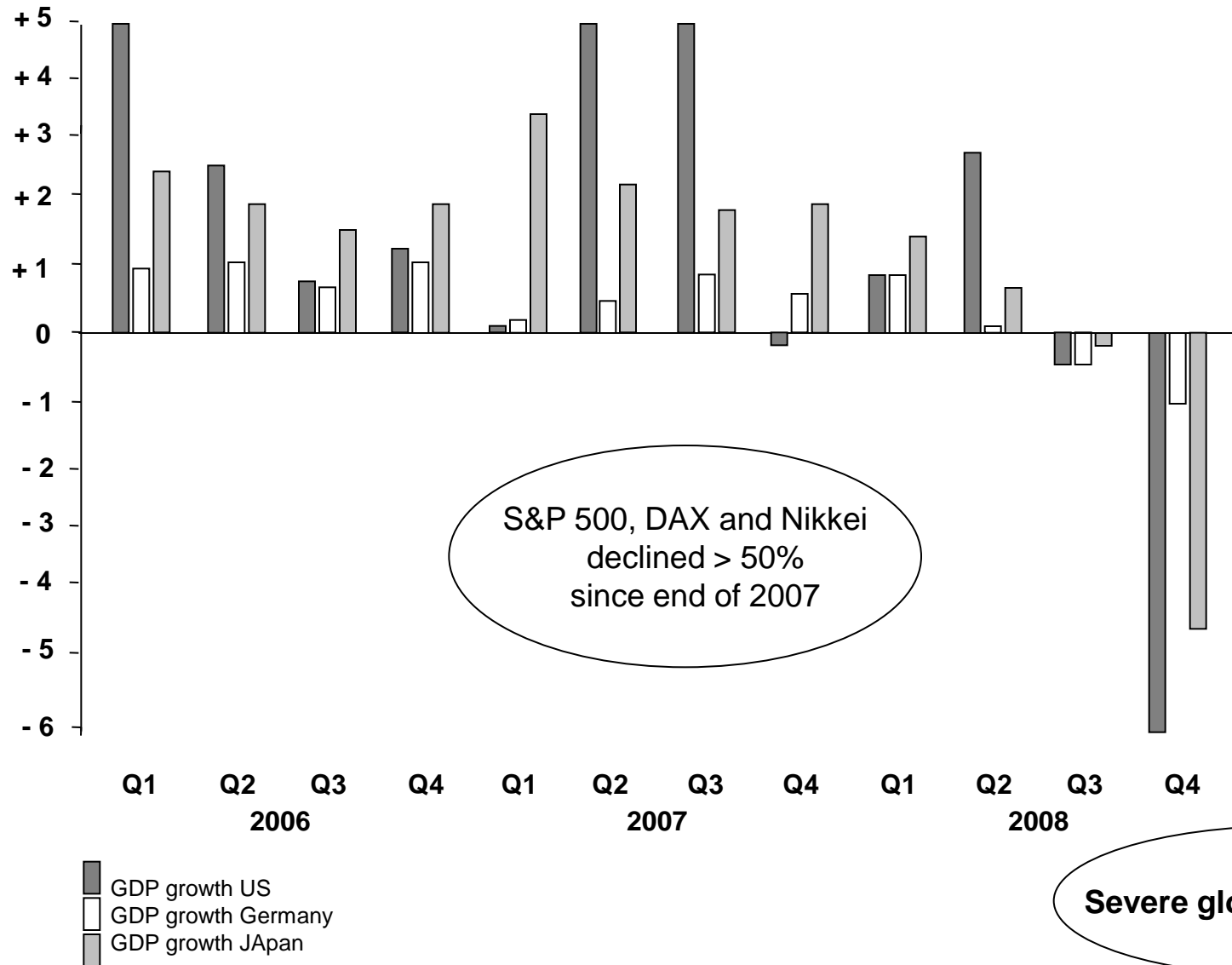


 **US CONSUMER DEBT**
in % of disposable income



 **US CONSUMER DEBT**
 **US BUSINESS DEBT**
 **US GOVERNMENT DEBT**
in % of GDP

Major economies have been shrinking since Q3 2008



Governments and central banks in sync to fight recession

Coordinated central banks initiatives

- Lower interest rates
- Increased liquidity

Similar Government actions world-wide

- Broad guarantees for financial institutions
- Selected support for industrial companies
- Significant direct investment programs

FED effectively acting as “bad bank”

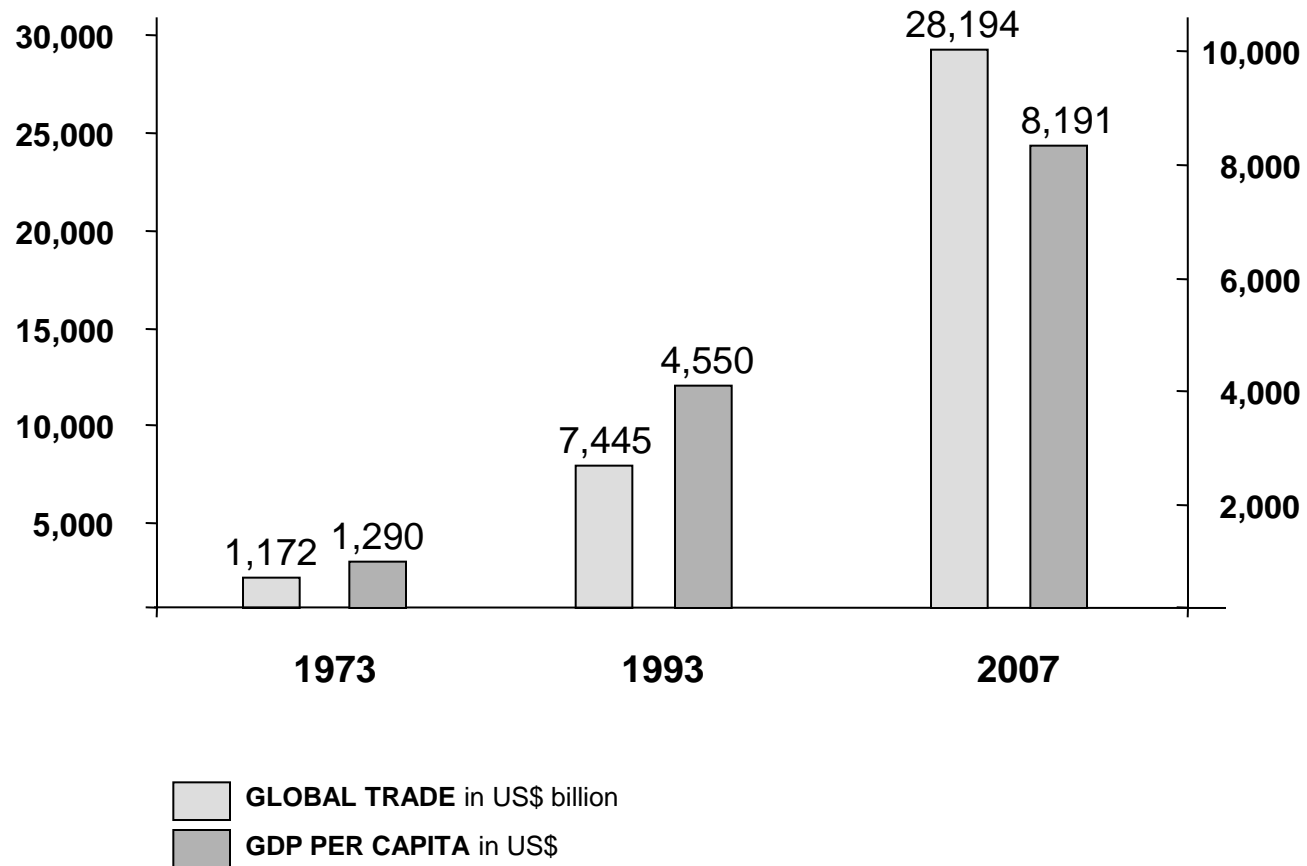
**Fast stabilization ?
Early recovery ?**

The first big uncertainty ...

**The recession:
how long and how deep?**

- Uncertainty about course of recession
- **Uncertainty about subsequent recovery**
- Four directional scenarios
- Non-regret moves

Free trade critical for strong global GDP growth



Increased protectionism in most legislations

Europe

- Governments direct Fortis, SEB and Royal Bank of Scotland to refocus on domestic clients
- Germany, France and Spain set up funds to support domestic industries
- France considers limiting Government support to French production sites in France only
- EU discusses re-introduction of export subsidiaries for selected agricultural products

BRIC

- Russia, Brazil and Argentina increased tariffs on vehicles
- India increased tariffs on iron and steel products
- China manages Fx-rate downwards

Northern America

- “Buy American” legislation in US

**Higher cost of capital ?
More fragmented supply chains ?
Reduced economic performance ?**

Limited post-recession options to reduce Government debt

Outgrowing debt

- Economies return to strong growth
- Absolute debt levels kept constant
- Taxation, spending and inflation remain within historical limits

**Robust growth ?
Stable environment ?**

Consolidating debt

- Economies return to modest growth
- Higher taxation and reduced spending
- Stabilized growth on low level

**Low growth ?
Stable environment ?**

Inflating debt away

- Economies return to modest growth
- “Fresh” central bank money to reduce debt
- Higher nominal growth; high inflation

**Reasonable growth ?
Risk of new bubbles ?**

Defaulting on debt

- Economies return to modest or no growth
- Insufficient tax increases and spending cuts
- Bankruptcy of at least some states

**Low growth ?
Continued uncertainty ?**

The second big uncertainty ...

The recovery:

how strong?

- Uncertainty about course of recession
- Uncertainty about subsequent recovery
- **Four directional scenarios**
- Non-regret moves

Four directional scenarios

- benign regulation
- open markets
- strong economies

Post-recession regime

- protectionism
- high inflation

<p>“Delayed Recovery”</p> <ul style="list-style-type: none"> • Recession continues for several years • Low confidence and promising outlook lead to bumpy recovery • Eventually economies return to pre-recession strength 	<p>“Pleasant Surprise”</p> <ul style="list-style-type: none"> • Markets bottom out quickly • Returning confidence and promising outlook lead to strong recovery • Economies return to pre-recession strength quickly
<p>“Lost Decade”</p> <ul style="list-style-type: none"> • Recession develops into depression • Overall confidence remains low • Economies stabilize and remain at depression levels 	<p>“Incomplete Recovery”</p> <ul style="list-style-type: none"> • Markets bottom out quickly • Players adjust to new regime • Economies stabilize and recover to level well below pre-recession

With limited impact

stabilize markets quickly

Central banks and governments

Implications of „Pleasant Surprise“

Economic scenario

- Financial and goods markets normalize quickly
- Emerging regulatory framework globally coordinated and efficient
- Financial and goods markets remain open
- Debt reduction through growth and consolidation
- Recovery starts 2nd half 2009
- Pre-recession economic performance reached 2011 / 2012

Strategic implications

- Manage liquidity with foresight
- Upgrade organizational capabilities
 - Eliminate barriers to fast decision making
 - Streamline operational processes
 - Focus R&D and new business development
 - Adjust low performing segment of work force
- Capture opportunities to strengthen competitive position
 - Targeted marketing campaigns to increase market share
 - Selected acquisitions

Implications of „Incomplete Recovery“

Economic scenario

- Financial and goods markets normalize quickly
- Emerging regulatory frameworks become increasingly nationalistic and restrictive
- Protectionism replaces globalization
- Debt reduction through consolidation and inflation
- Recessions bottoms out 2009 / 2010
- Economic performance stabilizes significantly below pre-recession levels in 2011 / 2012

Strategic implications

- Manage liquidity with foresight
- Focus on core strength
 - Business unit portfolio
 - Geographic coverage
- Review existing supply chains
 - Cross-border issues
 - Credit / financing risks
- Streamline organization and adjust resources
- Capture growth opportunities very selectively
 - Market share in core areas
 - Acquisitions close to existing businesses

Implications of „Delayed Recovery“

Economic scenario

- Financial and goods markets normalize only after sustained period of uncertainty
- Emerging regulatory framework globally coordinated and efficient
- Financial and goods markets remain open
- Debt reduction through consolidation and (limited) inflation
- Recessions bottoms out 2011 / 2012
- Pre-recession economic performance reached 2013 / 2014

Strategic implications

- Align liquidity and business needs
- Strengthen core businesses
- Upgrade organizational capabilities
 - Eliminate barriers to fast decision making
 - Streamline operational processes
 - Focus R&D and new business development
 - Reduce number of low performer
- Capture opportunities to strengthen competitive position
 - Targeted marketing campaigns to increase market share
 - Selected acquisitions

Implications of „Lost Decade“

Economic scenario

- Financial and goods markets fail to normalize
- Emerging regulatory frameworks become increasingly nationalistic and restrictive
- Protectionism replaces globalization
- Debt reduction through (hyper)inflation and Government defaults
- Recessions bottoms out 2010 / 2011
- Several “false” recoveries
- Pre-recession economic performance only reached between 2015 and 2020

Strategic implications

- Align liquidity and business needs
- Focus on core strength
 - Business unit portfolio
 - Geographic coverage
- Review existing supply chains
 - Cross-border issues
 - Credit / financing risks
- Streamline organization and adjust resources
- Capture growth opportunities very selectively
 - Market share in core areas
 - Acquisitions close to existing businesses

- Uncertainty about course of recession
- Uncertainty about subsequent recovery
- Four directional scenarios
- **Non-regret moves**

Focus on cash

Optimize liquidity

- Shift focus from profitability on cash-flow
- Shorten review periods for liquidity situation
- Review legal / geographic locations of cash-pools
- Review inventories / working capital

Secure funding

- Intensity relationship with few “house-banks”
- Assess draw-down of credit lines – even if not immediately needed
- Identify additional short-term sources of funding

Minimize cash-out

- Focus on cost reductions with immediate cash effect
- Review capital expenditures
- Focus R&D and business development on strategically most relevant activities
- Avoid long-term commitments

Upgrade organizational capabilities

Speed up decision making

- Streamline internal approval / consulting requirements
- Eliminate intrinsic bottle necks
- Rebalance central vs. de-central decision making

Streamline processes

- No across the board cuts! No elimination of capabilities required post-recession!
- Systematic reviews with focus on improvement implementation
- Focus on upgrading internal talent

Focus R&D and bus. development

- No across the board cuts!
- Systematic and transparent project / portfolio
- Consequent project termination and redeployment of resources

Capture M&A opportunities

- Core areas sustainable even in prolonged down-turn
- Competitors, suppliers, entries in new geographies
- Distressed situations and fire sale

Develop action plans for different scenarios

“Pleasant surprise”

“Delayed recovery”

**“Incomplete
recovery”**

“Lost decade”

For all scenarios:

- Impact on markets and business units
- Tailored financial projections
- Budgets and resource plans
- Transition schedule to actual scenario
- Detailed operational action-plans with responsibilities and timelines

Systematic monitoring of crisis
to identify real scenario (or mix)
as quickly as possible

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