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# REPORT

THE 2008 VALUE CREATORS REPORT

## Missing Link

Focusing Corporate Strategy on Value Creation



THE BOSTON CONSULTING GROUP

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September 2008

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The financial analyses in this report are based on public data and forecasts that have not been verified by BCG and on assumptions that are subject to uncertainty and change. The analyses are intended only for general comparisons across companies and industries, and should not be used to support any individual investment decision.

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# Note to the Reader

This publication is the tenth annual report in the Value Creators series published by The Boston Consulting Group. Each year, we publish detailed empirical rankings of the stock market performance of the world's top value creators, distill managerial lessons from their success, highlight key trends in the global economy and world capital markets, and share our latest analytical tools and client experiences to help companies better manage value creation.

This year's report addresses the challenges of value creation in a time of turbulence and uncertainty in the global economy. It also provides a comprehensive perspective on corporate strategy that integrates the traditional focus on business strategy with a new strategic focus on a company's financial policies and investors' priorities and goals.

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# Executive Summary

**I**t is a time of turbulence in the global economy. Macroeconomic, political, regulatory, and technological changes are roiling the business environment. As a result, many companies confront uncertainty and change.

- ◇ No one knows for sure how far the global financial crisis will reach or whether the world economy will suffer a recession
- ◇ It is unclear what the full economic impact of rising energy prices will be
- ◇ Many companies face the rise of a new class of global competitors from rapidly developing economies that will reshape the competitive dynamics of their industries

**Increased turbulence is taking place against the backdrop of a major discontinuity in capital markets.**

- ◇ The days of consistent high returns in the neighborhood of 15 percent per year, which characterized the 1980s and 1990s, are likely gone for the foreseeable future
- ◇ Most analysts see future returns more in line with the long-term historical average of approximately 8 to 10 percent per year—or even less
- ◇ It is becoming considerably more difficult to deliver the kinds of returns that executives and shareholders have come to expect

**To create superior shareholder value today, companies need to take a fresh look at corporate strategy.**

- ◇ In theory, a company's corporate strategy should provide a detailed road map for how the company's organizational capabilities, financial resources, and business-unit competitive advantages can create superior value for investors
- ◇ In practice, however, corporate strategy as it takes place at most companies fails to deliver on this mission because it is not grounded in a detailed consideration of how the company actually generates value
- ◇ As a result, there is a pervasive disconnect at many companies between corporate strategy and value creation; this is the missing link in the corporate strategy process

**Value creation must become a more central and explicit part of the corporate strategy process.**

- ◇ Maximizing shareholder value is not necessarily the only—or even always the most important—goal of corporate strategy; but there is a symbiotic relationship between corporate strategy and value creation
- ◇ No public company can afford to ignore the capital markets and the ways in which investors value the company's stock
- ◇ Senior executives need to understand precisely how their corporate strategy will create value and anticipate the likely reactions of investors to their strategic moves

**This year's Value Creators report focuses on strengthening the link between corporate strategy and value creation.**

- ◇ We argue that setting an explicit target for total shareholder return (TSR) needs to become a central part of the corporate strategy process
- ◇ We offer a broader and more comprehensive approach to corporate strategy that supplements the traditional focus on business and portfolio strategy with a new focus on a company's financial policies and investors' priorities and goals
- ◇ We describe a three-step process for implementing this more comprehensive approach to defining a company's corporate strategy
- ◇ We conclude with extensive rankings of the top value creators worldwide for the five-year period from 2003 through 2007





# Creating Value in Turbulent Times

**W**hen we began the Value Creators series, in 1999, global capital markets had enjoyed nearly two decades of relative stability. Little did we know that we were at the beginning of a period of unprecedented turbulence in the world economy: from the Internet boom to its subsequent bust, from the attacks on 9/11 to the downturn that followed, from the recovery to the current crisis in financial markets. Turbulence is no longer the exception; it has become the rule. Fasten your seatbelts, because it is likely to continue.

## Forces of Uncertainty

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There are many forces contributing to uncertainty and turbulence in today's economy. Some are macroeconomic. It is still unclear, for example, how far the current global financial crisis will spread or how long it will last; whether the global economy will tip over into recession (and, if so, for how long); and what the long-term economic impact of rapidly rising energy prices will be on company business models.

Other forces of turbulence are political and regulatory. Who wins the U.S. presidential election in November 2008, for example, will have enormous (and, for the moment, hard-to-predict) implications for free trade and the global economy. There are signs that central banks are turning away from more than two decades of relatively lenient monetary policies that have fueled easily available debt and spurred booms in the stock market, the housing market, and, some would argue, commodities. The long trend toward economic deregulation also seems to have finally run its course, but there is little indication of what the new forms of

government regulation will look like. And looming in the background is the long-term economic impact of terrorism.

Still other forces of uncertainty are more industry- or even company-specific. In some industries, rapid consolidation is forcing companies to consider multiple scenarios for the endgame and choose what role they want to play. In others, the rise of rapidly developing economies, such as China, India, and Brazil, is creating new competitors and more complex competitive dynamics.<sup>1</sup> And even in more stable industries, many companies face uncertainty and turbulence simply owing to the fact that their existing portfolio of businesses is maturing, requiring the development of new business models and new platforms for growth.

Finally, all these uncertainties are taking place against the backdrop of a major discontinuity in capital markets. The glory days of 15 percent average annual returns that characterized the final decades of the twentieth century may well be over. Most market analysts are predicting far more modest future returns, somewhere in the neighborhood of 8 to 10 percent—or even lower.<sup>2</sup> And in many industries, companies are generating far more cash than they can profitably invest, given the underlying growth rates in their existing businesses and markets, fueling concerns among investors that those companies

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1. See *The 2008 BCG 100 New Global Challengers: How Top Companies from Rapidly Developing Economies Are Changing the World*, BCG report, December 2007.

2. For example, one survey of 100 CFOs at *Fortune* 1000 companies reported that participants expect equities to deliver an average annual return of only 6.6 percent through 2011. See "CFO Survey 2006: Sometimes the Little Details Do Matter," Morgan Stanley, September 28, 2006.

will use their excess cash in ways that end up destroying shareholder value.<sup>3</sup>

Not every company will have to grapple with all these forces. But most will face at least some of them; and relatively few will encounter none at all. It's important to keep in mind, however, that while turbulence presents major challenges, it also creates opportunities.<sup>4</sup> For that reason, effectively navigating turbulence will be the key to superior value creation in the years to come.

## Corporate Strategy Revisited

How does a company skillfully navigate the turbulence? By revisiting its corporate strategy—and, in particular, the relationship of that strategy to value creation. Corporate

strategy and value creation exist in a symbiotic relationship. A company's corporate strategy defines its key areas of competitive advantage and how it will exploit those advantages to create value for investors.

But the energy flows in the opposite direction as well. Superior value creation is an important foundation for

3. For a fuller treatment of this subject, see *Avoiding the Cash Trap: The Challenge of Value Creation When Profits Are High*, The 2007 Value Creators Report, September 2007.

4. For insightful discussions of the challenges of turbulence in today's economy, see "Driving Success in Turbulent Economic Times," BCG Perspectives, June 2008; and Hans-Paul Bürkner, foreword to *Seeing What Is Not—Yet: What Poetry Brings to Business*, The Boston Consulting Group, December 2007, pp. iv–vi. This publication is an excerpt from a forthcoming book to be published by the University of Michigan Press.

## The BCG Value Creators Report: The First Ten Years

BCG began publishing the Value Creators report in 1999 because we wanted to share with our clients and the corporate community what we were learning from our work during the value management revolution of the 1990s. We also thought it would be useful to publish annual rankings of the best global performers, which companies could use to benchmark their own performance.

The main insight of value management was to put improvements in fundamental value—represented by the discounted value of the future cash flows of a business—at the core of value creation. According to this perspective, capital markets are efficient over the long term, and therefore improvements in fundamental value eventually translate into improvements in a company's stock-market value. More than two decades of research in corporate finance have shown that fundamental value does generally drive a company's TSR over the long term.

In 1991, BCG acquired the corporate consulting business of Holt Value Associates, a widely recognized innovator in quantifying fundamental value. Over the next decade, we refined and extended Holt's proprietary methodology and worked with hundreds of clients around the world to implement value management systems, making BCG a leader in the field. In early Value Creators reports, we introduced our model for increasing fundamental value through improvements in cash flow margin and asset productivity, and through profitable growth in invested capital.<sup>1</sup> We also described the key cash-based metrics that we recommend for managing fundamental value, including TSR, cash flow

return on investment (CFROI), cash value added (CVA), and total business return (TBR)—metrics that are now used widely in the corporate and financial world.<sup>2</sup>

But soon after we started publishing our annual Value Creators report, we began to realize the importance of investor expectations for a company's near-term valuation. Although improvements in fundamental value drive TSR in the long term, investor expectations (as reflected in a company's valuation multiple) often have a major impact in the short to medium term. What's more, these expectations can influence the choices a company makes about tradeoffs among growth, profitability, and paying out cash to shareholders. So subsequent reports emphasized these expectations as a potential enabler of—or constraint on—a company's value-creation strategy.<sup>3</sup> We developed techniques for measuring a company's *expectation premium* (that is, the difference between a company's actual stock price and the price derived from an analysis of the company's underlying fundamentals). And we examined how operational factors—such as market leadership, branding, intellectual property rights, management

1. See, for example, *The Value Creators: A Study of the World's Top Performers*, The 1999 Value Creators Report, December 1999.

2. Several leading investment banks now use versions of this CFROI methodology to assess investment opportunities. See, for example, *CFROI Valuation Report*, Credit Suisse First Boston, July 5, 2002.

3. See, for example, *Dealing with Investors' Expectations: A Global Study of Company Valuations and Their Strategic Implications*, The 2001 Value Creators Report, September 2001.

future competitive advantage. Not only does it reward investors, it also solidifies their support for management's long-term agenda. What's more, above average value creation delivers cheaper debt and equity currency for key growth or consolidation moves, makes available additional resources to invest in better serving customers, and helps attract the best people through the provision of attractive stock options. Particularly in times of uncertainty, it's important to be confident that this circle is a virtuous, not a vicious, one.

That's why we have focused this year's Value Creators report on corporate strategy. (To understand how this year's report builds on previous reports, see the sidebar "The BCG Value Creators Report: The First Ten Years.") We believe that the necessary connection between cor-

porate strategy and value creation is a missing link in many companies' corporate-strategy process today. Establishing that link doesn't necessarily mean privileging shareholder value creation over all other strategic goals (let alone always maximizing shareholder value in the short term). But it does mean understanding how a company's strategy actually generates value and how capital markets monetize it.

In this year's report, we introduce a broader approach to corporate strategy than companies typically employ today. It's an approach that puts value creation at the center of the corporate strategy process—supplementing the traditional focus on business strategy with a new strategic focus on a company's financial policies and investors' priorities and goals.

credibility, and governance transparency—can help companies sustain a high expectation premium over time.

By the midpoint of the current decade, we began to focus on incorporating these insights about investor expectations into a truly integrated approach to value creation—that is, one that combines the traditional focus on fundamental value with new techniques and methodologies for understanding and managing investor expectations and other dynamics inherent to the capital markets.<sup>4</sup> We argued that superior value creation depends on understanding the dynamic linkages and managing the tradeoffs across three dimensions of a complex value-creation system:

- ◇ *Fundamental value*, the traditional focus of value management
- ◇ *Investor expectations*, defined as the differences between stock price and fundamental value, and reflected in a company's valuation multiple
- ◇ *Free cash flow* that is returned directly to investors in the form of debt repayment, share repurchases, or dividends

Drawing on research and analysis from the BCG ValueScience Center, we developed a methodology for *comparative multiple analysis* that allows a company to identify the operational and financial factors that drive valuation multiples in its peer group. And we introduced

techniques for identifying the dominant investor styles in a company's investor base and for creating alignment between a company's value-creation strategy and its dominant investors.

More recently, we have focused on how this integrated approach sheds fresh light on some classic (and yet timely) value-creation challenges. In 2006 we put a spotlight on growth, analyzing the role of growth in achieving superior value creation.<sup>5</sup> And in 2007 we addressed an especially important issue that many global companies face today: how to decide the best uses of cash when the amount of cash that companies are generating far outpaces the opportunities for profitable organic growth in their industries.<sup>6</sup>

This year, we take our analysis to a more strategic level in order to redefine corporate strategy in light of our integrated approach to value creation. We think this is especially important now, given the massive uncertainties in the world economy. These uncertainties make it imperative for companies to take a fresh look at corporate strategy and link it more explicitly to value creation.

4. See, for example, *The Next Frontier: Building an Integrated Strategy for Value Creation*, The 2004 Value Creators Report, December 2004; and *Balancing Act: Implementing an Integrated Strategy for Value Creation*, The 2005 Value Creators Report, November 2005.

5. See *Spotlight on Growth: The Role of Growth in Achieving Superior Value Creation*, The 2006 Value Creators Report, September 2006.

6. See *Avoiding the Cash Trap: The Challenge of Value Creation When Profits Are High*, The 2007 Value Creators Report, September 2007.



# Focusing Corporate Strategy on Value Creation

In theory, corporate strategy should define how a company will use its organizational capabilities, financial resources, and business unit competitive advantages to create superior value for its investors. But in practice, what passes for corporate strategy at most companies does not achieve this goal because it does not include a detailed consideration of how the company actually generates value. Senior executives need to use a more comprehensive and more integrated approach.

## The Logic—and Limits—of Traditional Corporate Strategy

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Every business needs its own individual business strategy—that is, a plan to create and exploit sustainable competitive advantage. The role of corporate strategy, however, is to define pathways for a company to generate value in excess of that which its business units would create on their own and to make sure the company's portfolio sustains that superior shareholder value over time.

Ideally, a company's corporate strategy defines the fundamental logic that explains why a particular set of businesses are together in the first place. For example, it should identify the parenting advantages or financial and operational synergies that make the company the best owner of its particular set of businesses. And it should define the precise role of each business unit in the company's overall value-creation strategy.

Corporate strategy is also responsible for making sure that a company's portfolio of businesses evolves over time. Some businesses inevitably mature and may no longer be able to create value at a level that matches the company's aspirations. A company needs to weed out those that are

no longer creating enough value under its ownership and develop or acquire new businesses with greater value-creation potential because they offer operational, financial, or parenting advantages that can be captured.

Finally, corporate strategy is the process by which senior management sets the financial policies and determines investor communications that will optimize the value a company realizes from its businesses. What is the ideal capital structure for the company? How much of the company's cash flow will be reinvested in the businesses and how much returned to investors in the form of dividends or share repurchases? How will reinvested capital be allocated among the various business units? And how will the company ensure that the capital markets value its portfolio of businesses appropriately?

That's the theory. Unfortunately, corporate strategy as it is actually practiced at most companies rarely performs all these tasks effectively. In our experience, the corporate strategy process at most companies typically suffers from the following four shortcomings:

- ◇ *Too Much Incrementalism.* A company's current business model—including its existing portfolio of businesses and financial policies—both frames and constrains the entire corporate-strategy process. Legacy assumptions remain unexamined. And although the process typically incorporates forecasts of trends in the company's current markets at the individual business-unit level, it rarely examines potential discontinuities in the external environment that could affect the company as a whole.
- ◇ *Sequential Planning.* Planning and decision making tend to flow in only one direction. Once the strategies

of the various business units are defined and specific financial targets are set, those choices then determine the parameters of a company's financial policies and the communications necessary to "sell" the strategy to investors.

- ◇ *"Siloed" Decision Making.* Because decision making is sequential, it also ends up being highly fragmented across different operational and functional silos. Corporate strategists work with business unit management to set business strategies. Corporate finance determines the financial policies (which may focus as much on important but tangential issues—for instance, tax optimization or the availability of short-term debt—as on the imperative to create shareholder value). Investor relations crafts investor communications. But each does its work in relative isolation. The final result is often the product of negotiation and legacy thinking rather than of an objective fact-based analysis of what it will take to create value.
- ◇ *Weak Connection to Value Creation.* The result of all these limitations is a pervasive disconnect between corporate strategy and value creation. Few companies have an explicit goal for shareholder value. And those that do rarely incorporate that goal explicitly in their planning process or quantify the potential TSR contribution of their business plans. As a result, value creation may be a desired outcome, but it is not an actual driver of strategy development.

Despite these shortcomings, the traditional approach to corporate strategy can sometimes be "good enough"—when a company's environment is stable, its businesses healthy, and its investors are more or less content with performance. In periods of uncertainty and change, however, "good enough" is anything but. Little wonder, then, that when BCG recently interviewed more than a hundred corporate strategists at large global companies, they complained about the insufficient quality and depth of strategic thinking in their organizations.<sup>5</sup> They considered most of the analytical tools in the field inadequate to deal with the many new issues and problems that companies are facing. And they were frustrated by a strategy process they found inefficient, formulaic, bureaucratic, and rarely successful at mobilizing the organization.

**Companies need to make value creation an integral part of the corporate strategy process.**

In today's environment, companies need a better approach. First, they need to make value creation an integral part of the corporate strategy process. Second, they need to extend the scope of corporate strategy to give equal consideration to the company's business strategy, its financial policies, and the priorities and goals of its investors. Finally, business strategy, financial strategy, and investor strategy need to be examined simultaneously (not sequentially) by the entire senior executive team (not isolated functional experts) in order to identify and reach agreement on critical tradeoffs. (Exhibit 1 on the following page contrasts the traditional approach to corporate strategy with this new approach.)

### **An Integrated Model of Value Creation**

Most senior-executive teams believe that they are already committed to increasing shareholder returns. After all, they talk about it all the time. Some may even have set a target for improvement in TSR. But in most cases, they are not really focused on value creation, because their corporate strategy process does not consider the full range of factors affecting TSR.

In recent Value Creators reports, BCG introduced an integrated model of value creation incorporating three critical dimensions. The first is improvements in fundamental value, represented by the discounted value of the future cash flows of a company's business based on its margins, asset productivity, growth, and cost of capital. The second is improvements in a company's valuation multiple, driven by investor expectations that shape how capital markets value a company's fundamental performance at any given moment in time. The third is direct payments to investors or debt holders in the form of dividends, share repurchases, or the paydown of debt. (See Exhibit 2 on the following page.)

The key point about this model is that these three dimensions exist in dynamic interaction. For example, a company may improve its fundamental value through profitable growth. But precisely *how* a company goes about achieving that growth can have either a positive or a negative impact on its valuation multiple and, therefore,

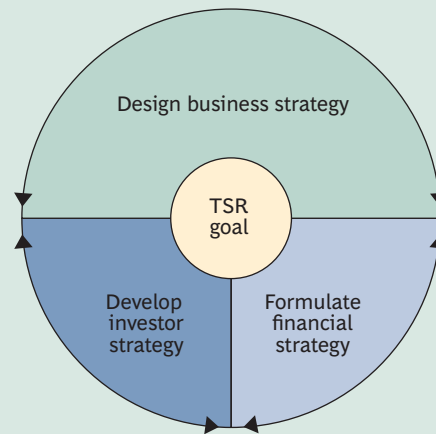
5. See "Does Your Strategy Need Stretching?" BCG Perspectives, February 2008.

## Exhibit 1. An Integrated Approach to Corporate Strategy Focuses on Value Creation

### Traditional Corporate-Strategy Process

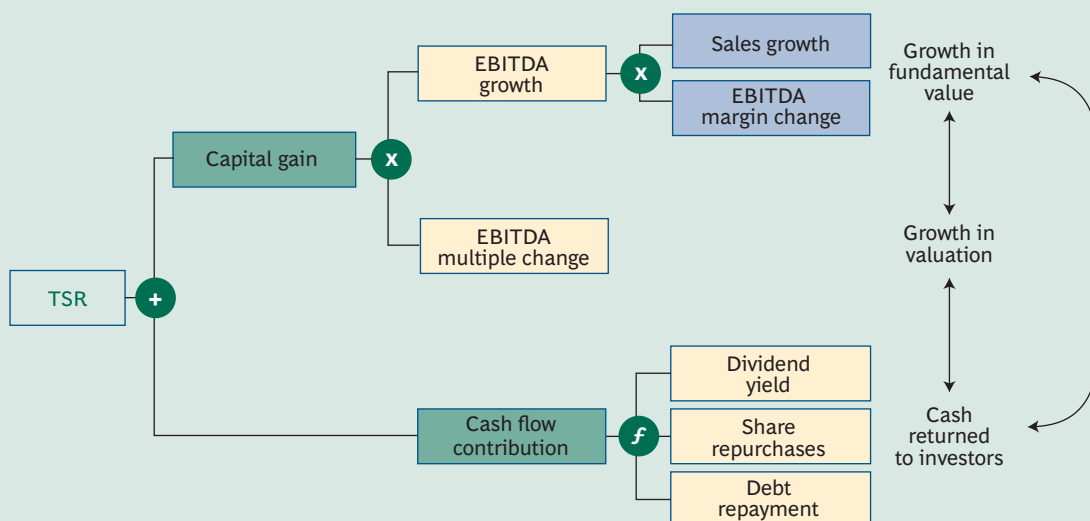


### Integrated Corporate-Strategy Process



Source: BCG analysis.

## Exhibit 2. Companies Must Understand the Linkages and Manage the Tradeoffs Across the Drivers of TSR



Source: BCG analysis.

on its TSR. Alternatively, the level of a company's multiple, compared with those of its peers, can enable certain business strategies and make others impossible. For instance, an especially strong multiple can make a company's stock a handy currency for acquisition; conversely, a weak multiple can make a company vulnerable to takeover. Finally, cash payouts not only can contribute directly to TSR but also can have a positive impact on a company's multiple by both strengthening the loyalty of existing investors and attracting new investors.

Unless a company has a corporate strategy process that takes these interactions and linkages into account and allows executives to manage the tradeoffs among them, it is not really focused on value creation. Its senior executives are unlikely to take full advantage of the company's value-creation potential, are more likely to make decisions that inadvertently destroy value, and may even find themselves vulnerable to pressure from activist investors. The way to avoid these negative outcomes is to make a company's financial policies and its investors' goals and priorities an integral part of the corporate strategy process.

## Business Strategy, Financial Strategy, and Investor Strategy

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A key aspect of our new approach is to see business strategy, financial strategy, and investor strategy as three equal parts of a company's corporate strategy and to treat them in parallel rather than sequentially. This integrated perspective is critical because both a company's financial policies and the goals and priorities of its dominant investors can have important implications for the company's business-unit strategies (and vice versa). They also can have a direct—and, sometimes, quite substantial—impact on TSR in their own right.

Financial strategy is the result of many different decisions about issues such as a company's capital structure, preferred credit rating, dividend policy, share repurchase plan, tax strategy, and hurdle rates for investment projects or mergers and acquisitions (M&A). Often these seem like discrete issues. But it takes a holistic approach to optimize a company's overall financial strategy.

For example, consider the impact of a business unit's proposed growth initiative. Business unit managers will naturally be focused on the initiative's return on invest-

ment—that is, whether it has a positive net present value (NPV). But even when a proposed growth initiative delivers returns above the cost of capital, a company may have been able to get even greater returns by, for instance, returning the cash to investors. Companies that are overleveraged, that are undervalued compared with their future plans, or that suffer from a low valuation multiple relative to peers can often realize major improvements in their valuation multiples and TSR by paying out more cash to investors or by using that cash to reduce debt. Put simply, every investment option needs to be considered *simultaneously* against alternative uses of capital. Unless senior executives integrate considerations of financial policy with considerations of business strategy, managing such tradeoffs is extremely difficult.

So too with a company's investor priorities. It's essential for a company's corporate strategy to be aligned with the priorities and expectations of its investors. Those expectations will drive the company's valuation multiple relative to its peers, which is the key source of short-term TSR and a critical influence on the company's long-term value creation.

One typical source of misalignment is the difference in how executives and investors assess business opportunities. Most managers evaluate the potential of a business initiative incrementally—that is, whether it adds to earnings per share (EPS) today or has a positive NPV, given reasonable assumptions about future cash flows and likely risks. But investors tend to focus not just on EPS or on standalone NPV but also on how a company's initiatives fit in with their view of its overall TSR profile.

For example, take a specific growth initiative that delivers returns above a company's cost of capital. If the returns are less than the average returns being earned by the business as a whole, they will erode the average and therefore may disappoint investors who expect the company to maintain its current level of returns. The result is a reduction in the company's valuation multiple. This is especially the case in today's environment, in which investors are sensitive to any indication that current high levels of profitability are being undermined by companies that are overinvesting in order to compete for limited growth opportunities.

Another source of misalignment is the different expectations of different types of investors. For example, value

investors tend to reward increasing the payout of free cash flow over growth. Growth-at-reasonable-price (GARP) investors, by contrast, favor stable, low-risk EPS growth. And growth investors target revenue growth greater than 15 percent. Unless a company's corporate strategy corresponds to the priorities of the specific groups that dominate its investor mix (or includes a detailed plan for migrating to a more compatible set of investors), it will not realize the value from its strategy that executives expect.

Taking investors' priorities and goals into account doesn't necessarily mean doing whatever current investors say they want. In some cases, the correct response to misalignment may be to migrate to new categories of investors who are more in sync with the company's strategy. In others, the solution may be to educate existing investors in order to persuade them that the current strategy will

meet their goals. And in still others, a company may decide to "take a hit" to its near-term valuation in order to pursue a sound strategy that will pay off in the future. But whatever the situation, executives need to anticipate the likely results of their decisions and plan for them in advance.

Unless senior executives are considering business strategy, financial strategy, and investor strategy simultaneously, they are likely to miss critical interactions. When understood in this more dynamic way, however, corporate strategy clearly becomes a more complex process with many moving parts, each to some degree dependent on the others. To make this complex process work, a company needs to take three steps: start a senior executive dialogue on value creation strategy, develop a comprehensive value-creation fact base, and align the organization around the right strategy.





# Starting a Dialogue on Value Creation Goals

**T**he purpose of a more integrated approach to corporate strategy is to more accurately take into account the complex dynamics and tradeoffs shaping value creation. In order to manage that complexity, senior executives need a straightforward and relatively easy-to-implement process. The starting point is for senior executives to begin an honest dialogue about the company's TSR goals.

## A Stake in the Ground

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It may seem strange to suggest that senior management *start* by discussing a TSR target. Shouldn't the company's TSR goal be the final outcome of the entire corporate-strategy process? But the purpose of this dialogue is not necessarily to finalize the company's value-creation goal immediately. Rather, the dialogue is meant to jump-start the corporate strategy process by getting the aspirations, assumptions, and perspectives of key decision-makers on the table and by putting a "stake in the ground" that will serve as an important reference point during subsequent steps in the process.

There are a number of advantages to beginning the process with a discussion of the senior team's TSR goal. For one thing, such a discussion can be a powerful focusing mechanism—and not only for the senior team but for all executives involved in the corporate strategy process. Most likely, the final TSR target to which a company's executives ultimately commit will be different from the goal they start out with. But having that initial goal in place signals to those participating in the development of the company's plan that TSR performance is an important objective and a key criterion for choosing among strategic options.

Another advantage of starting with a discussion of TSR goals is that it requires executive teams to start thinking through the specific drivers of value creation in their business, the amount of risk they are prepared to take on, and the amount of change necessary to achieve their goal. Indeed, an important value of this dialogue is precisely to surface senior executives' beliefs about all these issues. It's likely that these beliefs will vary widely. If the dialogue is conducted appropriately—that is, as a truly open and honest discussion with no preconceived outcomes—it will put key differences in perspective and disagreements about future direction on the table for further analysis and debate.

## Why TSR Is the Best Metric

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Using TSR as the central metric for value creation has a number of advantages. For one thing, it incorporates the value of dividends and other cash payouts, which can represent anywhere from 20 to 40 percent of a company's TSR (and even more at large, highly profitable companies with below-average valuation multiples). In this respect, TSR is a far more comprehensive measure than share-price appreciation.

But, even more important, focusing on TSR as the key metric of company performance is critical because it is the only measure that integrates all the dimensions of the value creation system. Consider some other commonly used proxies for value creation: growth in EPS, for instance, or cash-based metrics such as cash flow return on investment (CFROI) or cash value added (CVA). Because EPS growth is an accounting construct, it is vulnerable to manipulation that makes it look good at the expense of a company's actual cash flow. And since any investments above the cost of debt grow EPS, the ap-

proach encourages companies to take on debt even for investments that generate returns below the weighted average cost of capital. Capital markets generally see through these actions and discount a company's stock accordingly.

Cash-based metrics are much better. They avoid these shortcomings because they more accurately measure the fundamental value that a company creates. And they can be extremely effective for getting divisions and line management to think and act in terms of value creation. By themselves, however, they do not capture the impact of improvements in fundamental value on a company's valuation multiple or the full value of cash payments to investors.

### How High Should a Company Reach?

The minimum appropriate TSR goal is easy to establish: it will be set by either the company's cost of equity or the expected average TSR of its peer group (assuming that average is higher than the cost of equity). For most industries today, whichever criterion is used, that floor will be somewhere between 8 and 10 percent per year. But how much higher should a company reach?

That decision depends on the aspirations of the senior team and on the competitive advantages and management capabilities of the company. In our experience, most

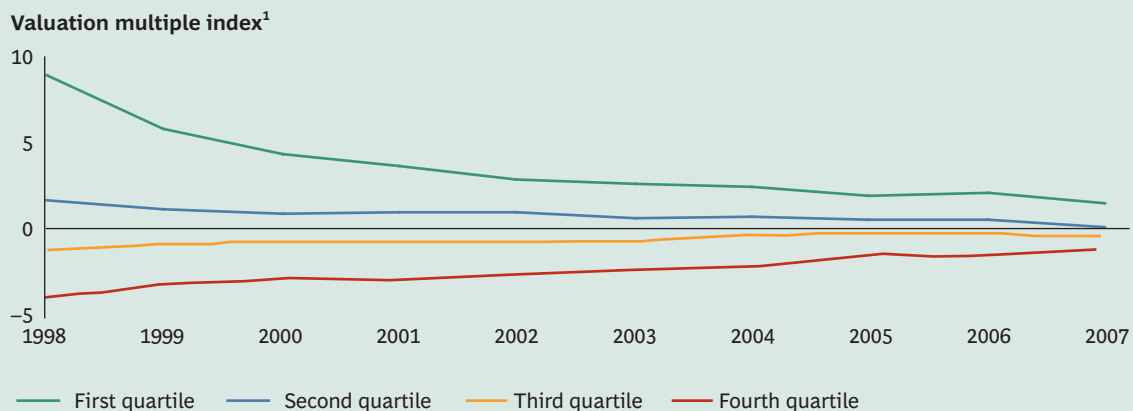
senior executives think in terms of achieving top-third or top-quartile performance in their industry or peer group. In today's environment, that generally translates into an annual TSR of 14 to 16 percent over a five-year period.

Starting with an ambitious stretch goal of this sort can be useful to get an organization to take a critical look at its plans. But keep in mind that it is extremely difficult to consistently achieve something like top-quartile performance. Indeed, it is even difficult to regularly beat the market average. We have analyzed the ten-year average annual TSR at nearly 2,400 global companies with a market capitalization of more than \$1 billion. We found that only about 6 percent of the companies beat their local market average for eight years or more—and only a single company beat the average for the entire ten-year period.

The reason? Over the long term, markets are efficient and, taken as a whole, have access to enough information to accurately estimate a company's future performance. Therefore, to regularly beat the average, a company has to consistently deliver above the expectations that are already embedded in its stock price and reflected in its valuation multiple. If, by contrast, a company only meets those expectations, its multiple is likely to decline over time, bringing its TSR down to the market average.

Exhibit 3 demonstrates that this fade to the average in valuation multiples is experienced by the vast majority of

### Exhibit 3. Over Time, a Company's Valuation Multiple Tends to Fade to the Average



Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; BCG analysis.

Note: The sample consists of 1,964 companies with market capitalizations greater than \$1 billion; companies were assigned to quartiles by industry on the basis of their 1998 EBITDA multiples (the ratio of enterprise value to EBITDA).

<sup>1</sup>The valuation multiple index is the median EBITDA multiple of each quartile minus the median of the total sample.

companies. The exhibit divides a sample of 1,964 companies into four quartiles, based on a comparison of their valuation multiples in 1998 with the average multiple for their industries. The chart then tracks the median multiple of each quartile, compared with the median of the total sample, through 2007. As the four converging lines suggest, over the ten-year period the median multiple of each group approaches that of the entire sample. (See the sidebar “Coping with Multiple Compression,” on pages 18 and 19.)

So senior executives will need to be prepared to test their stretch goals against the realities of their company’s competitive position and organizational capabilities, as well as against the expectations of investors. In our experi-

ence, the result of this process is often to scale back the TSR goal to a more modest level. But that’s not necessarily a disaster. The good news is that if a company succeeds in delivering TSR just two to three percentage points above average year after year, such a performance can add up to top-quartile TSR over the long term.

There is one final advantage to starting the corporate strategy process with a debate about TSR goals. The dialogue often helps the senior team identify what it knows—and, perhaps more important, what it does not know—about the dynamics of value creation in its industry and its company. Therefore, the next step in the integrated corporate-strategy process is to develop a comprehensive value-creation fact base.

## Coping with Multiple Compression

Sooner or later, any company that has enjoyed a period of rapid growth will face multiple compression—the decline of its valuation multiple to the market average. Dealing with that compression so that it does not severely erode the company’s TSR is a tough strategic challenge.

The exhibit below illustrates the basic dynamics of multiple compression. Strong growth leads to an above-average valuation multiple, as investors bid up the company’s stock price in expectation of the future value created by that growth (which is considerable compared with the company’s current earnings). As the company continues to grow, the absolute value of sales increases, but because the company is starting from a higher base, its growth rate slows and starts to decline.

This decline in the company’s growth rate has two results. First, the value of expected future earnings relative to current earnings decreases—causing the multiple to decline as well. Although the company’s stock price may still increase, it will not do so as fast as the company’s earnings. Second, the company’s investor base starts to migrate from growth-oriented investors toward more value-oriented investors.

For an example of multiple compression in the real world, consider what happened at a U.S. software company. (See

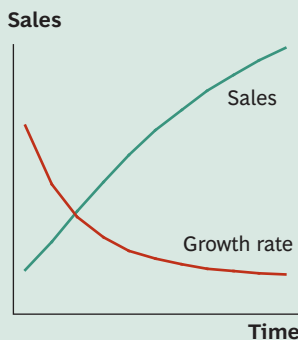
the exhibit “Multiple Compression at a U.S. Software Company Caused a Significant Shift in Its Investor Base.”) In 1999 the company had an annual growth rate of nearly 40 percent, which resulted in a price-to-earnings ratio of about 60—nearly double the S&P 500 market average. But as the company’s growth rate plummeted over the next few years, its multiple dropped with it—to the point where it was actually below the market average in 2007. Simultaneously, value investors as a percentage of the company’s total investor base more than doubled (from 14 percent to 30 percent), while its core growth investors declined from 32 percent to 20 percent.

The phenomenon of multiple compression presents senior executives with a fundamental strategic choice: They can find ways to prolong their high growth rate (or, at least, cause it to decline more slowly than investors expect), thus beating the expectations of their current growth investors, keeping their multiple relatively high, and continuing to grow their stock price at a high rate. Or they can shift decisively to a strategy that balances growth against other priorities attractive to the growing number of more value-oriented investors in their investor base.

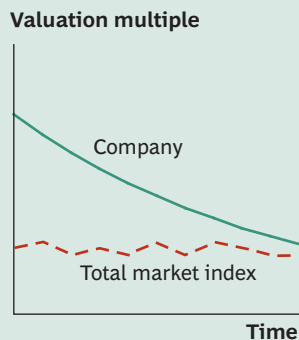
Beating investor expectations for growth can be extremely difficult to do. It is a bit like fighting against gravity. More

### After Periods of Rapid Growth, a Company Typically Experiences Multiple Compression

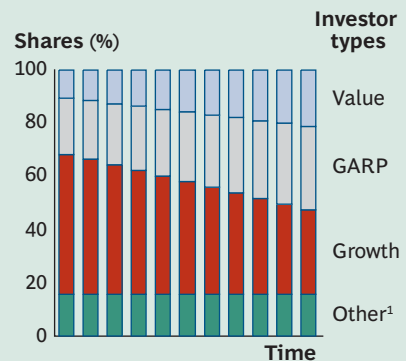
As a company gets bigger, its rate of growth slows ...



... causing its above-average multiple to decline ...



... and shifting the mix of its investor base toward value



Source: BCG analysis.

Note: This exhibit is for illustrative purposes only.

<sup>1</sup>Other consists of hedge, index, international, momentum, sector-specific, specialty, venture-capital, private-equity, and yield investors.

often than not, it requires eroding current margins (or failing to improve margins as much as investors expect), taking on more risk, or investing cash in uncertain growth initiatives when more TSR could be created by giving that cash back to investors. Any of these moves may cause the multiple to decline even more than it would if the company simply let its growth rate drop. Executives need to examine these moves carefully to determine if they are creating value over the long term.

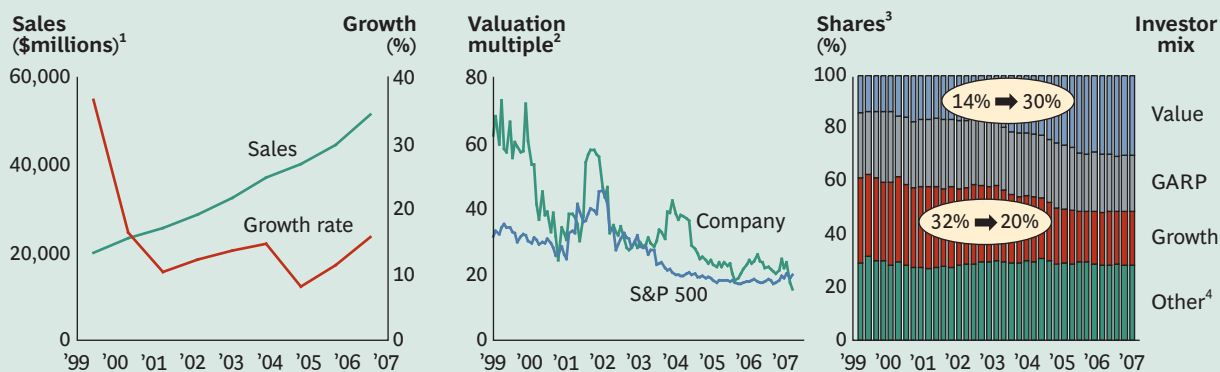
Alternatively, executives can stop thinking of growth as a privileged driver of value creation and start focusing on other drivers of TSR. For example, they can start paying more attention to margins in an effort to ensure that growth translates into operating leverage that boosts earnings faster than revenues. Or they can start appealing directly to value-oriented investors in their investor base—for instance, by paying out more cash through share repurchases or dividends.

Figuring out which choice is genuinely the most appropriate requires considerable judgment. There are situations in which companies successfully beat back multiple compression by finding new ways to grow; some even do so multiple times. Indeed, if a company plans far enough in advance, it can avoid multiple compression—for example,

by using its still-high stock price as an attractive currency with which to acquire higher-growth businesses. And yet the far more common experience is for a company to persist in trying to remain a growth company long after the favorable conditions for such a strategy have disappeared—at the price of creating major misalignments with its current investor base and triggering a systematic discount on its multiple relative to peers.

Companies that do not orchestrate an effective transition to a new, more value-oriented strategy as their growth rate slows often experience a number of years of stagnation or declining stock price, even though they are delivering above-average revenue growth. Migration in a company's investor base to more value-oriented investors is a clear signal that it may be time to change strategies. Ideally, however, executives should not wait for this to happen but rather anticipate it and shift their company's corporate strategy to create a "soft landing" for its multiple.

### Multiple Compression at a U.S. Software Company Caused a Significant Shift in Its Investor Base



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

Note: Valuation multiple data are reported monthly; investor data for identified free-float shares are reported quarterly.

<sup>1</sup>The data shown reflect sales at the end of the respective business year.

<sup>2</sup>Price-to-earnings ratio.

<sup>3</sup>Data are shown for institutional investors only.

<sup>4</sup>Other consists of hedge, index, international, momentum, sector-specific, specialty, venture-capital, private-equity, and yield investors.



# Developing a Value Creation Fact Base

**I**n our experience, most companies never really establish the kind of fact base they need in order to make fully informed decisions about corporate strategy. Instead, they make do with a confusing mix that is one part hard data (often owned by functional players and not broadly shared by the senior team), one part legacy beliefs and opinions that have acquired the status of facts for the simple reason that no one has ever challenged them, and one part blind spots about key information they need but don't have. As a result, assumptions can't be tested and disagreements in perspective can't be objectively resolved. The solution is to develop a comprehensive value-creation fact base spanning all three dimensions of corporate strategy: business strategy, financial policies, and investors' priorities.<sup>6</sup>

## What's Behind TSR Performance

The business strategy fact base provides basic information about a company's historical and expected future value-creation performance. Its purpose is to answer the following questions:

- ◇ What are the historical sources of value creation at our company and at our peers?
- ◇ How much TSR can our current company plans deliver?
- ◇ Is there a gap between our plans and our aspirations?
- ◇ If so, can our current strategy fill the gap—or do we need either to consider major changes in our strategy or to scale back our goals?

It's not enough simply to know a company's TSR record over time. Rather, executives need to break down that

performance (as well as that of their peers and each of their individual business units) into the key drivers of value creation. BCG has developed a model for quantifying the relative impact of the various drivers of TSR. (See Exhibit 4.) This TSR decomposition model uses the combination of sales growth and change in margins (resulting in growth in EBITDA) as an indicator of a company's improvement in fundamental value. It then uses the change in the EBITDA multiple—the ratio of enterprise value (the market value of equity plus the market value of debt) to EBITDA—as a measure of how changes in investor expectations affect TSR.<sup>7</sup> Finally, it tracks the distribution of free cash flow to investors and debt holders—dividend yield, change in shares outstanding, and net debt change—in order to track the impact of paying out cash or raising new capital. Using this model, executives can analyze the sources of TSR for their company, its business units, a peer group of companies, an industry, or an entire market index over a given period.

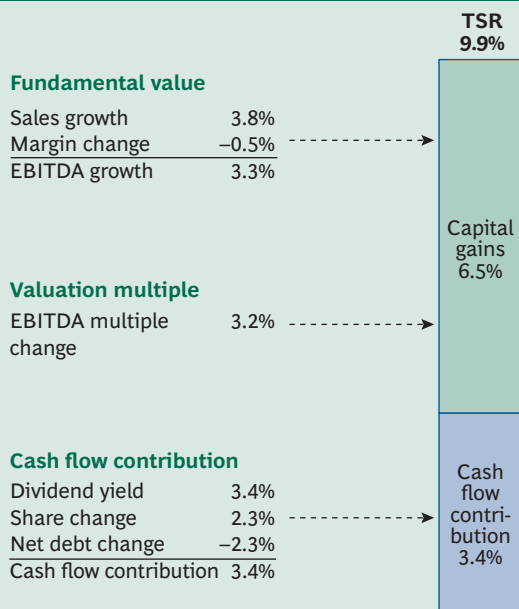
When executives go through this process, they tend to learn that even companies in the same industry create value in different ways. Take, for example, the analysis shown in Exhibit 5, which compares the TSR decomposition of a company with that of its five main peers. The

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6. This section focuses exclusively on the analyses necessary to make value creation an integral part of the corporate strategy process. There are many other issues that a comprehensive corporate strategy should consider—for example, an examination of the evolving industry landscape or the logic of a company's portfolio. These topics are outside the scope of this report.

7. There are many ways to measure a company's valuation multiple, and different metrics are appropriate for different industries and different company situations. In this study, we have chosen the EBITDA multiple in order to have a single measure with which to compare performance across our global sample. (See "Appendix: The 2008 Value Creators Rankings," beginning on page 34.)

### Exhibit 4. BCG's Decomposition Model Allows a Company to Identify the Sources of Its TSR



Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; BCG analysis.

Note: This analysis is based on an actual company example; the contribution of each factor is shown in percentage points of annual TSR.

TSR of the first two peer companies is virtually identical—20.6 percent and 20.5 percent, respectively—but there the similarities end. The first company gained the lion's share of its TSR through margin improvement. For the second, however, the main source of TSR was above-average sales growth (even though it came at the price of some erosion in margins). And other peer companies created substantial value from improvement in their multiple (Peer 3), from paying down debt (also Peer 3), or from share repurchases (Peer 5).

The point is simple: there are many different ways to create value. A company has to consider carefully which combination of factors is most appropriate at any moment in time. It is important both to understand the historical sources of a company's TSR and to anticipate which drivers of value creation will be most important in the future.

Just as a company has to "get under the hood" of its overall TSR performance, it also has to get under the hood of its valuation multiple—that is, understand the precise drivers that set relative multiples in its industry or peer group. Many managers tend to see the factors affecting their company's multiple as something of a mystery

### Exhibit 5. Breaking Down the Sources of TSR Shows That Different Companies Create Value in Different Ways

Contribution to average annual TSR, 2003–2008

		Peer 1	Peer 2	Peer 3	Peer 4	Peer 5	Company	Peer group average <sup>1</sup>
Fundamental value	Sales growth	4.5	18.0	8.4	12.2	7.3	10.6	10.2
	Margin change	8.5	-1.4	0.5	-0.3	-3.1	-6.3	0.2
Valuation multiple	EBITDA multiple change	3.6	6.3	10.0	3.9	-0.8	-3.1	3.5
Cash flow contribution	Dividend yield	4.0	0.0	2.1	0.7	0.9	0.4	1.7
	Share change	0.0	-0.4	-4.3	0.1	5.9	0.0	0.1
	Net debt change	0.0	-2.0	3.0	0.0	0.0	4.4	1.1
<b>Total TSR</b>		<b>20.6</b>	<b>20.5</b>	<b>19.7</b>	<b>16.6</b>	<b>10.2</b>	<b>6.0</b>	<b>16.8</b>

Sources: Compustat; BCG analysis.

Note: The primary sources of a company's TSR are circled in red. The contribution of each factor is shown in percentage points of five-year average annual TSR.

<sup>1</sup>Weighted average of peer group.

largely outside their control. In fact, it is possible to identify the specific drivers of multiples in a particular industry or peer group and, therefore, to quantify how a company's actions affect its multiple.

In recent Value Creators reports, BCG has described a technique for identifying what differentiates multiples among the companies in a given industry. The technique uses statistical regressions to compare observed multiples against a broad range of financial and performance data. We have found that we can explain roughly 70 to 90 percent of the observed differences among multiples in an industry over a five- to ten-year period.<sup>8</sup>

Going through such an exercise will likely confirm some assumptions about what affects the multiple. But it will also highlight new and unexpected dynamics. For example, despite most executives' focus on EPS growth, in many industries it is operational factors that really drive the multiple. In the retail grocery sector, for example, factors such as high gross margins, low operating expenses, and rapid inventory turnover account for more than 70 percent of the differences in multiples among companies; by contrast, the impact of growth is negligible. (See Exhibit 6.) In other sectors, financial factors turn out to be extremely important. For companies in the capital-intensive mining and materials industry, having a low debt-to-capital ratio is the most important differentiator among multiples, accounting for roughly 30 percent of the difference in multiples. (See Exhibit 7.) Whatever the precise result for a company's peer group, developing a more granular understanding of what drives relative multiples helps senior executives assess the impact of their decisions on their company's multiple—and, therefore, on TSR.

Armed with data about TSR decomposition and the drivers of relative multiples in its peer group, a company is in a position to quantify not only its historical TSR performance but also the TSR potential of its existing business plans. Is there a gap between the senior team's initial TSR goal and the value likely to be delivered by its current plans? If so, what are the opportunities for improving planned performance? If the gap is relatively small, it may be possible to squeeze more TSR out of existing plans. Alternatively, there may be financial moves the company can make to add additional TSR. If the gap is

large, however, the senior team may have to look more broadly: What is the likelihood of innovating new platforms for growth? Are there any potential megatrends the company can take advantage of? Or is major restructuring of the portfolio called for, including the requisite acquisitions and divestitures?

In some cases, such discussion will surface new options and opportunities. In others, it may suggest that the company has to scale back its TSR aspirations so that they are more in sync with the capabilities of the company's existing businesses. But whatever the initial conclusions, it will be necessary to test them against new information coming out of the other pieces of

the value creation fact base.

**The purpose of the financial fact base is to determine the best uses of the company's cash.**

## A Holistic View of Financial Policies

The second part of a comprehensive valuation-creation fact base involves a company's financial strategy. The purpose of the financial fact base is to inform senior management about the best uses of the company's cash. It is meant to answer the following four key questions:

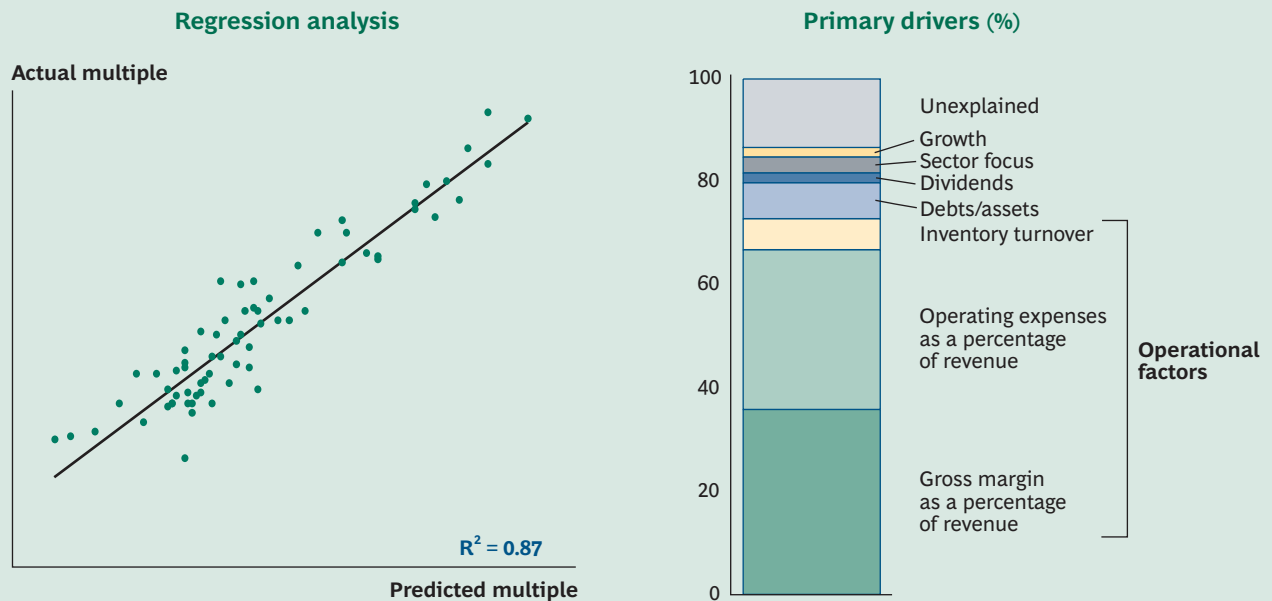
- ◇ How can we ensure financial flexibility to fund future growth?
- ◇ What is the optimal capital structure (debt-to-capital ratio) for minimizing our weighted average cost of capital?
- ◇ How much cash should we pay out and in what form?
- ◇ What are the appropriate hurdle rates for potential acquisitions?

Most companies have preexisting answers to these questions. The problem is that those answers are often based on long-standing historical norms or on theoretical financial models that aren't especially relevant to the compa-

8. For a more detailed description of this technique, which we call *comparative multiple analysis*, see "Exploiting Valuation Multiples" in *The Next Frontier: Building an Integrated Strategy for Value Creation*, The 2004 Value Creators Report, December 2004, pp. 29–36; and "Understand What Drives Relative Valuation Multiples" in *Balancing Act: Implementing an Integrated Strategy for Value Creation*, The 2005 Value Creators Report, November 2005, pp. 15–18.



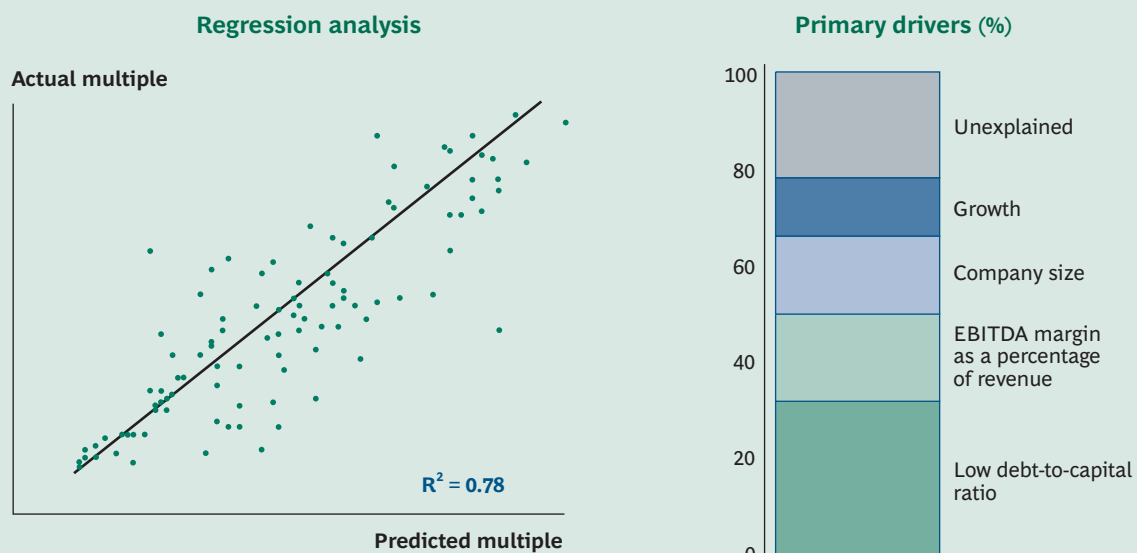
## Exhibit 6. In the Retail Grocery Sector, Operational Factors, Not Growth, Determine the Differences in Valuation Multiples



Sources: Compustat; BCG analysis.

**Note:** The scatter plot charts actual multiples for 15 leading grocery retailers over the five-year period from 2002 through 2006 against the predicted multiples derived from the regression analysis.  $R^2$  stands for multiple regression correlation coefficient. An  $R^2$  of 0.87 means that 87 percent of the observed differences among relative multiples are explained by the model.

## Exhibit 7. In the Mining and Materials Sector, a Low Debt-to-Capital Ratio Is the Most Important Differentiator of Valuation Multiples



Sources: Compustat; BCG analysis.

**Note:** The scatter plot charts actual multiples for a selection of mining and materials companies over the ten-year period from 1994 through 2003 against the predicted multiples derived from the regression analysis.  $R^2$  stands for multiple regression correlation coefficient. An  $R^2$  of 0.78 means that 78 percent of the observed differences among relative multiples are explained by the model.

ny's current competitive situation or the makeup of its investor base. What's more, most companies address these questions individually while they need to address them holistically.

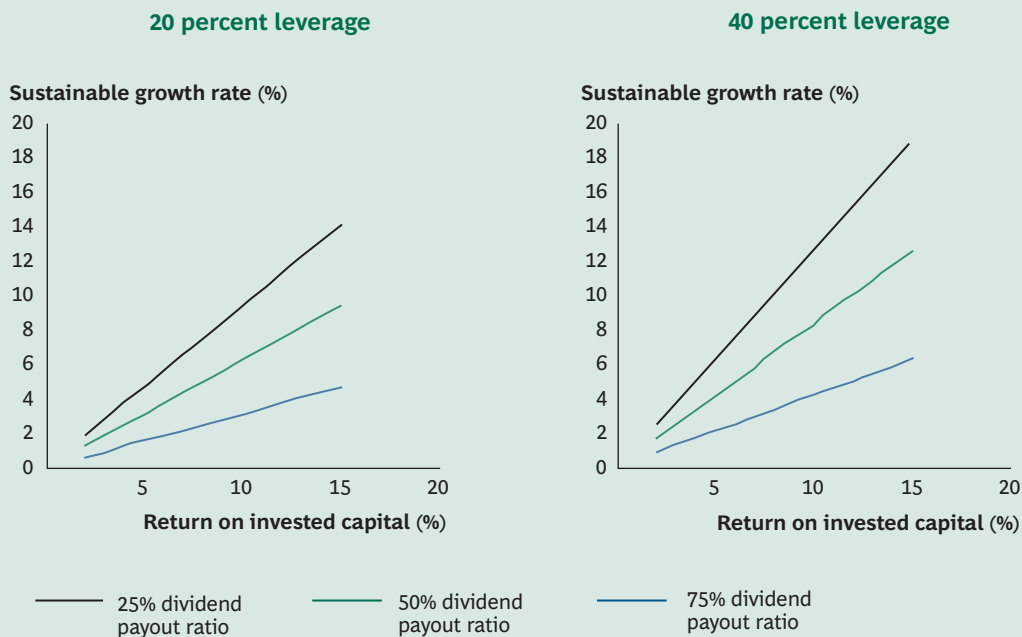
One critical piece of the financial fact base is quantifying a company's financially sustainable growth rate—that is, the organic growth rate in revenues that a company can fund without issuing new shares, assuming that its current returns and financial policies (such as debt-to-capital ratio and dividend payout) remain unchanged. Comparing this financially sustainable growth rate with a company's growth aspirations and with the underlying organic growth rates of its served markets can provide key insights for corporate strategy. For example, this analysis may signal that growth aspirations need to be scaled back unless returns on invested capital can be improved, or that financial policies need to be revisited, or that there is an industrywide problem because the company and its peers can fund substantially more investment for growth than the markets they compete in can absorb. (Exhibit 8 illustrates the components of a company's finan-

cially sustainable growth rate and the tradeoffs that can affect it.)

As senior executives begin to develop a sense of where they are currently positioned—and where, ideally, they would like to be positioned—on the sustainable growth chart, they will also learn not only how much growth they can fund but also how much cash they have available to return directly to investors after funding their growth strategy. The next step is to decide the best way, from a value creation perspective, to return that cash. Here the main focus should be on the effect that different types of cash payout have on the company's valuation multiple and on the company's ability to attract those types of investors who are most in sync with its long-term strategy.

Take the choice of dividends versus stock repurchases. Many executives believe that increasing dividend payout can damage a company's valuation multiple. Increasing dividends reduces the cash available for investment in growth, they reason, and therefore will reduce a compa-

### Exhibit 8. A Company's Sustainable Growth Rate Depends on Its Return on Capital, Dividend Payout, and Leverage



Source: BCG analysis.

ny's expected future EPS growth (which they believe is a key driver of their valuation multiple). At the same time, they tend to think that repurchasing shares can have a positive impact on their multiple because it automatically increases EPS—and suggests that the company thinks its stock is undervalued.

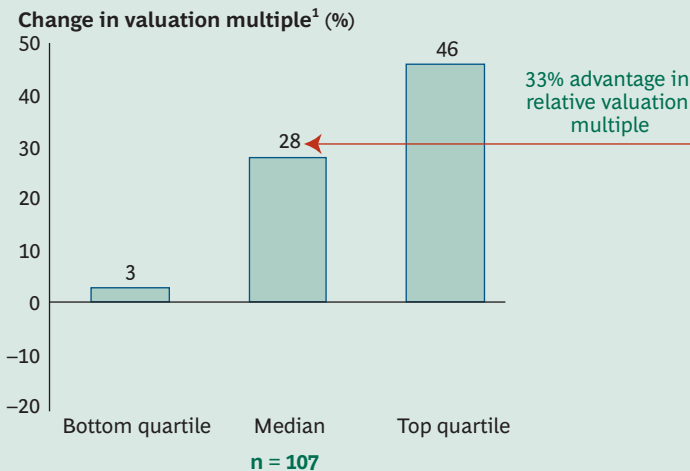
And yet, empirical evidence demonstrates that precisely the opposite is the case. We conducted an event study comparing the impact of increases in dividend payout (as a percentage of net income) with that of annual share-repurchase programs. (See Exhibit 9.) We studied 107 companies that either initiated a dividend payout of at least 10 percent of net income or increased an existing dividend payout by at least 25 percent. These increases improved relative valuation multiples over the following three quarters by 28 percent, on average, and improved the multiples of the top quartile by 46 percent. Conversely, an analysis of 100 companies that increased their ongoing share repurchases by a similar amount showed an average impact on relative valuation multiples of -5 percent—and of only 16 percent for the top quartile.

The reason for this dramatic difference has to do with the signaling power of dividends. Higher dividend payouts signal to current investors that management is confident in the company's future profitability (so much so that it doesn't need to worry about financial flexibility) and that the company is disciplined about using its cash to create shareholder value. As a result, new investors are attracted to the stock—thus producing stronger demand and a higher stock price as the new dividend yield is arbitrated to a lower level. The result is an increase in the company's valuation multiple and a higher near-term TSR.

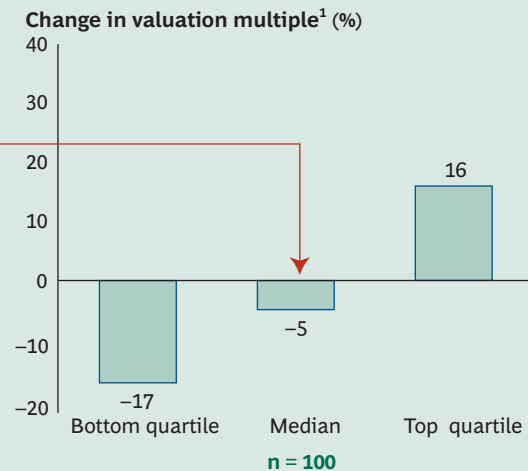
By contrast, share repurchases do not provide positive signals about long-term profitability or shareholder value discipline. They don't encourage investors to hold the company's stock (indeed, they mainly reward those who sell) or attract new long-term investors to buy it. As a result, the impact of share repurchases on a company's stock price often undermines the positive impact of the growth in EPS that the repurchases make possible. Although share repurchases may seem like an attractive way to preserve future financial flexibility (because, un-

### Exhibit 9. Dividend Increases Improve Relative Valuation Multiples More than Share Repurchases Do

**Impact of dividend increases on relative valuation multiples, U.S. S&P 500 and S&P MidCap 400, 2001–2005**



**Impact of share repurchases on relative valuation multiples, U.S. S&P 500 and S&P MidCap 400, 2001–2005**



Sources: Compustat; BCG analysis.

**Note:** The dividend sample includes all U.S. S&P 500 and S&P MidCap 400 companies that had a dividend-payout ratio of at least 10 percent of net income and that raised their dividend-payout ratio by at least 25 percent. The share repurchase sample includes all companies from the two indexes that had a repurchase-payout ratio of at least 10 percent of net income in the 12 months preceding a share repurchase announcement and that increased share repurchases by at least 25 percent in the subsequent four quarters. Both samples exclude companies with price-to-earnings (P/E) ratios greater than 150 percent of the U.S. S&P 500 average or at which EPS growth was less than zero (in order to exclude companies with P/E increases caused by lower earnings).

¹This is the change in P/E ratio relative to the U.S. S&P 500 average over the two quarters following the dividend or repurchase announcement.

like with dividends, it is easy to temporarily halt or reduce them), their impact on valuation multiples and TSR is far less than that of increasing dividend payout.

Finally, given the growing importance of M&A to corporate strategy at many companies, another key financial policy that needs to be rethought from the perspective of value creation is the financial hurdle a company sets for acquisitions. Despite all the recent articles in the business press about tight credit and the decline in the M&A market, BCG research shows that downturns are an especially good time for companies to consider M&A.<sup>9</sup> What's more, companies that systematically pursue growth through acquisitions tend to have superior TSR performance to those that grow mainly through organic expansion.<sup>10</sup> But mistaken financial policies often prevent companies from making the right moves around M&A.

When setting hurdle rates for M&A, companies often focus on whether a deal is *EPS accretive* (that is, whether it adds to a company's EPS) in the near term. The assumption is that when a deal adds to a company's EPS, it will be favorably received by investors, increase the company's valuation multiple, and thus add to TSR. But that assumption is misleading. The fact that a particular deal may be EPS accretive does not necessarily mean that it will improve a company's TSR. There are situations in which a deal can increase EPS but still cause the acquirer's multiple to decline, ending up *eroding* TSR—for example, if the acquired company provides near-term synergies but has a relatively low long-term growth potential.

By the same token, deals that dilute EPS in the near term can increase the acquirer's multiple and turn out to improve TSR. For instance, a company that acquires a fast-growing business with a high valuation multiple as a platform for future growth may have to pay a high price that will dilute its near-term EPS; but the company will likely increase its TSR because adding the new business will cause its own multiple to rise. Only when executives start evaluating potential acquisitions not only in terms of earnings but also in terms of their comprehensive impact on the entire value-creation system will they be able to assess whether a particular deal really makes sense or not.

## The Investors Who Matter—and What Matters to Them

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Even as the senior team is developing the above information and analyses, it also has to be building an investor fact base. After all, it is a company's investors who ultimately determine whether management's decisions and actions translate into the desired TSR results. Therefore, the third piece of a comprehensive value-creation fact base is to develop a detailed understanding of the priorities and expectations of a company's investors, as well as of any potential new investors that the company could reasonably attract given its intended strategy. The investor fact base should answer such

questions as the following:

- ◇ Who are our dominant investors?
- ◇ Are they the right ones given our current strategy?
- ◇ Do current or desired investors find the company's strategy credible?
- ◇ What can we do to create better alignment between our strategy and our investor base?

Of course, executives talk with investors and sell-side analysts all the time. The problem is that these interactions are often so superficial that their "signal-to-noise" ratio is disappointingly low. The trick is for companies to discern the signal within the noise by carefully segmenting the investors who own a company's stock. Investors are much like customers.<sup>11</sup> Different classes of investors have different appetites for growth, profitability, cash flow generation, and risk. Any large public company will have a mix of different kinds of investors with different—and sometimes conflicting—priorities. Therefore, it is important for a company to quantify its mix of investors (value, income, GARP, aggressive growth, and so on) in order to identify which classes are overweighted

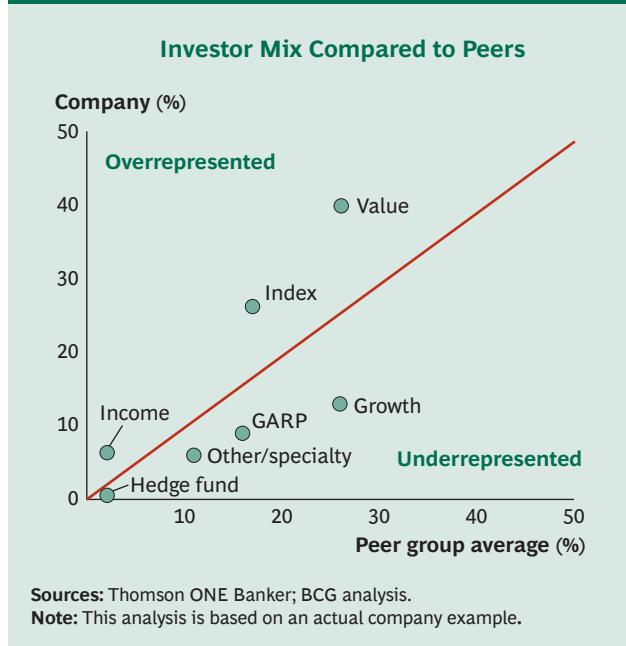
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9. See *The Return of the Strategist: Creating Value with M&A in Downturns*, BCG report, May 2008.

10. See *Growing Through Acquisitions: The Successful Value Creation Record of Acquisitive Growth Strategies*, BCG report, May 2004.

11. See "Treating Investors Like Customers," BCG Perspectives, June 2002.

## Exhibit 10. Identifying Dominant Investor Groups Is a Key Component of the Value Creation Fact Base



compared with market, industry, or peer-group averages—and therefore most attracted to the company’s current value proposition and most likely to respond to its strategic moves. (See Exhibit 10.)

Companies should supplement these quantitative analyses with qualitative data. Once the dominant investors have been identified, senior management needs to develop a rich understanding of how these investors really see the company. For example, many large and relatively slow-growth companies can have a significant portion of growth-style funds in their investor ownership mix. But the fund managers will often say that the company is not expected to play a growth role in their portfolio, and they are not looking for management to take risks or divert cash to increase their growth rate. Only by talking to investors, asking the right questions, and carefully listening to and interpreting their responses can management gain a clear view of the expectations and priorities of the company’s investor base. A company’s executives may be uncomfortable doing this directly—out of concern that their questions will send signals that they don’t intend or want to provide. But there is a lot that they can learn from having an objective third party engage in in-depth, face-to-face dialogues with dominant

investors and report back on their views of the company and its strategy.

When companies develop this kind of sophisticated fact base about investors’ priorities and goals, they tend to learn things that can fundamentally change how senior executives think about their corporate strategy. In some cases, they realize that they have been misunderstanding precisely who their dominant investors are and what they really value. At one company, for example, senior managers assumed that the key to improving the valuation multiple was aggressive growth. But an investor segmentation demonstrated that the company’s dominant investors were GARP investors who saw the company’s ambitious growth plans as neither necessary nor achievable and discounted the company’s stock price accordingly. The executives realized that they needed a more balanced strategy with demonstrated improvements in margins, more modest near-term growth, and greater cash payout.

In other situations, executives discover that legacy financial policies are precluding their company from attracting the kinds of investors who are most appropriate for its long-term strategy. One company, for instance, happened to have a history of frequent share repurchases that had attracted a class of investors narrowly focused on that priority. This relatively minor financial policy had become the tail wagging the value creation dog and was preventing the company from initiating a dividend or using cash for M&A.

Finally, sometimes senior executives discover that there is a major misalignment between the company’s strategy and the priorities of its investor base that creates a systematic drag on its valuation multiple. Usually, this is a signal that the company has the wrong investors for its strategy and needs a plan for migrating to a more appropriate investor base. But in some cases, misalignment is a signal that the company has the wrong strategy for the investors it currently has or might attract and needs to change its strategy so that it aligns more closely to the goals and priorities of the dominant groups in its investor base.



# Aligning Around the Right Strategy

**P**utting together a comprehensive value-creation fact base will quantify the impacts of discrete choices, raise new issues, and offer fresh insights about the tradeoffs senior executives need to manage. By itself, however, having such a fact base will not suggest the best overall corporate strategy for the future. This final step often requires senior teams to explore and debate a range of strategic options and align around the best path forward.

## Let the Debate Begin

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For some companies, the best path may be relatively clear, involving little more than a slight tweaking of the existing strategy. For most, however, it's likely that the exercise of assembling a detailed fact base will suggest a number of alternative paths that the company might follow. These options will appeal to different investors (and to different members of the executive team), entail different levels of risk and degrees of difficulty in implementation, and produce different overall TSR results. Therefore, they need to be debated.

A useful starting point is to get management opinions on the table about the key choices and tradeoffs facing the company. (See Exhibit 11.) Having members of the senior team decide where they think the company should be on these tradeoffs generally has two results. First, it identifies where the key disagreements are about the direction that the company should take. The more divergence there is among senior executives on such key questions as how much growth to go for, the appropriate balance between organic growth and M&A, and whether to stick with the current portfolio or move to a new one, the greater the need to fundamentally examine different strategic options.

The exercise also illustrates another important point: reaching consensus on each of these dimensions cannot be decided on an issue-by-issue basis. The strategic alternatives a company considers need to be coherent. No realistic option, for instance, is going to allow a company to shift from modest growth to aggressive growth without also requiring a major increase in risk. As executives define alternative value-creation options, they need to make sure that these options are internally consistent.

## The TSR Impact of Alternative Value-Creation Scenarios

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The exercise in Exhibit 11 will provide a rough idea of what the main alternatives facing a company are. But deciding which path to take will require carefully defining the key options, discussing in detail their pros and cons, and quantifying their likely impact on TSR. It is extremely difficult to do this within the context of the traditional planning process. Rather, it will require focused, top-down effort by the senior team.

Take, for example, the recent situation at a global pharmaceutical company. The company had a number of large and extremely profitable businesses in its core therapeutic areas. But growth in these businesses had slowed in recent years. For the company's executive team, the starting point of the scenario process was a significant gap between the senior team's TSR goal of 16 percent and the likely future TSR to be generated from the existing business plan—estimated at only 10 percent. The gap was primarily due to the fact that a number of the company's best-selling drugs would be coming off patent in the fourth and fifth year of the five-year business plan. And the company's valuation multiple was taking a hammering as a result.

## Exhibit 11. Defining Value Creation Scenarios Requires Making Strategic Choices Across Multiple Dimensions

Dimension	Range of choices
Growth ambition	Harvest   Invest
Growth path	Organic   Acquisition
Portfolio mix	Maintain   Migrate
Time frame	Near term   Long term
Financial flexibility	Maximize   Monetize
Appetite for risk	Low   High
Financial policies	Dividend   Repurchase
Investor mix	Core value   GARP   Growth

Source: BCG analysis.

Under the circumstances, company executives knew that to reach their TSR goal, they had to think about transforming the portfolio in order to substantially boost growth. But there was considerable disagreement about the best way to do so. The group initially defined three possible scenarios for the future.

The first scenario was built around a major merger of equals—that is, the acquisition of another large pharmaceutical company with drugs in overlapping therapeutic areas that would remain under patent throughout the five-year time frame. Merging with a major rival would reduce the TSR impact of the drugs going off patent and create a less volatile earnings pattern for the merged company. The company also explored the possibility of acquiring a large biotech company instead. Moving into biotech would diversify the pharmaceutical company's technology base and improve its overall growth profile. A third scenario avoided large acquisitions altogether and instead emphasized the focused acquisition of many small companies in high-growth specialty therapeutic areas underrepresented in the pharma company's portfolio.

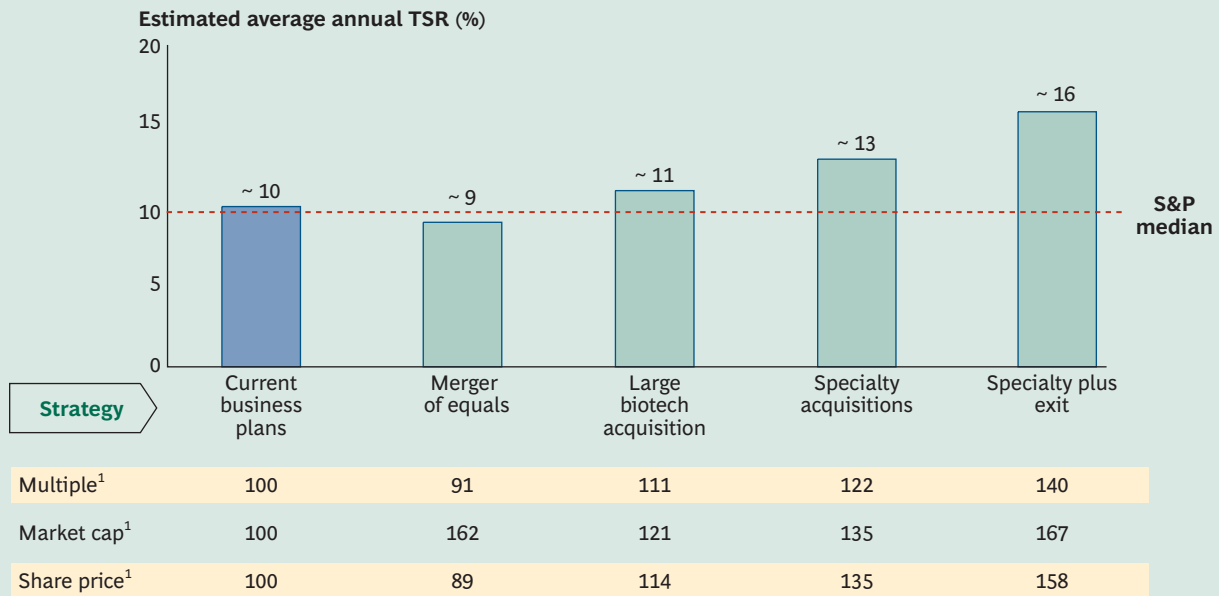
When company executives began to assess the three scenarios, the merger-of-equals option proved to be disappointing. (See Exhibit 12 on the following page.) When the team compared the expected revenue and cost syner-

gies with the likely premium required to do such a deal, they found that the option would actually erode the company's average annual TSR rather than increase it. The biotech option did better, improving TSR somewhat—but only by about one percentage point. The team concluded that this exceedingly modest improvement was not worth the risks involved in trying to integrate a company with a fundamentally different organizational culture and business model.

By contrast, the specialty option was much more promising—improving the company's five-year average annual TSR by about three percentage points. But this option also had a problem: although the average TSR was quite good, the time required to acquire a critical mass of smaller companies and grow them enough to significantly move the needle on the company's massive annual earnings meant that most of the positive impact on TSR would come toward the end of the five-year period. But the company's current investor base, dominated by value investors, was unlikely to recognize the long-term value of the strategy. As a result, the company's valuation multiple would remain low, and TSR in the early years of the plan would be less than 10 percent.

In the end, the executives decided to combine the specialty strategy with a plan to exit of one of the company's

## Exhibit 12. A U.S. Pharmaceutical Company Assessed Multiple Value-Creation Scenarios



Source: BCG analysis.

Note: This analysis is based on an actual company example; numbers are for illustrative purposes only.

<sup>1</sup>Index; current business plans = 100.

large but slow-growing therapeutic areas. This move, they reasoned, would have the effect of more quickly improving the company's growth profile and attracting more growth-oriented investors who would fully value the company's proposed strategy. The resulting increase in the company's valuation multiple would improve TSR in the first years of the plan, and the exit would free up cash, which could be used to accelerate the company's acquisition program. The combined impact of these changes would be to raise the company's five-year average annual TSR close to its 16 percent goal, as well as better position the company in key areas of underserved medical needs that would be the focus for future growth in the industry. The company is currently executing this new plan.

### The Corporate Strategy Timeline

One of the advantages of closely examining specific value-creation options is that the very act of debating alternative paths forward tends not only to thoroughly vet all the options but also to build alignment around the ultimate direction chosen. That alignment greatly diminishes

the likelihood that persistent unresolved disagreements will distract management's attention, thus improving the odds that the company's planned strategy will be implemented. But before the senior team is finished, it must turn its desired corporate strategy into a detailed implementation plan that can be delivered by the organization and clearly communicated to investors. We like to call this the *corporate strategy timeline*.

For an example of the process of creating a timeline, consider the recent experience of a U.S. consumer-goods company. Several years ago, the company had a classic bimodal portfolio. The portfolio contained a number of large business units consisting of mature brands that, although quite profitable, had a relatively low—and declining—growth rate. More recently, however, the company had either built or acquired a number of smaller brands. These businesses generated a minority of the company's revenues, but they were growing rapidly and were highly promising for the future.

The company's investor base, like that of the pharmaceutical company, was dominated by value investors



who were not interested in rapidly improving growth. As a result, the potential value of these new businesses was not fully reflected in the company's valuation multiple, which was among the lowest in its peer group.

The consumer goods company didn't face an immediate crisis. But executives felt trapped between the strategy they firmly believed was best for the long term and the priorities of current investors. The executive team wanted to invest in the company's new businesses, expand internationally, and acquire additional brands—all with the goal of boosting profitable growth. And because senior executives believed the company's stock was undervalued, they wanted to use cash or debt for any new acquisitions, not issue new shares. The company's dominant investors, by contrast, were looking for higher cash payout. And to the degree that the company increased debt, they wanted it used for share repurchases, not acquisitions.

There was no easy way for the company to quickly transform itself into a growth company and be rewarded by the capital markets. It would be at least three—and maybe as many as five—years before the company's new businesses would, on their own, be big enough to deliver the majority of the company's revenues. And while divestitures of some slow-growth businesses might more quickly speed up the company's growth rate, none of these businesses was big enough to materially change the growth profile of the company in a single deal.

Therefore, the senior team concentrated on coming up with a carefully sequenced, quarter-by-quarter strategic plan to progressively shift its strategy and its investor base over the next two years. (See Exhibit 13 on the following page.) The plan consisted of three major phases. In the first phase, the top priority would be to maximize the appeal of the company to its current value investors, even as it began to set the groundwork for attracting new types of investors who were somewhat more growth-oriented and less focused on very high cash payouts. The major event in this phase would be a near doubling of the company's dividend. The second phase would emphasize a tuck-in acquisition—to improve the scale of one of the company's high-growth brands—and the divestiture of one of its core brands. These moves would improve the company's growth profile, attract more growth-

oriented investors, and generate more cash for both organic and acquisitive growth. Once the company's investor base had shifted decisively from value to growth, and the growth profile of the company's portfolio had achieved critical mass, the company would embark on a third phase: a series of aggressive growth initiatives, both organic and acquisitive.

### **Executives felt trapped between their strategy and their investors' priorities.**

Equally important to these strategic moves, however, was a sequence of investor communications to shape the context for how investors perceived these moves. For example, the entire strategy was kicked off with an "investor day," at which the company announced an explicit TSR goal in order to communicate to the investor

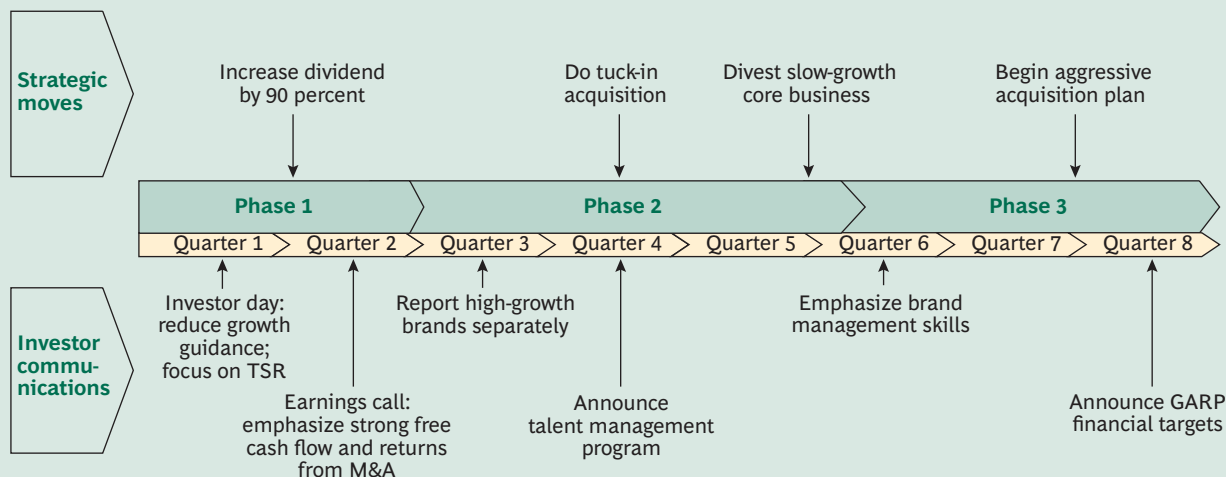
community that the company was focused on TSR, rather than growth for growth's sake. At the same time, the company scaled back its growth guidance somewhat to show that it was disciplined about its growth initiatives. These announcements laid the groundwork for the dividend increase. At the first earnings call after the increase, however, the company began to introduce growth-oriented themes to analysts and investors. For example, it touted its relatively high returns on invested capital, emphasized its success at creating value from some of its earlier acquisitions, and argued that it had sufficient resources both to increase dividend payout and to fund new growth.

In the second phase, before doing its tuck-in acquisition and divestiture, the company began reporting the results of its smaller, fast-growing brands separately from those of its core brands in order to emphasize the smaller brands' higher growth potential. It also announced the creation of an internal talent-management program that would build the capabilities necessary to manage a stable of high-growth global brands.

In the third phase, as the company shifted decisively to a high-growth path, it began emphasizing to analysts and investors the depth of its brand-management skills. Finally, at the end of the two-year transition plan, the company released financial targets aimed squarely at more growth-oriented investors.

For the consumer goods company, the events of the timeline became stakes in the ground against which its management team had to deliver. It also defined the script for a steady diet of positive news that would be commu-

## Exhibit 13. A Detailed Corporate-Strategy Timeline Aligns Employees and Investors to a Company's Plan for Value Creation



Source: BCG analysis.

Note: This analysis is based on an actual company example.

announced to investors. The company is now in the final phase of its strategic plan. The increase in dividend payout had a major impact on the company's valuation multiple—causing it to increase by 30 percent within six months of the announcement. The company's multiple, which had been the lowest in its peer group, soared to substantially above average. From the start of the company's plan through 2007, its TSR outpaced that of its peer-group average by 24 percent. The company has successfully migrated its dominant investor group from value investors to GARP investors. Although the tough economic conditions of 2008 have caused the company's TSR to decline, it is still outpacing that of its peer group.

As these examples suggest, systematically exploring a broad range of value creation scenarios and testing them against an explicit TSR goal is the best way to forge a close link between corporate strategy and value creation. It helps companies avoid corporate strategies that are incremental responses when larger opportunities are within reach or bolder moves are required. It also results in far greater commitment on the part of the organization to whatever path the senior team chooses, thus ensuring more effective implementation. Given the ongoing turbulence roiling the global economy, now may be the ideal time to adopt this more comprehensive approach to corporate strategy.



# Ten Questions That Every CEO Should Know How to Answer

**I**n conclusion, we offer ten questions about corporate strategy and value creation that every CEO should know how to answer. The questions synthesize the basic arguments and recommendations made in this year's report in a concise format.

1. *Do you have an explicit TSR target guiding your strategic plan?* Is that target appropriate given the expectations embedded in your stock price and the ability of your business plans to deliver improved performance? Do you understand how each of your businesses will contribute to meeting your TSR goal?
2. *What are the historical sources of TSR for your company?* How does your historical profile compare with that of your peers? How has the way you create value evolved over time? Are the company's future sources of TSR likely to be similar to or different from those underlying your recent performance?
3. *What drives the differences in valuation multiples in your industry?* Are investors discounting your multiple? If so, do you understand why and what to do about it? Are you experiencing multiple compression? How will your strategic choices affect your multiple in the future?
4. *What is your financially sustainable growth rate?* Is it in balance with the estimated growth rates in the markets you currently serve? If not, what is the best way to deploy your excess cash?
5. *Is M&A a critical part of your corporate strategy?* If so, do you know whether the deals you are considering will improve TSR? Have you set the appropriate financial hurdle rates for potential deals?
6. *What is the impact of your financial policies on your valuation multiple and TSR?* Do you know their implications for your business strategy choices?
7. *Who are your dominant investors?* Do you know their goals and priorities for value creation? Is your corporate strategy in sync with those goals and priorities? If not, do you have a plan for migrating to investors more closely aligned with your strategy?
8. *What are your key value-creation alternatives for the future?* Do you have a robust process in place for analyzing these alternatives, debating their pros and cons, and creating alignment around the right path forward?
9. *Are your business strategy, financial strategy, and investor strategy internally consistent?* Do they reinforce or contradict one another?
10. *Do you have a detailed corporate-strategy timeline describing how you will execute your strategy?* Does it include the necessary internal development programs and external investor communications?

# Appendix

## The 2008 Value Creators Rankings

**T**he 2008 Value Creators rankings are based on a detailed analysis of total shareholder return at 644 global companies for the five-year period from 2003 through 2007.

To arrive at this sample, we began with TSR data for more than 5,000 companies provided by Thomson Financial Worldscope. We eliminated all companies that were not listed on some world stock exchange for the full five years of our study or did not have at least 25 percent of their shares available on public capital markets. We also eliminated certain industries from our sample—for example, financial services.<sup>1</sup> We further refined the sample by organizing the remaining companies into 14 industry groups and establishing an appropriate market-valuation hurdle to eliminate the smallest companies in each industry. (The size of the market-valuation hurdle for each individual industry can be found in the tables in the “Industry Rankings,” beginning on page 42.) In addition to our 644-company sample, we also separated out those companies with market valuations of more than \$50 billion. We have included rankings for these large-cap companies in the “Global Rankings,” on page 40.

The global and industry rankings are based on five-year TSR performance from 2003 through 2007.<sup>2</sup> We also show TSR performance for 2008, through June 30. In addition, we break down TSR performance into the six investor-oriented financial metrics used in the BCG decomposition model described on pages 20–21. Finally, we chart TSR against valuation multiples for all the companies in each sample.

The average annual return for the 644 companies in our sample was an extremely healthy 17.1 percent. (See Ex-

hibit 1.) This return reflects the strong rebound of the global economy after the bursting of the late-1990s financial bubble and the 2001 recession. However, looking ahead, TSR is unlikely to be so robust. Most of the top ten companies in each industry, for instance, have reported negative—and, often, substantially negative—TSR in the first half of 2008.

It is also important to emphasize that many companies in our sample substantially outpaced both the total sample average and their own industry average. For example, the average annual TSR of the global top ten was more than five times greater than that of the sample as a whole—an extraordinary 95.1 percent per year, on average. (See Exhibit 2.) The top ten companies in each industry outpaced their industry TSR averages by between 14 percentage points (in utilities) and 47.3 percentage points (in mining and materials). In every industry we studied, the top ten companies also did substantially better than the overall sample average—by at least 8 percentage points of TSR. The lesson for executives is this: Coming from a sector with below-average market performance is no excuse. No matter how bad an industry’s average performance is relative to other sec-

1. We chose to exclude financial services because measuring value creation in the sector poses unique analytical problems that make it difficult to compare the performance of financial services companies with companies in other sectors. For BCG’s view of value creation in financial services, see *Managing Shareholder Value in Turbulent Times*, The 2008 Creating Value in Banking Report, March 2008.

2. TSR is a dynamic ratio that includes price gains and dividend payments for a specific stock during a given period. To measure performance from 2003 through 2007, 2002 end-of-year data must be used as a starting point in order to capture the change from 2002 to 2003, which drives 2003 TSR. For this reason, all exhibits in the report showing 2003–2007 performance begin with a 2002 data point.

tors and to the market as a whole, it is still possible for companies in that industry to deliver superior shareholder returns.

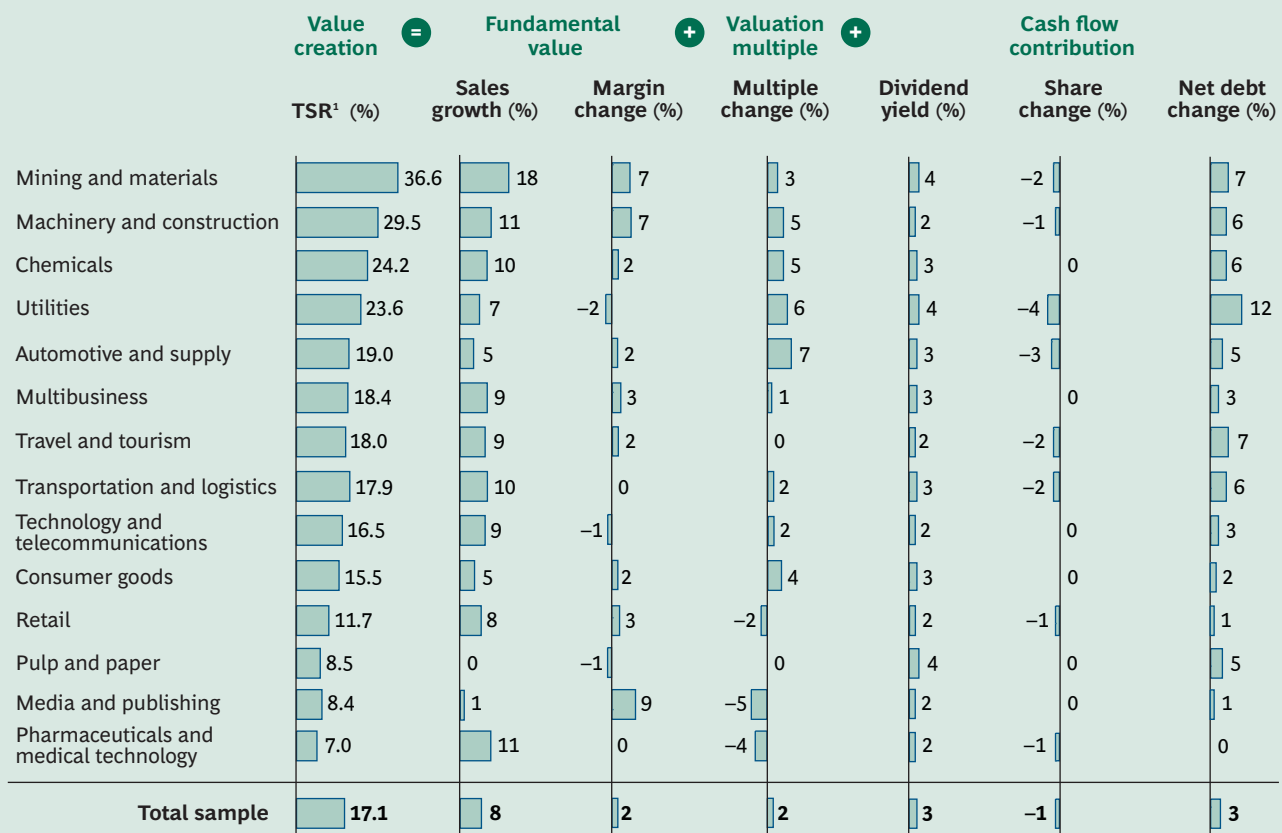
What kind of improvement in TSR was necessary to achieve top-quartile status? The exhibit “Average Annual Total Shareholder Return by Quartile, 2003–2007” on page 38 arrays the 644 companies in our global sample according to their five-year TSR performance. In order to achieve top-quartile status, companies needed to post an average annual TSR of at least 32.2 percent. The very best performers had truly stunning returns ranging from roughly 90 to nearly 150 percent per year.

The arrival of companies from rapidly developing economies (RDEs) on the global value-creation stage has

been dramatic. Fully half of the companies in the global top ten come from either China or India. (See the exhibit “The Global Top Ten, 2003–2007” on page 38.) By contrast, only one is from the United States. And the sole European representative, the global steel company ArcelorMittal (based in the Netherlands), is the product of India steelmaker Mittal’s 2006 acquisition of the European steel company Arcelor. RDE-based companies are present in many of the individual industry top-ten lists as well.

Exhibit 1 and Exhibit 2 also show the decomposition of TSR performance by industry for the sample as a whole and for the top ten companies in each industry, respectively. While, of course, results vary by industry, there are at least four broad trends of interest:

### Exhibit 1. For Most Industries, Profitable Growth Has Been a Major Driver of Value



Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: Decomposition is shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals are due to rounding.

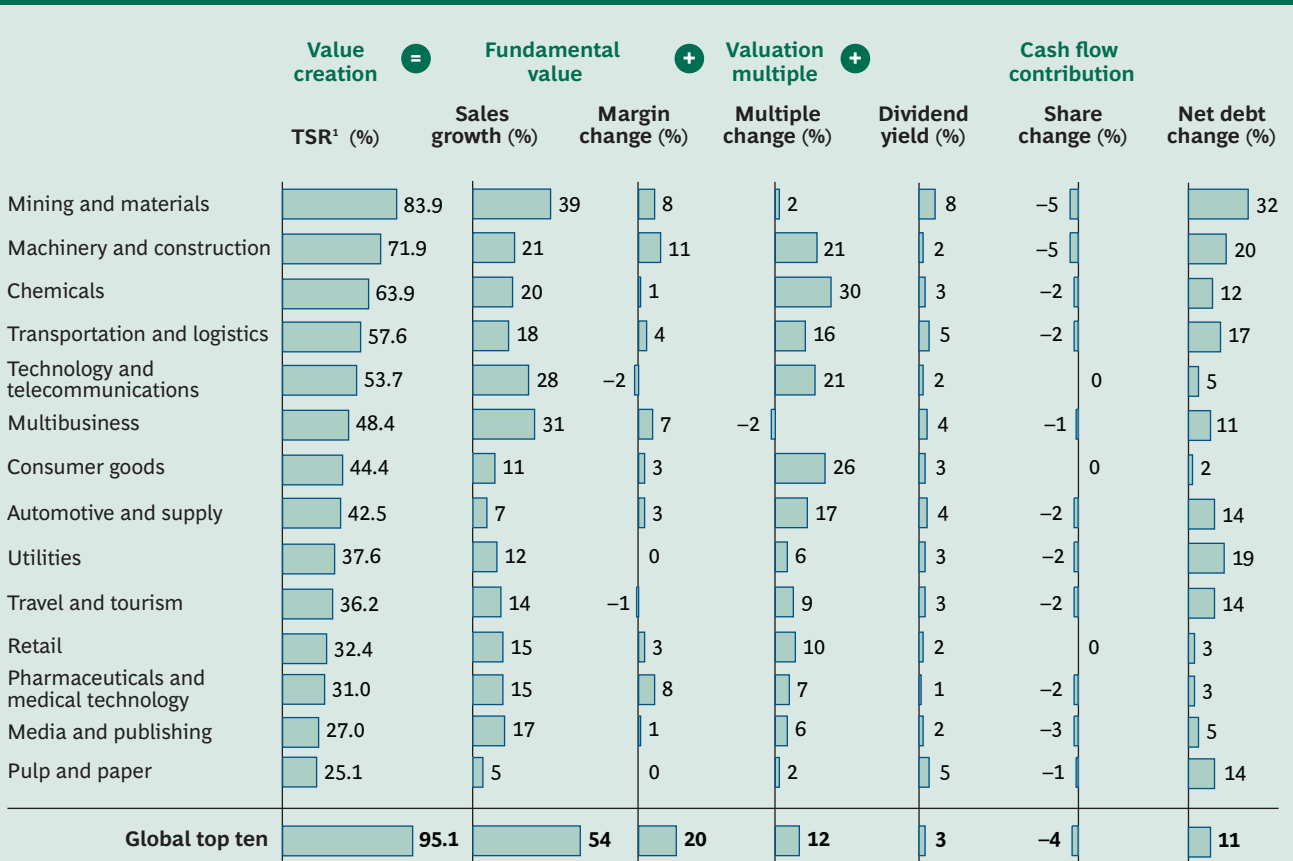
<sup>1</sup>Five-year average annual TSR (2003–2007) for weighted average of respective sample.

- ◇ As is to be expected during a period of recovery, profitable growth proved to be a major contributor to TSR. We found this to be true for the top ten companies in every industry we studied. But it was also true on average in 12 of the 14 industries in our sample. And in many industries, profitable growth was accompanied by substantial improvements in margins as well.
- ◇ Financial policies also proved to be a major source of TSR. Improved growth and margins allowed companies across our sample not only to clean up their balance sheets and pay down debt but also to increase dividends—in some cases, generating as much TSR through these financial moves as through growth itself. To take one dramatic example, the top ten performers

in the mining and materials sector (the best performing, on average, in our sample) created a full 40 percentage points of average annual TSR by means of these two financial policies.

- ◇ In no industry did share repurchases increase TSR—either on average or among the top ten performers. Indeed, in all but six industries, changes in the number of shares actually *reduced* TSR, on average. This suggests that companies’ share-repurchase programs have been offset by the issuance of new shares for options or the use of shares as equity for acquisitions.
- ◇ Finally, it is clear that multiple compression is a problem plaguing some industries. For example, in both

## Exhibit 2. The Top Ten Industry Performers Successfully Manage All Three Levels of Value Creation



Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: Decomposition is shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals are due to rounding.

<sup>1</sup>Five-year average annual TSR (2003–2007) for weighted average of respective sample.

the media and publishing sector and the pharmaceuticals and medical technology sector—the two industries with the lowest average annual TSRs in our sample—declines in multiples eroded TSR by five percentage points and four percentage points respectively. By the same token, companies in industries that

have benefited from improved multiples (top-performing sectors such as mining and materials, machinery and construction, chemicals, utilities, and automotive and supply) should start planning now for possible multiple compression in the future.

# Global Rankings

## Total Global Sample

### The Global Top Ten, 2003–2007

#	Company	Location	Industry	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
						Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Cosco Corporation	Singapore	Transportation and logistics	143.6	8.985	98	-8	20	4	-7	36	-43.4
2	Larsen & Toubro	India	Machinery and construction	112.1	29.983	22	-4	66	4	-2	26	-47.3
3	Bharti Airtel	India	Technology and telecom	110.7	47.840	78	26	0	0	0	7	-25.4
4	Kweichow Moutai	China	Consumer goods	100.7	29.719	41	12	49	2	0	-4	-39.4
5	WorleyParsons	Australia	Machinery and construction	100.4	10.953	74	-1	33	3	-8	-1	-26.6
6	Bharat Heavy Electricals	India	Machinery and construction	98.5	32.095	23	12	59	2	0	2	-46.3
7	SAIL	India	Mining and materials	98.0	29.798	17	43	-7	4	0	42	-50.0
8	DC Chemical	South Korea	Chemicals	95.6	5.299	11	-2	36	4	-3	50	40.6
9	Apple	United States	Technology and telecom	94.2	172.791	34	49	39	0	-4	-24	-15.5
10	ArcelorMittal	Netherlands	Mining and materials	93.4	110.197	76	16	-12	2	-43	54	19.5

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 644 global companies.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

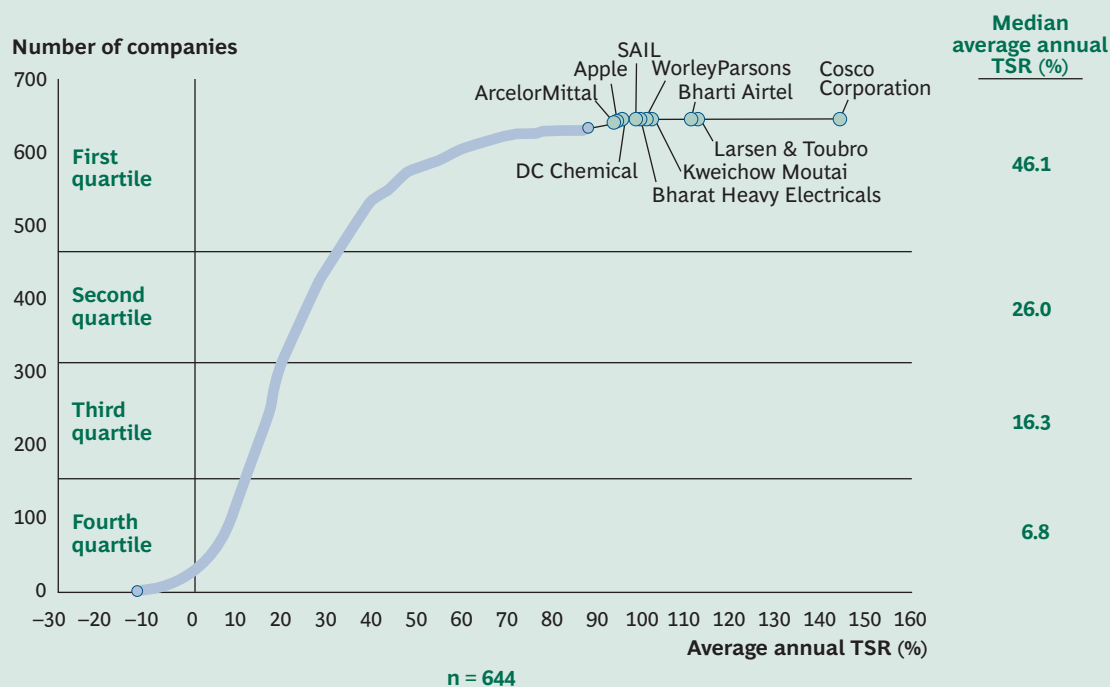
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

### Average Annual Total Shareholder Return by Quartile, 2003–2007

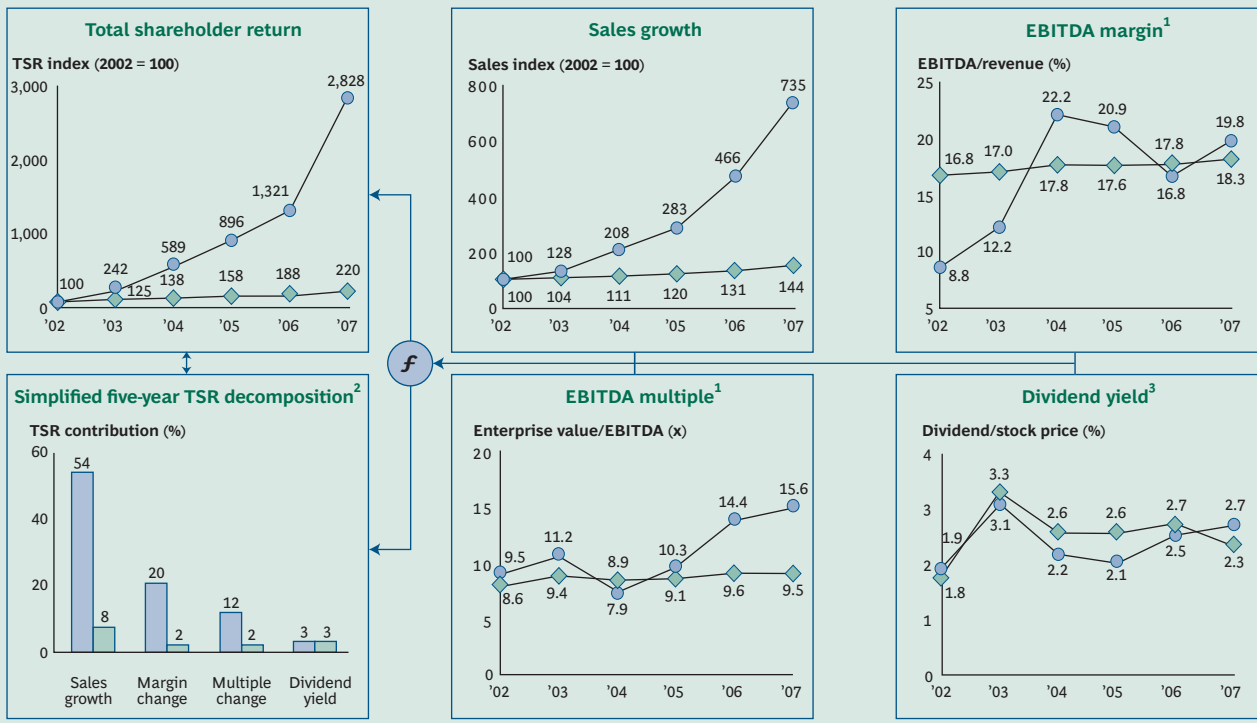


Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data; values shown for top ten companies only.



# Value Creation at the Top Ten Versus Global Sample, 2003–2007



● Global top ten    ◆ Total sample, n = 644

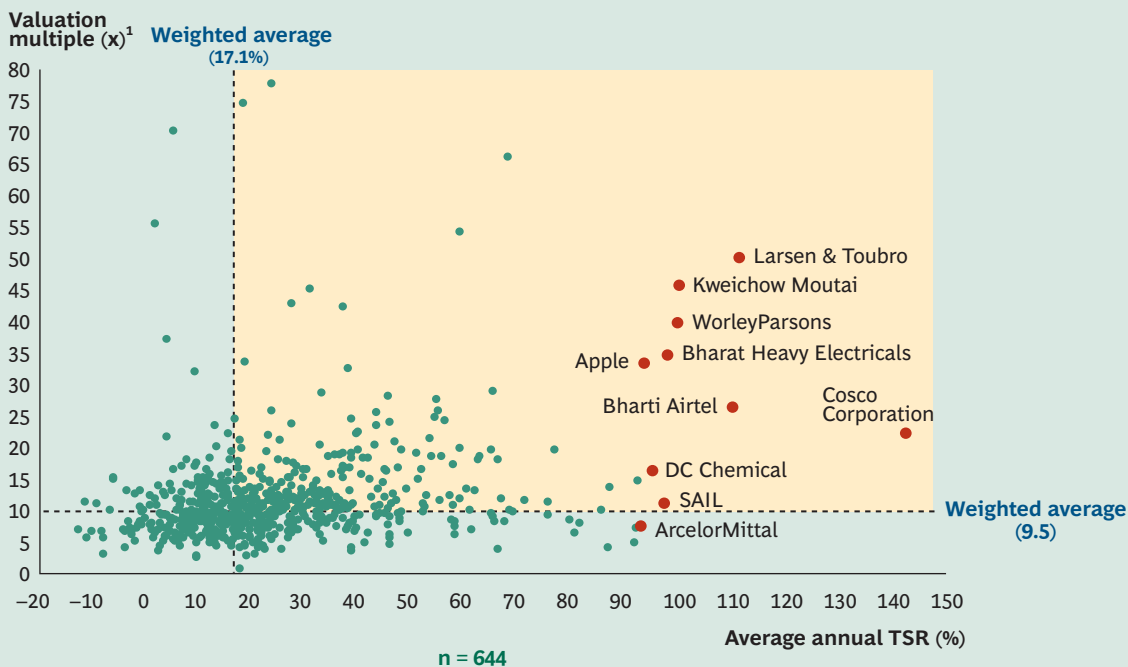
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Total-sample calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Total-sample calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Large-Cap Companies

## The Large-Cap Top Ten, 2003–2007

#	Company	Location	Industry	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
						Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Apple	United States	Technology and telecom	94.2	172.791	34	49	39	0	-4	-24	-15.5
2	ArcelorMittal	Netherlands	Mining and materials	93.4	110.197	76	16	-12	2	-43	54	19.5
3	Reliance Industries	India	Chemicals	77.2	101.859	25	-1	41	2	-5	14	-26.1
4	América Móvil	Mexico	Technology and telecom	68.9	107.050	42	3	14	1	2	7	-18.2
5	Monsanto	United States	Chemicals	65.6	60.939	15	7	37	2	-1	5	13.6
6	ABB	Switzerland	Machinery and construction	60.5	66.191	12	26	7	1	-8	23	-10.9
7	Xstrata	United Kingdom	Mining and materials	58.3	68.522	67	10	1	2	-24	3	13.8
8	China Mobile	Hong Kong	Technology and telecom	53.1	354.272	25	-1	23	4	0	2	-23.4
9	Vale do Rio Doce	Brazil	Mining and materials	52.3	161.016	37	4	4	5	-1	2	-2.5
10	Nintendo	Japan	Consumer goods	45.8	67.939	12	1	39	3	4	-13	-8.8

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 95 global companies with a market valuation greater than \$50 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

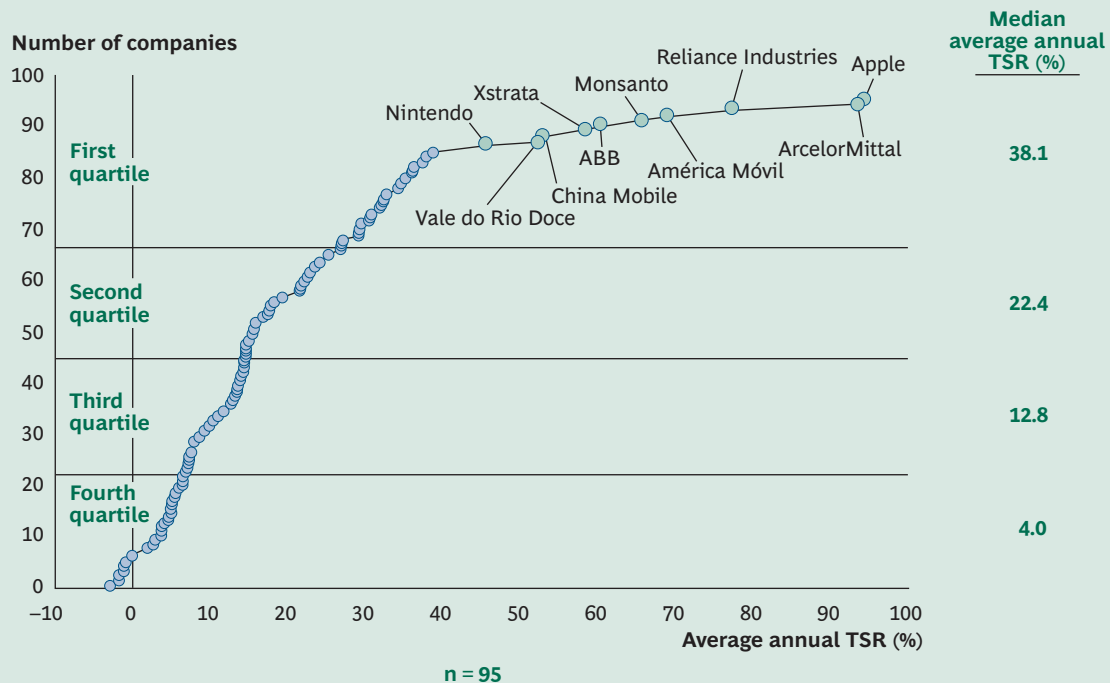
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

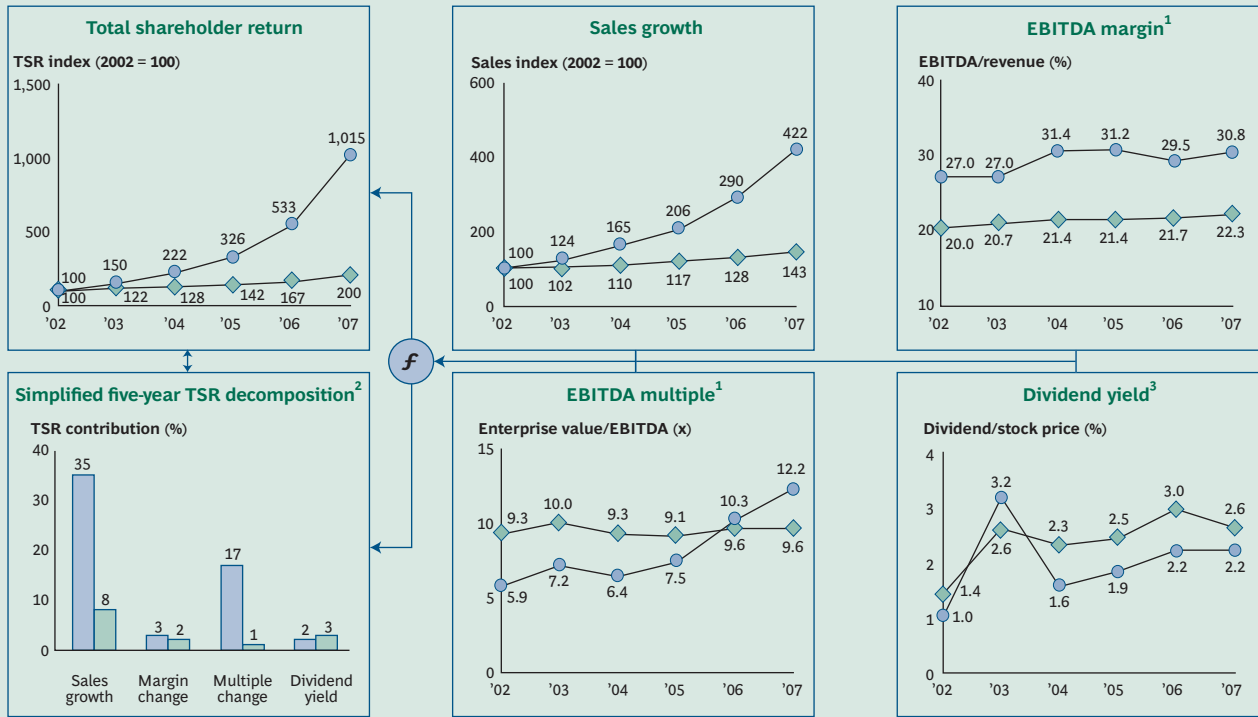
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

## Value Creation at the Top Ten Versus Large-Cap Sample, 2003–2007



● Large-cap top ten    ◆ Total sample, n = 95

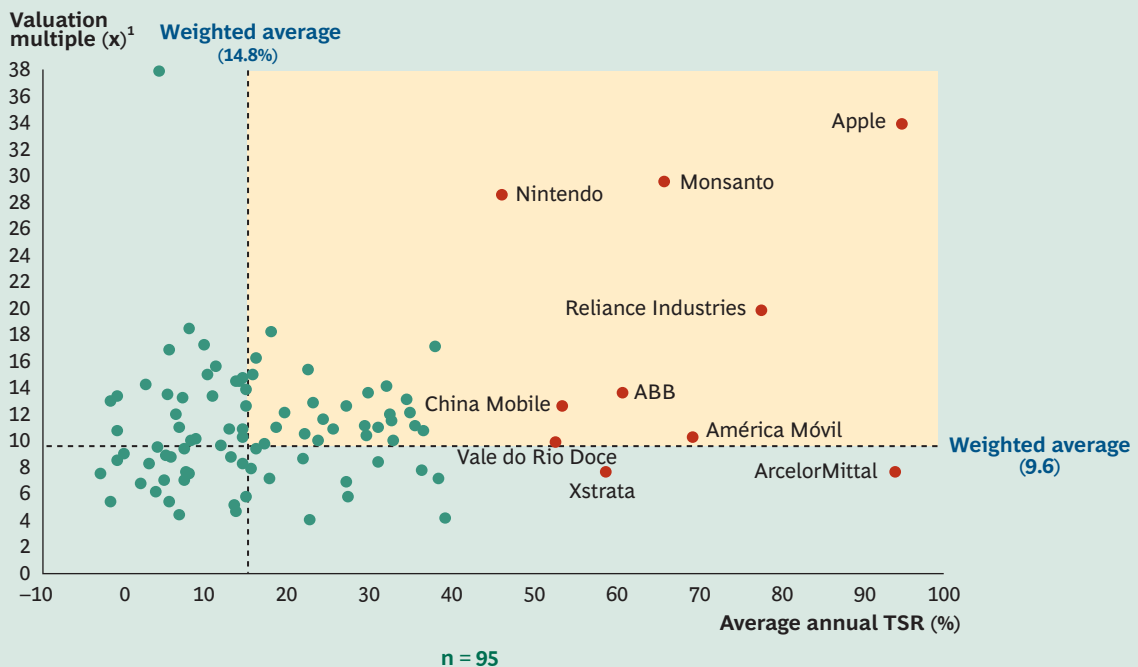
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Total-sample calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Total-sample calculation based on sample average.

## Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Industry Rankings

## Automotive and Supply

### The Automotive Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Mahindra & Mahindra	India	76.1	5.359	27	16	10	5	-1	20	-43.9
2	Astra International	Indonesia	67.3	11.767	21	6	23	5	-3	15	-27.8
3	Isuzu Motors	Japan	66.1	7.702	1	8	-2	1	-5	64	1.6
4	MAN	Germany	58.3	24.542	3	16	15	4	0	20	-36.3
5	Continental	Germany	45.9	20.981	8	4	26	3	-4	9	-25.1
6	Toyota Boshoku	Japan	43.7	6.073	57	-9	12	1	-20	3	-21.1
7	Volvo Group	Sweden	39.6	34.005	10	12	1	6	1	10	-27.7
8	Volkswagen	Germany	38.8	90.700	4	1	16	3	-1	15	18.0
9	Tata Motors	India	38.2	7.256	33	3	1	3	-4	2	-42.5
10	Paccar	United States	36.7	20.070	17	-1	11	5	1	3	-22.6

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 40 global companies with a market valuation greater than \$5 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

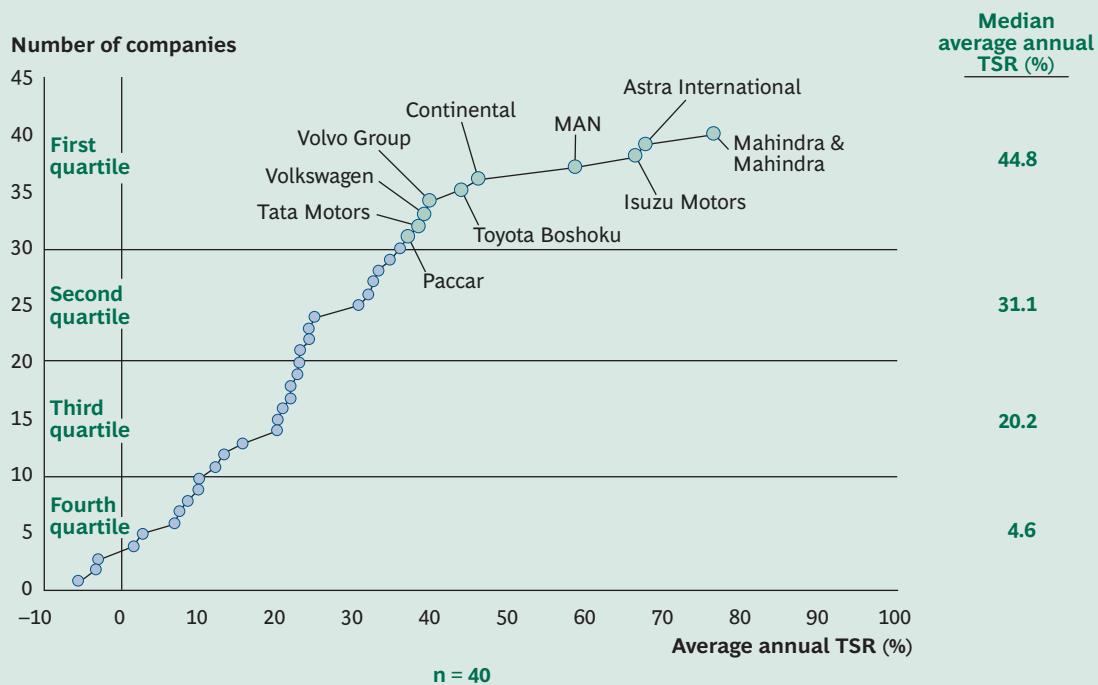
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

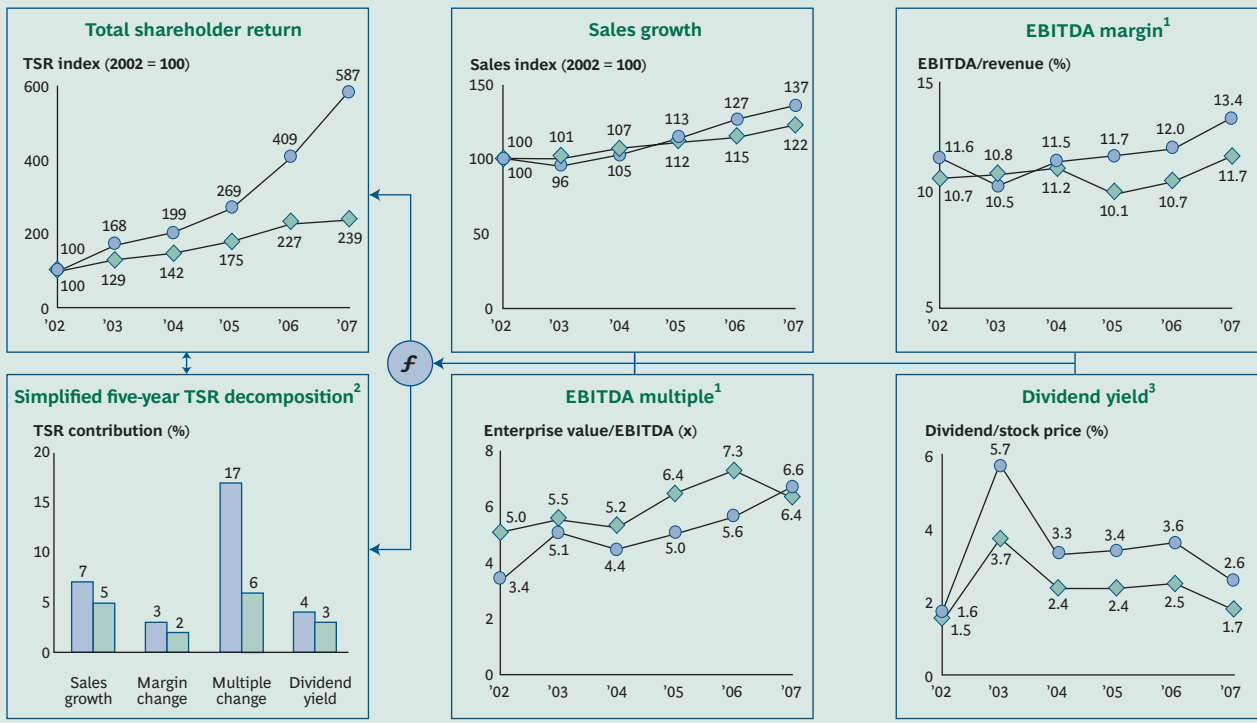
### Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Automotive top ten    ◆ Total sample, n = 40

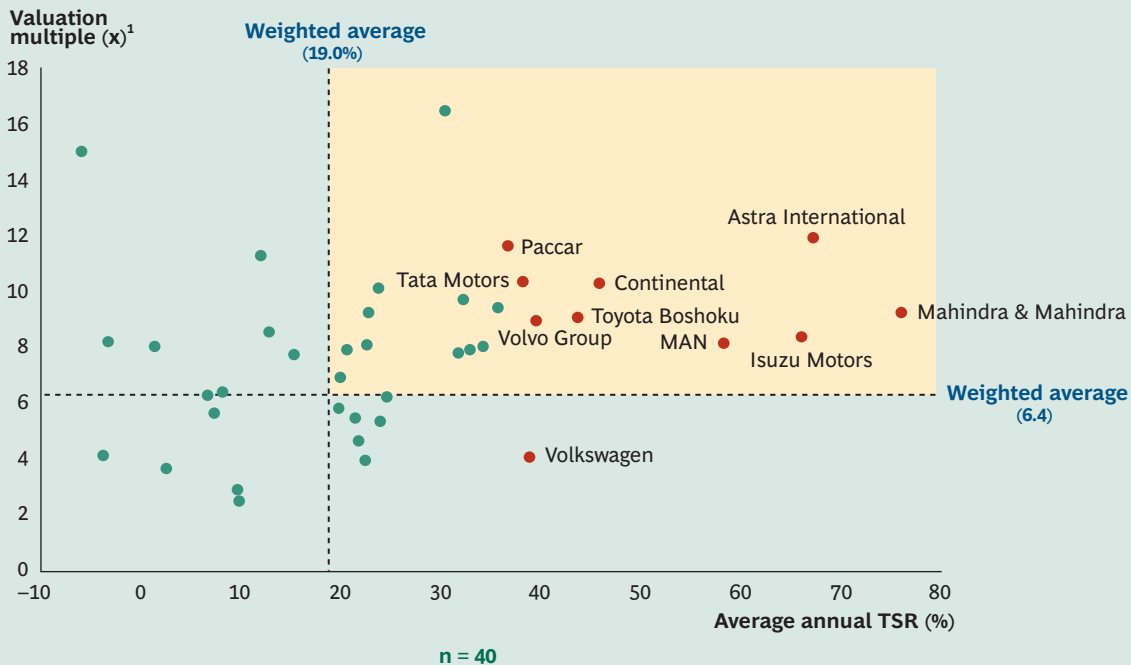
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Chemicals

## The Chemicals Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	DC Chemical	South Korea	95.6	5.299	11	-2	36	4	-3	50	40.6
2	Reliance Industries	India	77.2	101.859	25	-1	41	2	-5	14	-26.1
3	Monsanto	United States	65.6	60.939	15	7	37	2	-1	5	13.6
4	Israel Chemicals	Israel	65.2	16.391	18	5	22	6	-1	15	57.3
5	K+S	Germany	62.8	9.897	9	3	46	5	0	0	123.8
6	PotashCorp	Canada	55.2	46.002	26	15	7	1	0	6	65.1
7	Mitsubishi Gas Chemical	Japan	48.1	4.342	12	27	-16	2	2	21	-29.6
8	Sika	Switzerland	46.1	4.728	19	3	19	1	0	5	-22.7
9	Química y Minera de Chile	Chile	44.9	4.757	17	3	15	3	0	6	174.4
10	Braskem	Brazil	41.4	3.502	22	-17	6	1	-10	39	-7.4

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 74 global companies with a market valuation greater than \$3 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

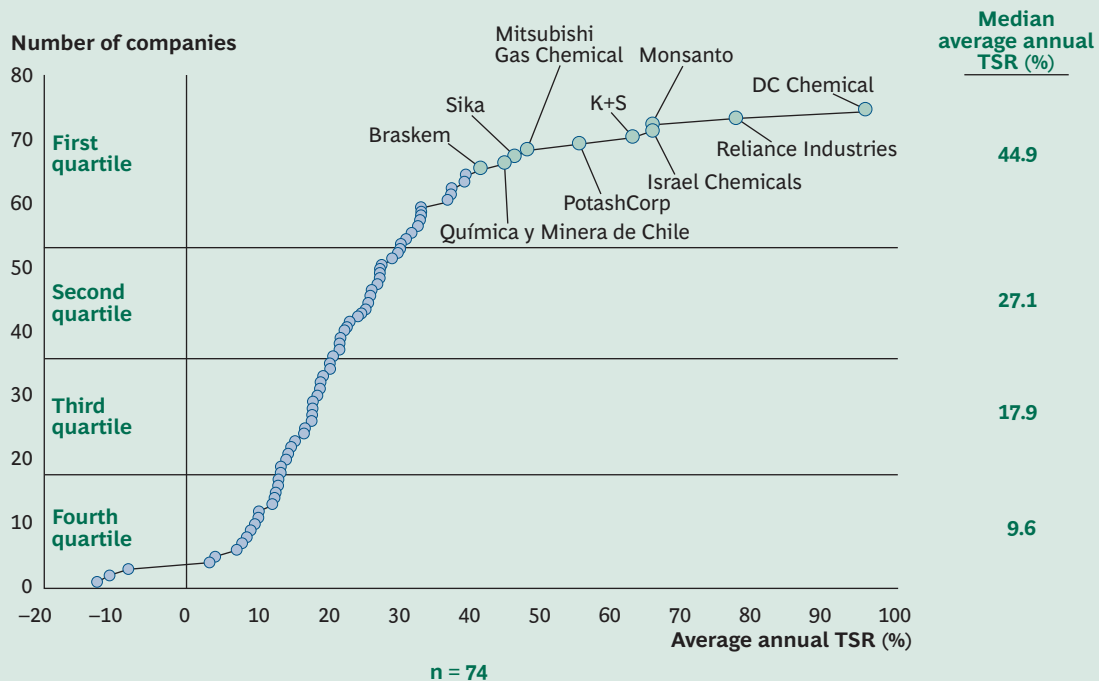
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

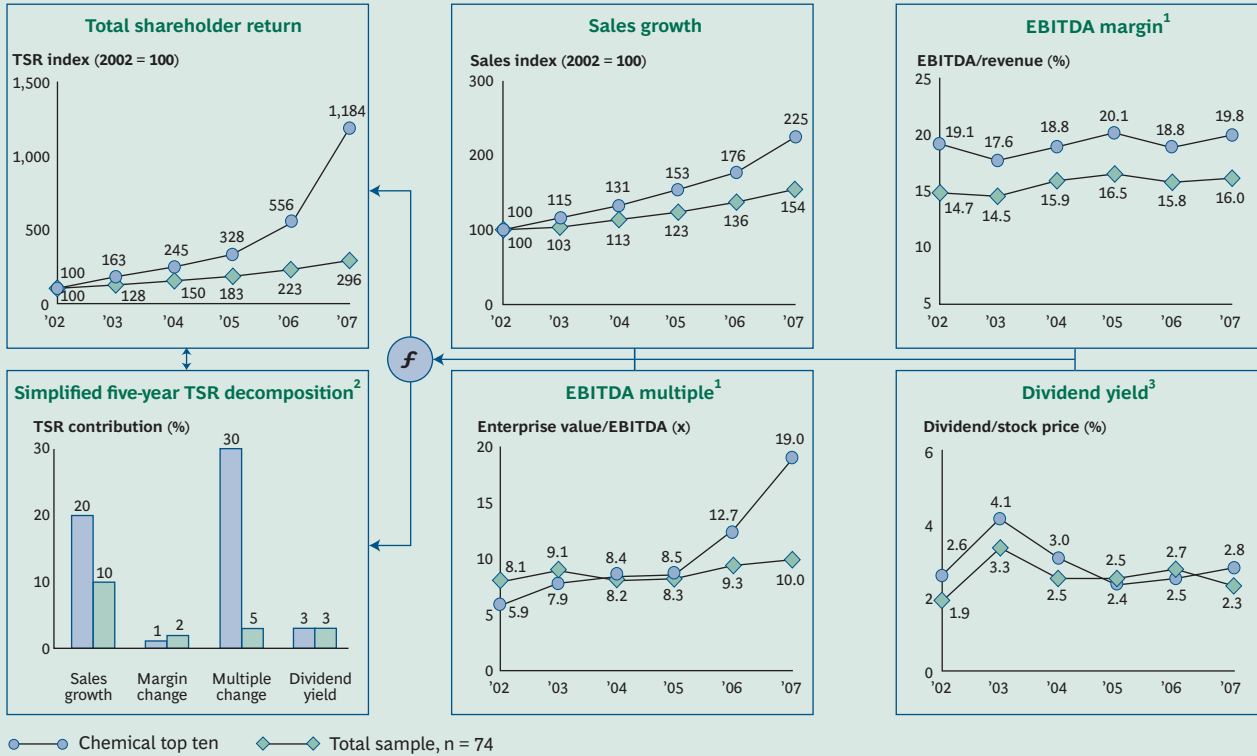
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



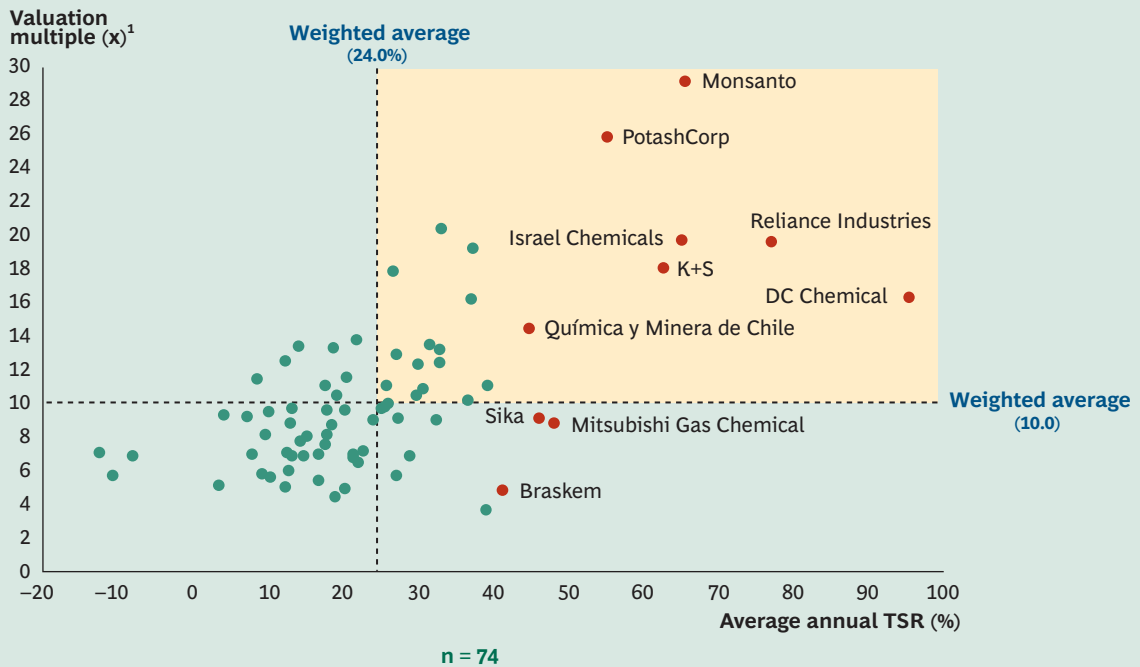
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Consumer Goods

## The Consumer Goods Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Kweichow Moutai	China	100.7	29.719	41	12	49	2	0	-4	-39.4
2	Wuliangye Yibin	China	68.3	23.636	7	13	49	1	0	-1	-59.9
3	Garmin	United States	47.2	21.047	46	-6	7	1	0	-1	-55.8
4	Nintendo	Japan	45.8	67.939	12	1	39	3	4	-13	-8.8
5	KT&G	South Korea	43.7	11.140	10	3	13	7	4	8	12.9
6	Orkla	Norway	42.5	20.090	9	-3	22	8	0	7	-35.8
7	ITC	India	39.1	20.073	21	-2	17	3	0	1	-14.1
8	Bunge	United States	38.6	14.112	23	-9	16	2	-4	12	-7.2
9	Nikon	Japan	34.8	13.814	12	14	-1	1	-1	10	-19.5
10	Japan Tobacco	Japan	34.7	54.778	1	6	19	1	2	5	-31.9

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 70 global companies with a market valuation greater than \$10 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

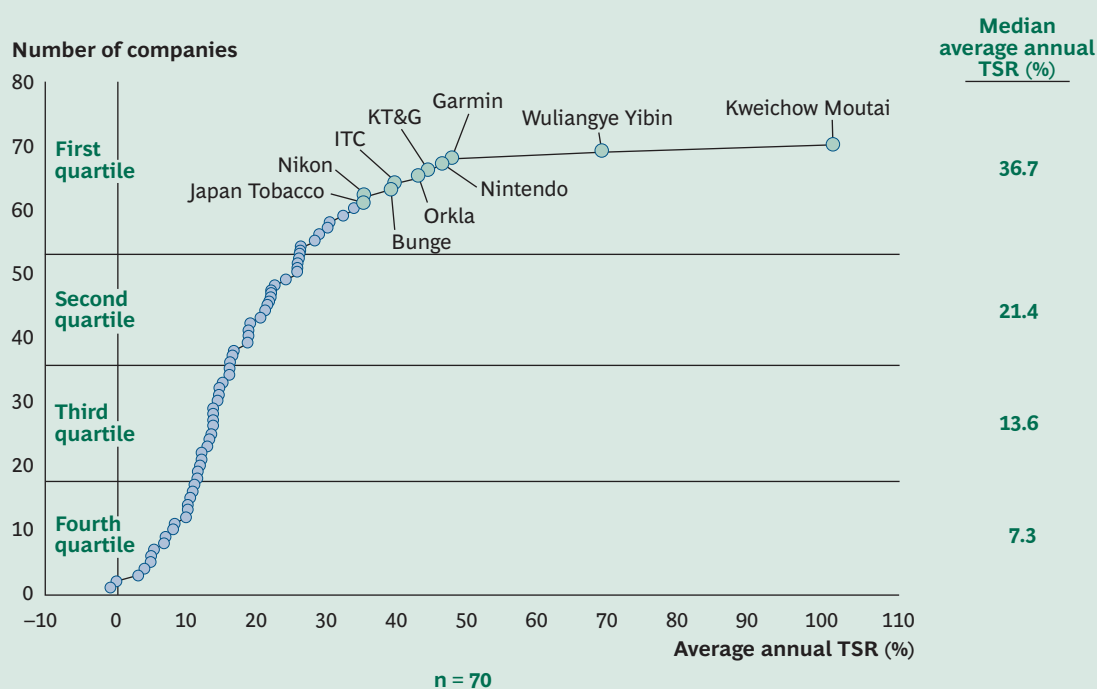
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

## Average Annual Total Shareholder Return by Quartile, 2003–2007

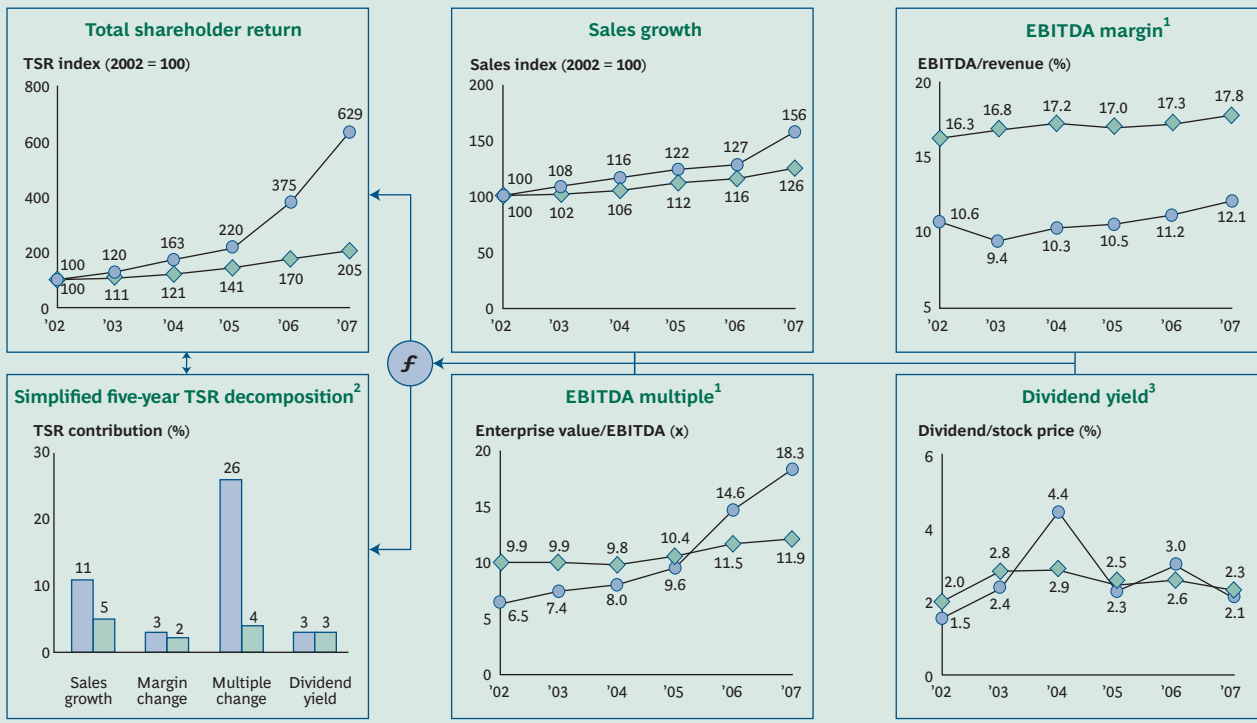


Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.



# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Consumer goods top ten    ◆ Total sample, n = 70

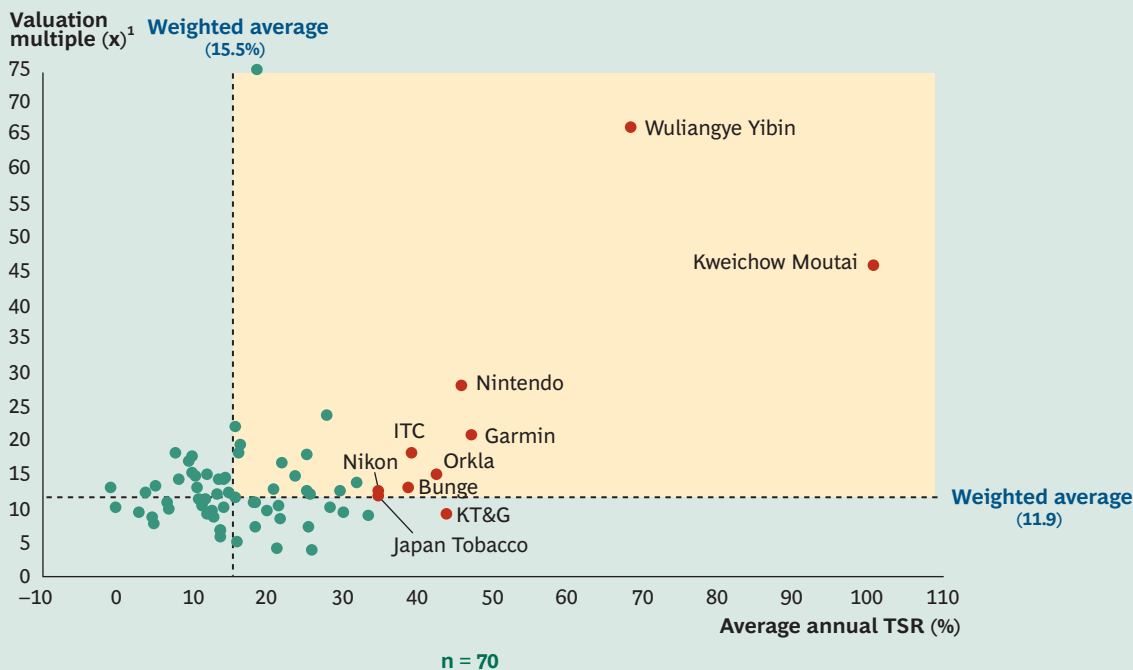
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Machinery and Construction

## The Machinery and Construction Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Larsen & Toubro	India	112.1	29.983	22	-4	66	4	-2	26	-47.3
2	WorleyParsons	Australia	100.4	10.953	74	-1	33	3	-8	-1	-26.6
3	Bharat Heavy Electricals	India	98.5	32.095	23	12	59	2	0	2	-46.3
4	Hyundai Heavy Industries	South Korea	92.6	29.410	20	9	7	5	-13	64	-26.8
5	Doosan Heavy Industries	South Korea	87.5	11.589	35	6	35	2	-4	13	-21.4
6	Precision Castparts	United States	63.2	19.031	19	3	33	0	-5	13	-30.5
7	ABB	Switzerland	60.5	66.191	12	26	7	1	-8	23	-10.9
8	Cummins	United States	58.2	12.463	19	13	1	3	-4	26	3.3
9	Enka	Turkey	55.9	15.739	38	-9	26	1	0	0	-8.0
10	Vestas Wind Systems	Denmark	54.7	19.966	31	4	22	0	-8	6	12.3

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 55 global companies with a market valuation greater than \$10 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

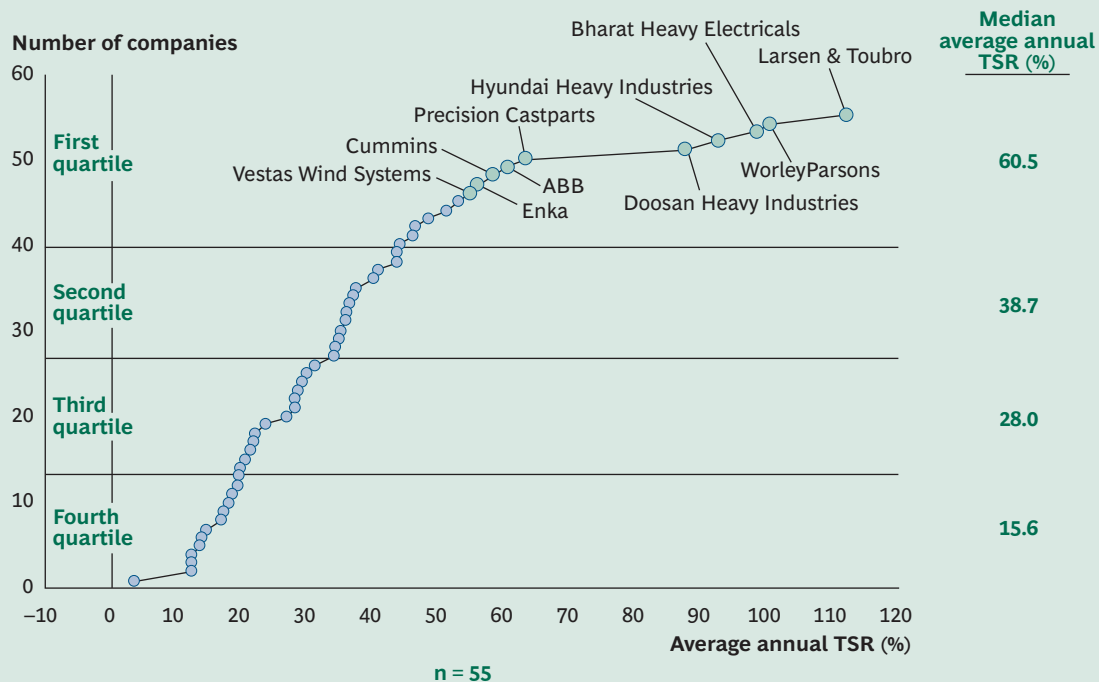
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

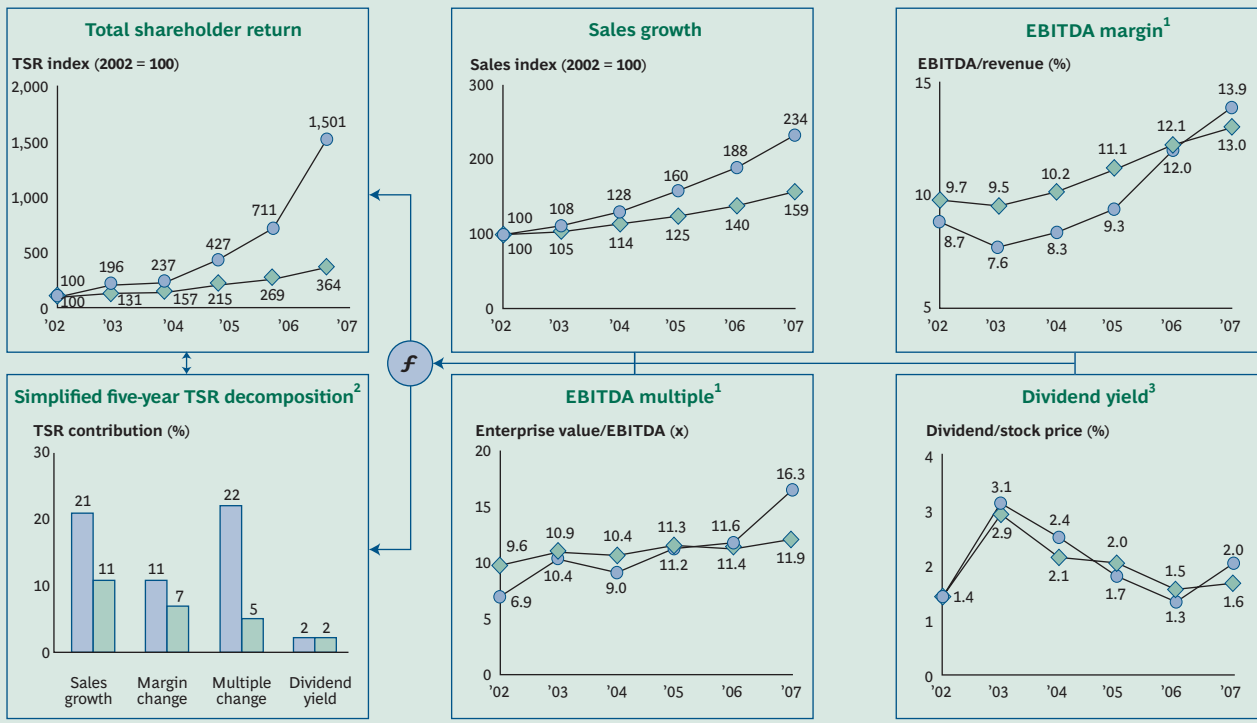
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Machinery and construction top ten    ◆ Total sample, n = 55

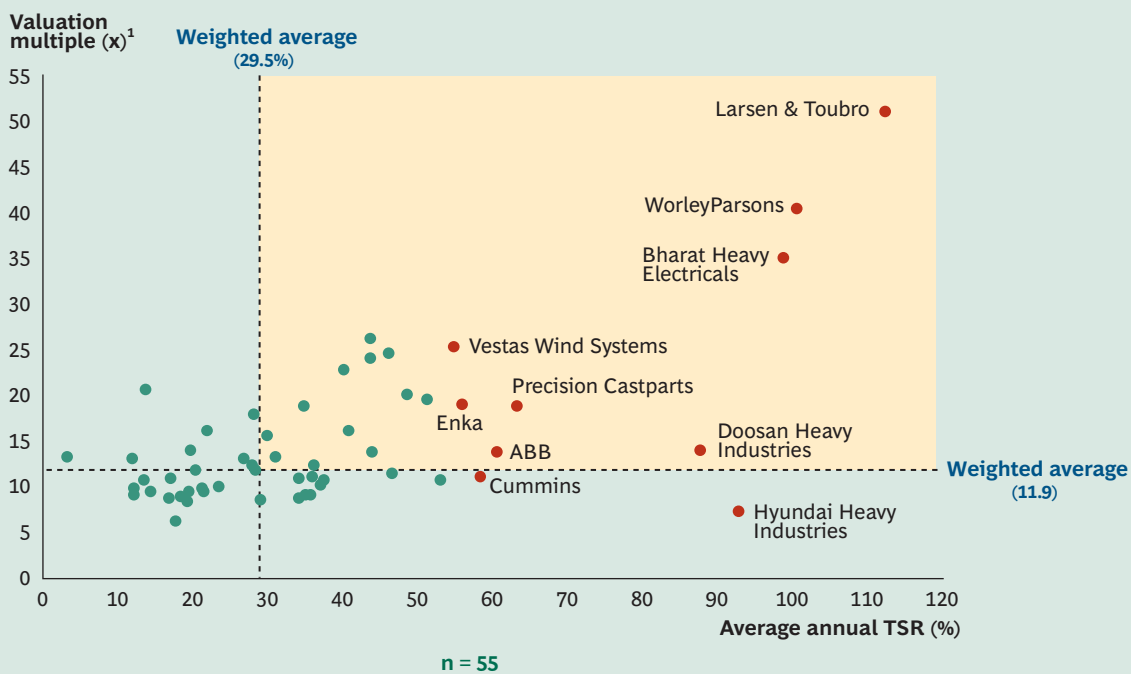
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Media and Publishing

## The Media and Publishing Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Naspers	South Africa	48.5	8.186	15	18	0	2	-15	29	5.6
2	Modern Times Group	Sweden	47.7	4.671	16	15	10	0	0	7	-19.3
3	Net Serviços de Comunicação	Brazil	37.5	4.086	19	12	-2	0	-10	18	-6.4
4	Grupo Televisa	Mexico	32.4	11.719	11	8	7	3	-1	5	-5.1
5	Informa	United Kingdom	28.4	3.895	30	9	10	3	-21	-3	-7.6
6	Zee Entertainment	India	27.8	3.611	7	-4	22	1	-1	3	-38.2
7	SES	Luxembourg	27.0	14.037	4	-4	15	4	2	6	-8.4
8	Shaw Communications	Canada	25.6	10.332	9	5	0	2	2	9	-10.4
9	ProSiebenSat.1 Media	Germany	24.1	5.185	7	19	0	2	-2	-4	-54.2
10	Yahoo!	United States	23.3	30.955	43	-1	-15	0	-2	-1	-11.2

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 44 global companies with a market valuation greater than \$3 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

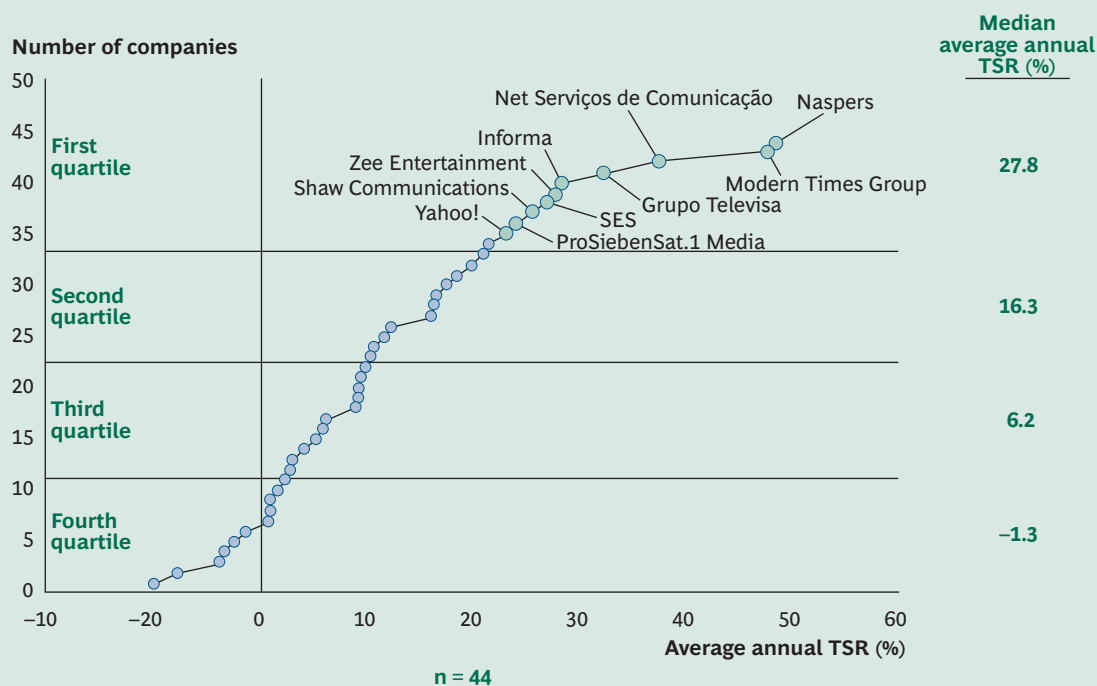
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

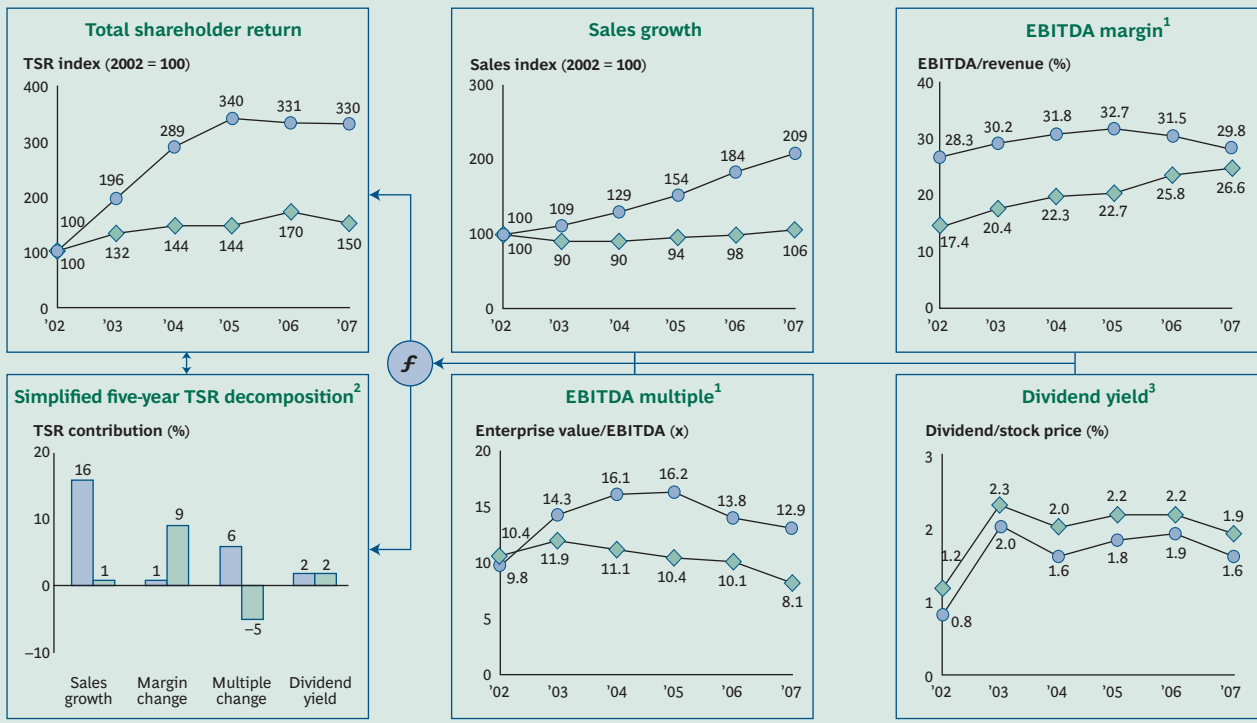
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Media and publishing top ten    ◆ Total sample, n = 44

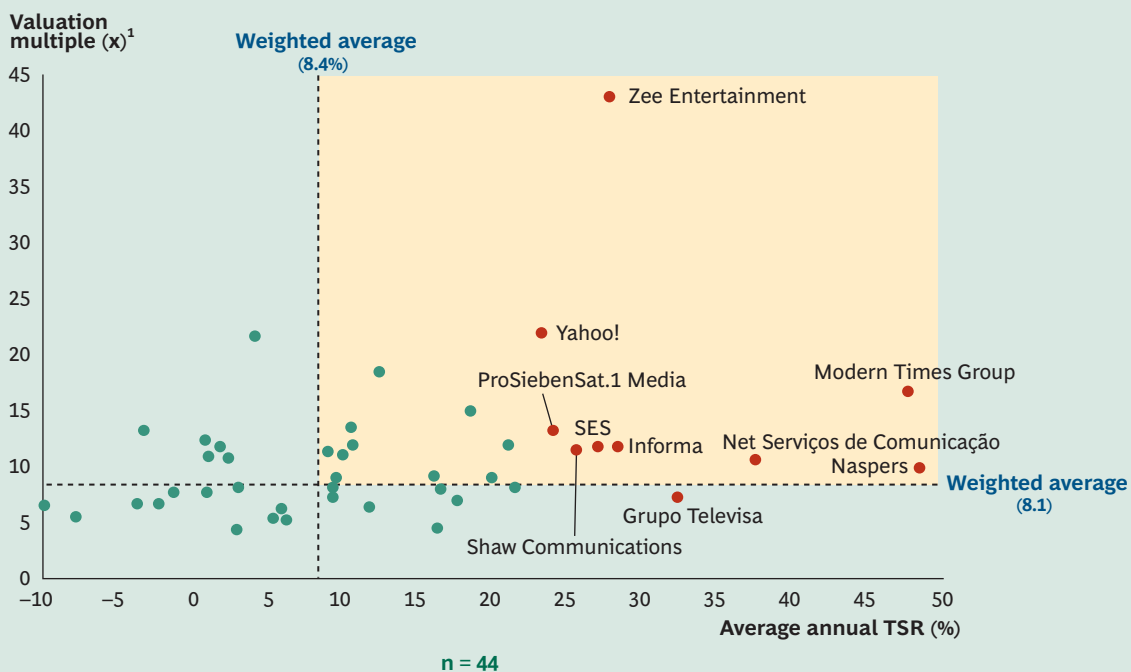
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Mining and Materials

## The Mining and Materials Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	SAIL	India	98.0	29.798	17	43	-7	4	0	42	-50.0
2	ArcelorMittal	Netherlands	93.4	110.197	76	16	-12	2	-43	54	19.5
3	Usinas Sider Minas	Brazil	92.2	15.066	18	1	2	15	0	57	46.8
4	Grupo México	Mexico	87.2	16.148	25	24	-10	6	-4	45	5.1
5	Siderúrgica Nacional	Brazil	85.9	22.708	20	2	22	23	3	17	39.3
6	Southern Copper	United States	82.1	30.999	58	18	3	11	-11	3	4.4
7	Eramet	France	81.0	13.082	15	37	4	6	-1	19	82.0
8	CHALCO	China	76.0	29.811	40	1	21	7	-4	12	-43.9
9	Sumitomo Metals	Japan	67.9	20.790	4	15	-6	4	-4	55	-8.9
10	Severstal	Russia	65.6	22.855	51	-6	30	3	-11	-1	16.4

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 49 global companies with a market valuation greater than \$10 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

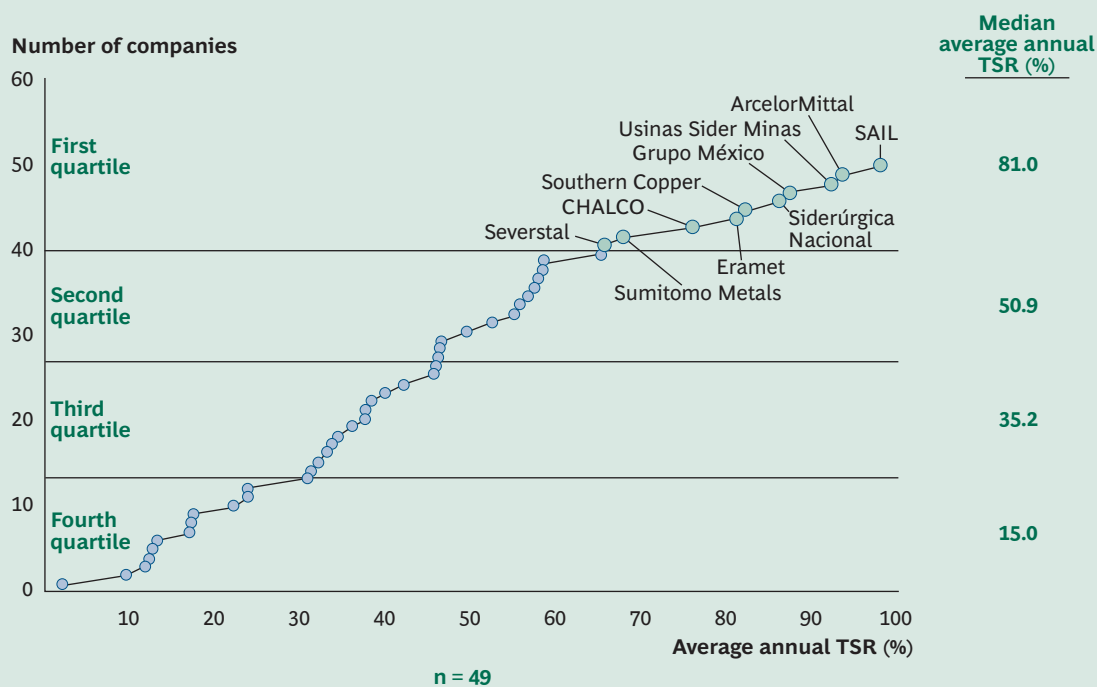
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

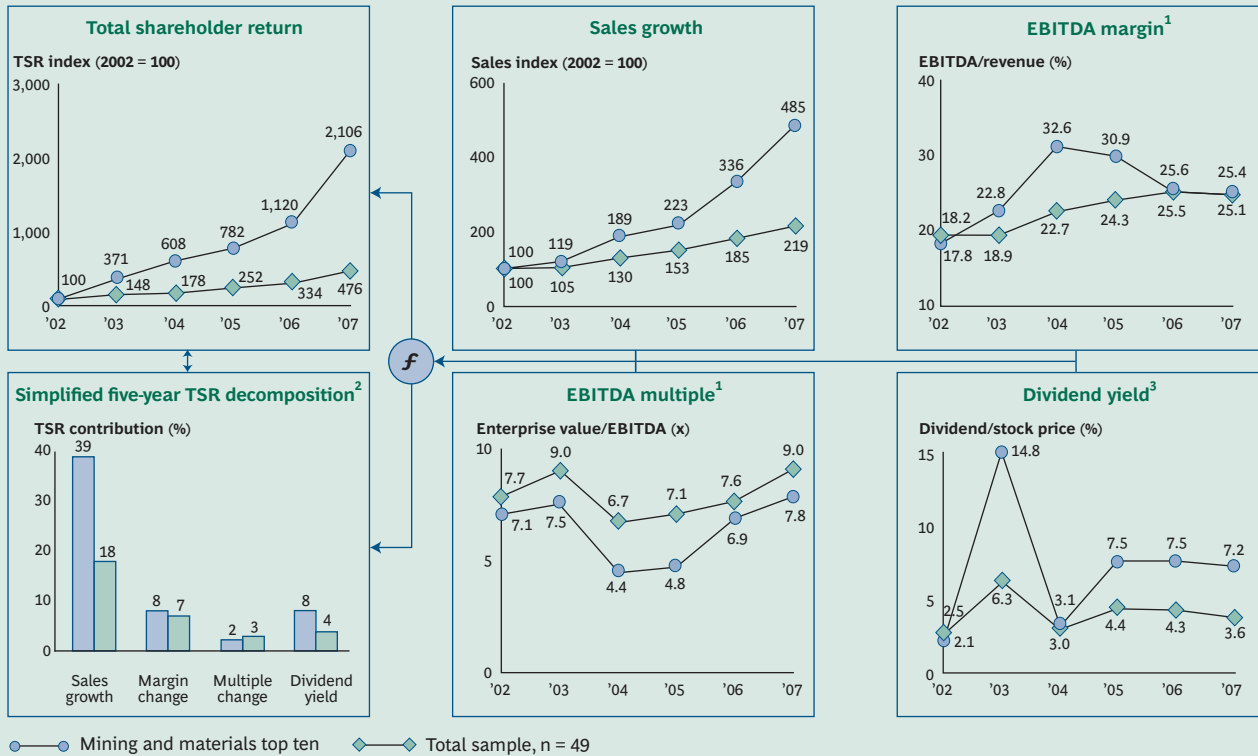
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



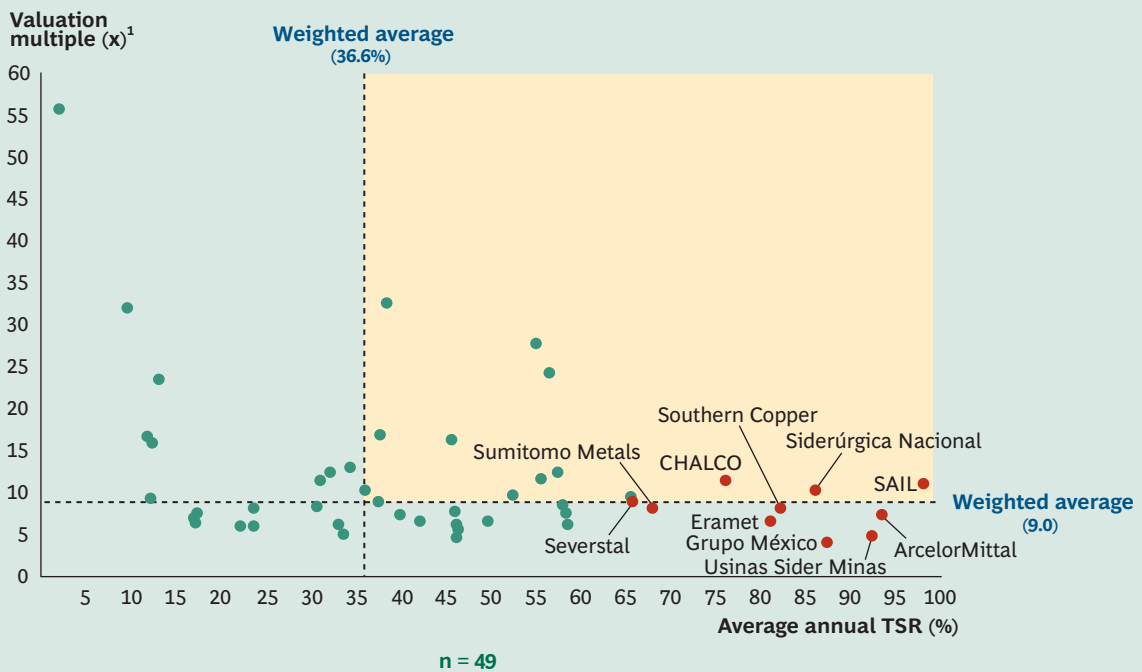
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Multibusiness

## The Multibusiness Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	WEG	Brazil	66.7	8.744	27	0	31	7	0	2	-19.3
2	LG Group	South Korea	66.5	12.827	66	17	-28	3	-22	31	-2.9
3	Daewoo E&C	South Korea	59.2	8.555	13	1	25	4	-13	29	-36.0
4	Keppel	Singapore	54.0	14.315	29	-9	8	5	-1	22	-9.8
5	Sembcorp	Singapore	51.4	7.187	17	8	4	4	0	19	-25.3
6	Ibiden	Japan	44.2	10.076	15	14	12	1	-3	5	-49.8
7	China Resources Enterprise	Hong Kong	43.4	10.247	13	-1	26	5	-3	3	-32.8
8	Toyota Tsusho	Japan	42.8	9.316	24	8	-2	1	-4	14	-17.2
9	Jardine Matheson	Singapore	38.9	17.146	23	5	1	4	0	5	13.7
10	Grupo Carso	Mexico	38.6	8.881	5	-2	14	2	2	18	18.0

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 33 global companies with a market valuation greater than \$7 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

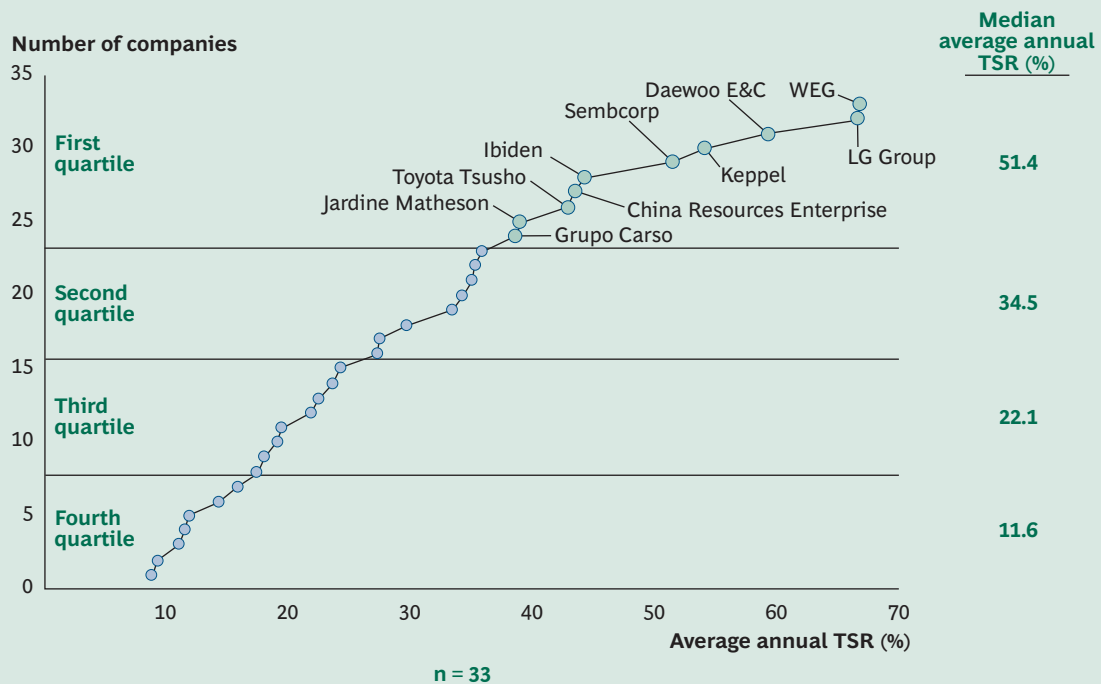
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

## Average Annual Total Shareholder Return by Quartile, 2003–2007

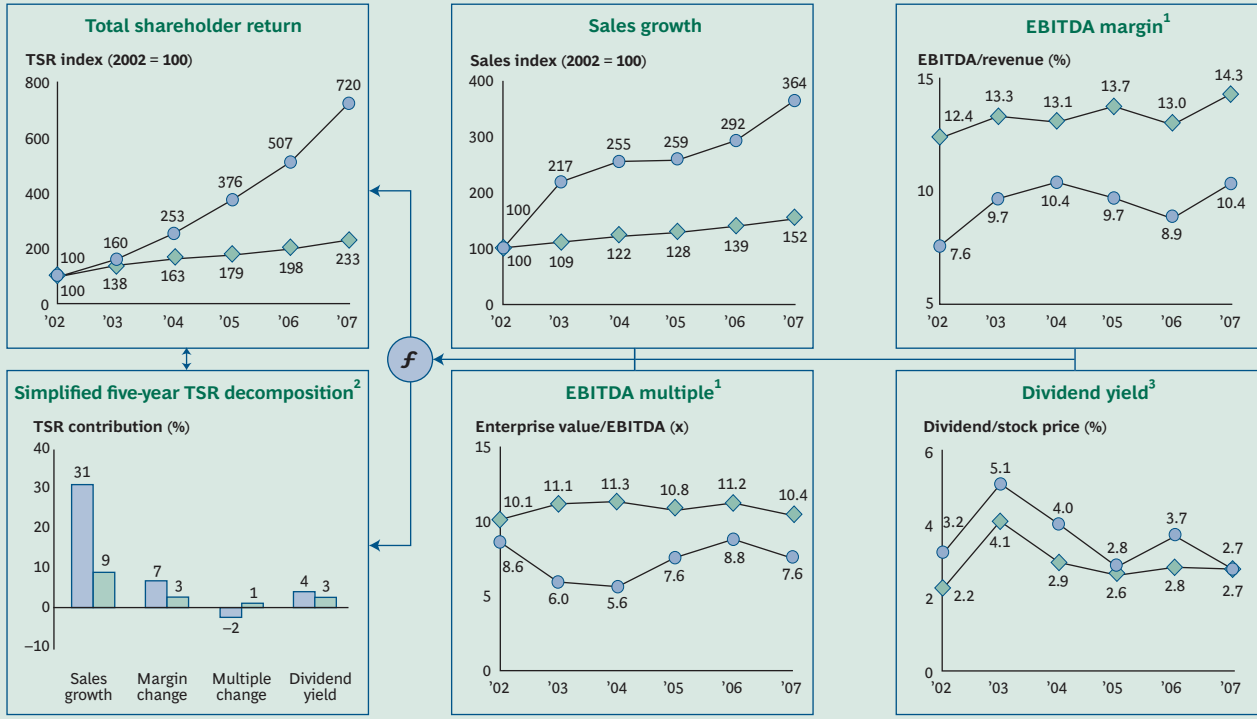


Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.



# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



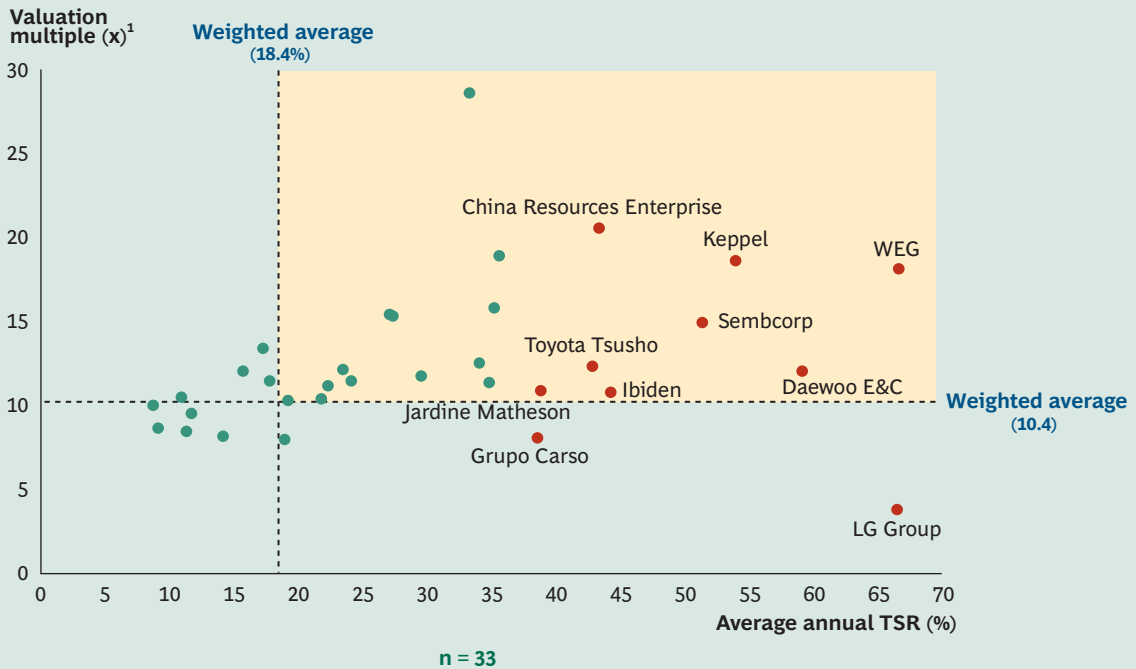
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Pharmaceuticals and Medical Technology

## The Pharmaceuticals and Medical Technology Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	CSL	Australia	40.2	17.481	21	6	12	2	-3	2	-1.3
2	Gilead Sciences	United States	40.2	42.904	50	19	-24	0	-4	-1	15.1
3	Fresenius	Germany	39.4	12.856	9	3	9	2	-4	20	-1.8
4	Genentech	United States	32.2	70.558	34	8	-8	0	-1	-1	13.2
5	Merck KGaA	Germany	32.0	28.338	-2	17	9	3	-4	10	5.1
6	Novo Nordisk	Denmark	28.8	40.800	12	0	12	2	2	1	-6.2
7	Fresenius Medical Care	Germany	24.3	15.573	15	2	2	2	0	3	-2.5
8	Shire	United Kingdom	24.0	12.713	16	-33	49	0	-3	-6	-28.1
9	Becton Dickinson	United States	23.8	20.380	10	2	6	2	1	3	-2.1
10	Thermo Fisher Scientific	United States	23.4	23.951	33	7	2	0	-18	-1	-3.4

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 42 global companies with a market valuation greater than \$10 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

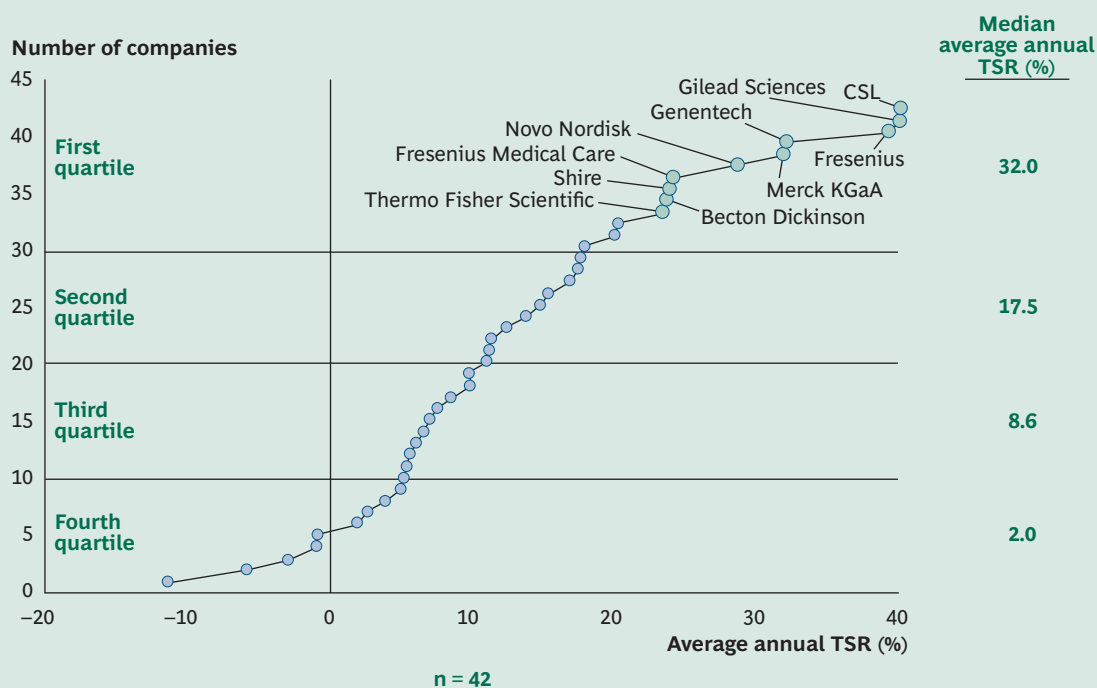
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

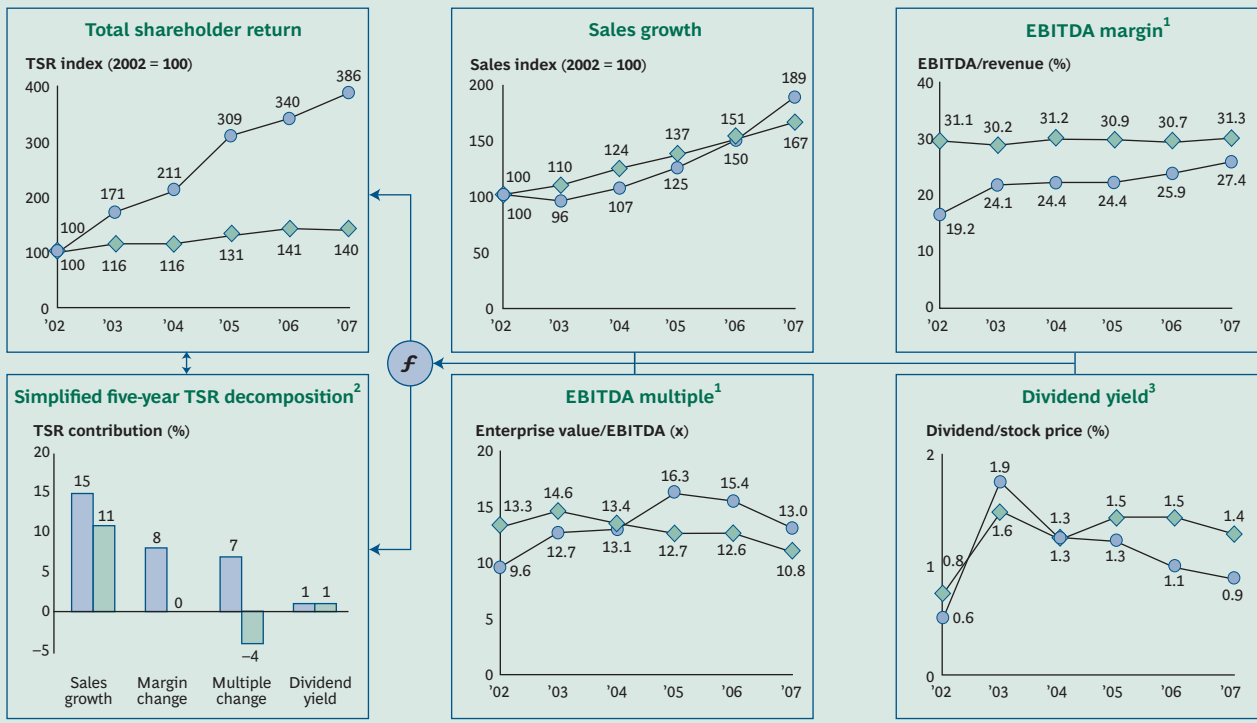
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Pharmaceuticals and medical technology top ten    ◆ Total sample, n = 42

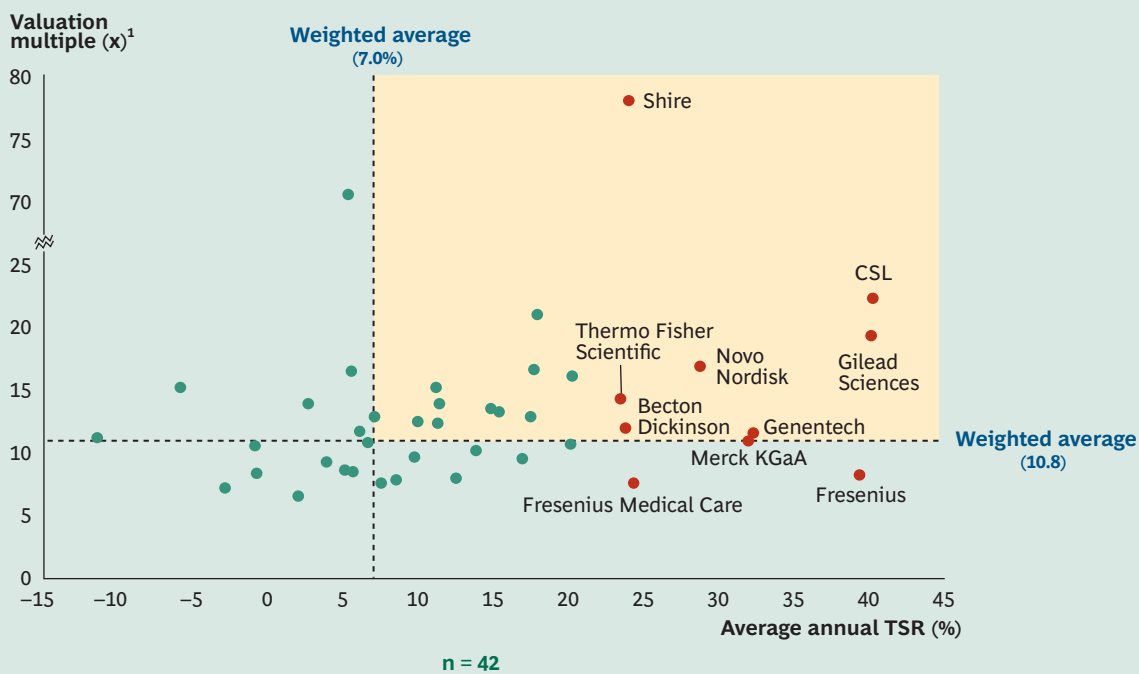
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Pulp and Paper

## The Pulp and Paper Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Klabin	Brazil	52.3	3.352	0	-5	24	7	0	26	-7.2
2	Suzano Papel e Celulose	Brazil	47.3	5.101	30	-9	21	6	-11	9	-10.5
3	Empresas CMPC	Chile	26.7	7.551	13	2	6	3	0	3	-12.9
4	Grupo Empresarial ENCE	Spain	25.3	1.859	6	0	11	3	-6	10	-30.0
5	Votorantim Celulose e Papel	Brazil	23.4	6.215	10	-5	6	5	-1	8	-20.5
6	Rengo	Japan	22.9	1.588	2	2	0	2	0	17	2.4
7	Aracruz Celulose	Brazil	19.8	7.475	14	0	-2	6	0	2	-6.7
8	Mayr-Melnhof Karton	Austria	18.7	2.385	7	-3	9	3	0	4	-17.0
9	Temple-Inland	United States	18.3	2.213	-3	-12	-15	7	0	40	-45.2
10	Portucel	Portugal	17.5	2.502	1	-2	5	3	0	10	-7.5

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 24 global companies with a market valuation greater than \$1.5 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

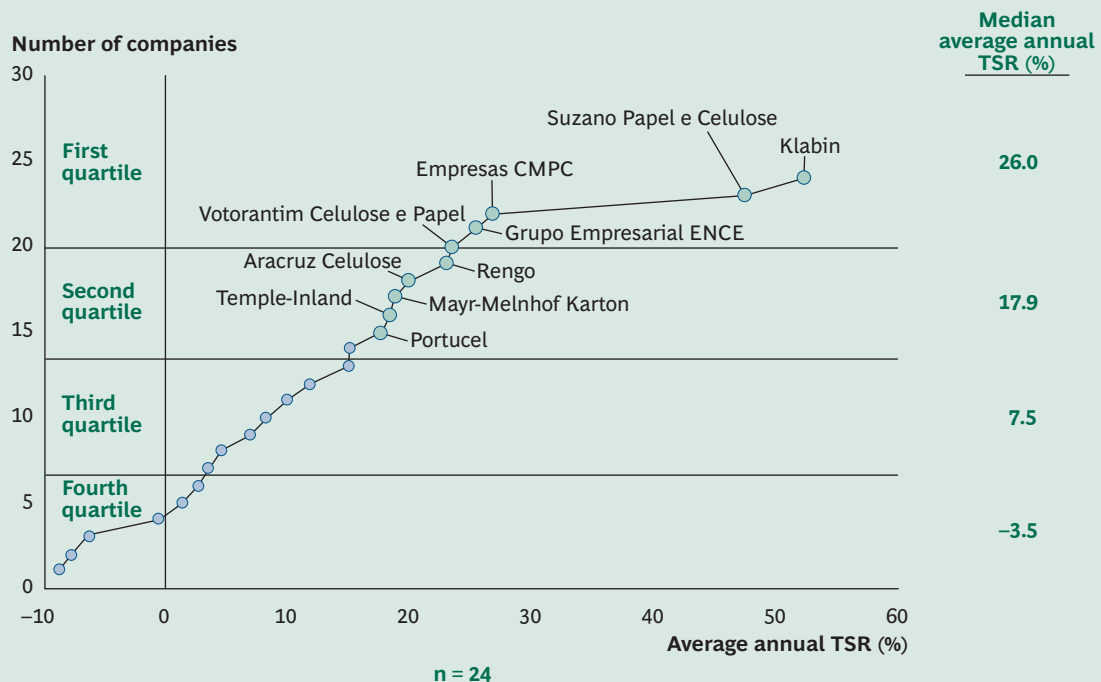
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

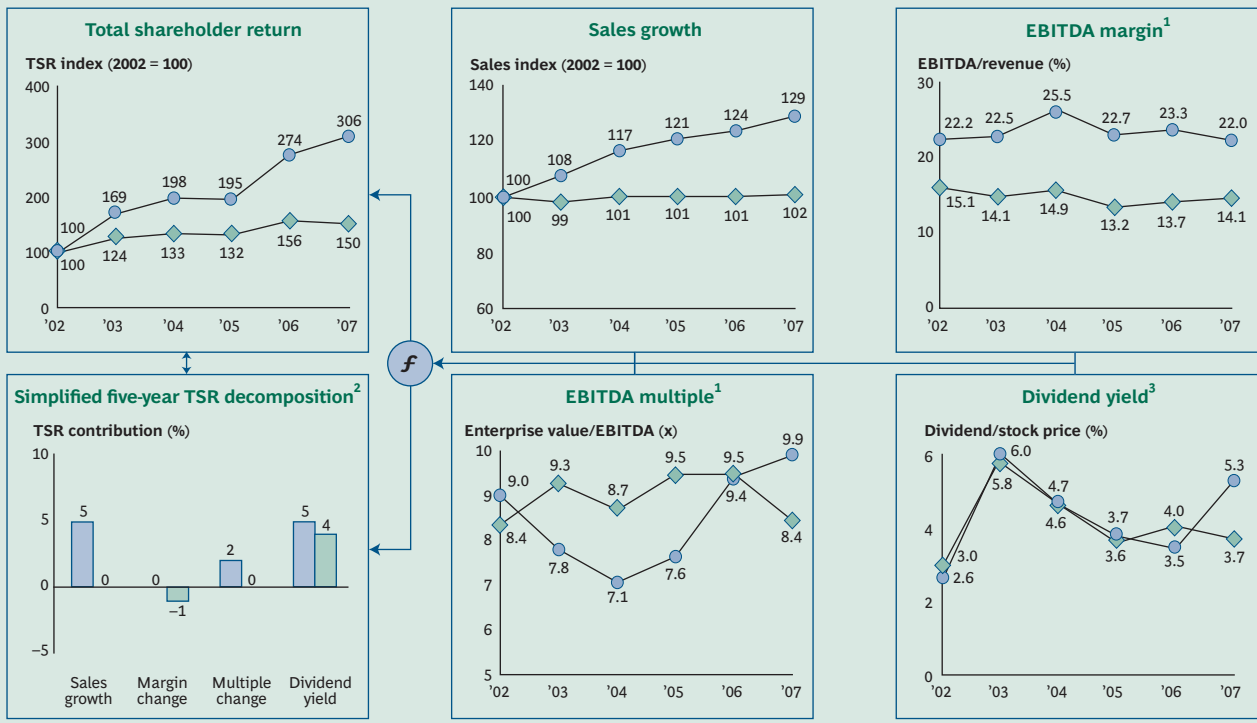
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Pulp and paper top ten    ◆ Total sample, n = 24

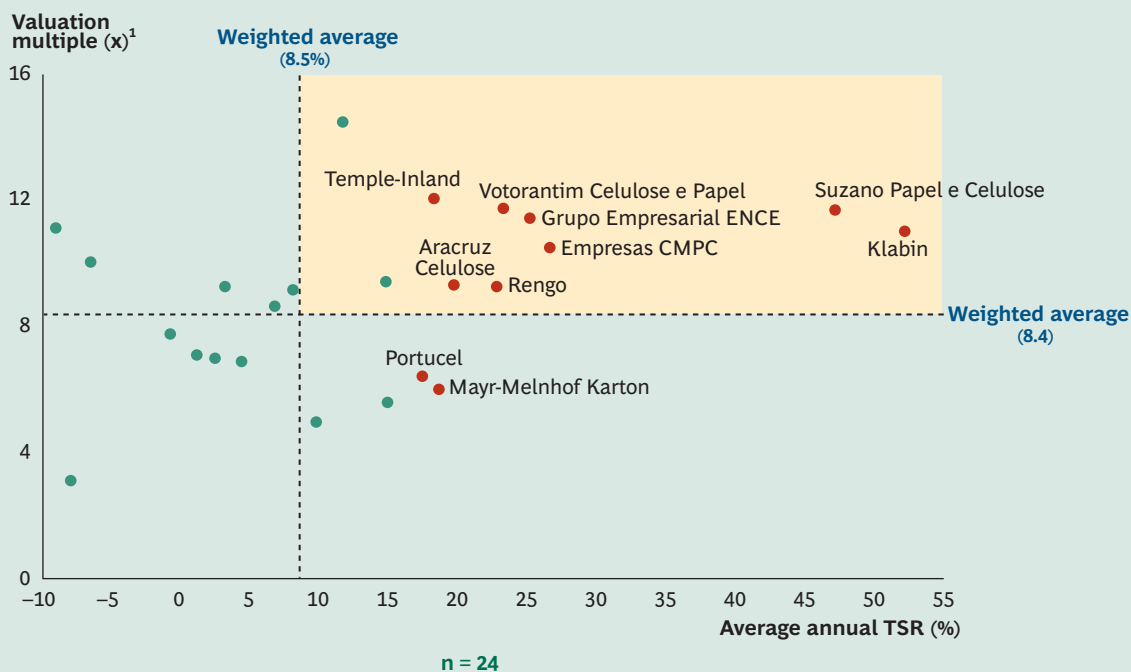
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Retail

## The Retail Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Esprit Holdings	Hong Kong	59.4	18.313	30	7	17	5	-1	1	-29.5
2	Yamada Denki	Japan	38.9	10.913	22	3	18	1	-3	-2	-40.6
3	Shinsegae	South Korea	37.5	14.628	14	0	23	0	-4	5	-22.5
4	Amazon.com	United States	37.4	39.928	32	4	0	0	-2	4	-20.8
5	S.A.C.I. Falabella	Chile	36.9	11.617	28	-2	11	3	-4	1	-7.9
6	McDonald's	United States	32.3	68.630	9	8	3	3	2	7	-3.3
7	Woolworths	Australia	28.3	35.706	12	6	8	4	-3	0	-26.9
8	Wal-Mart de México	Mexico	27.7	29.261	13	5	8	2	1	-2	9.2
9	Best Buy	United States	27.7	25.306	16	1	11	1	0	-2	-24.4
10	Yum! Brands	United States	26.9	19.097	7	0	12	1	4	4	-7.6

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 40 global companies with a market valuation greater than \$10 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

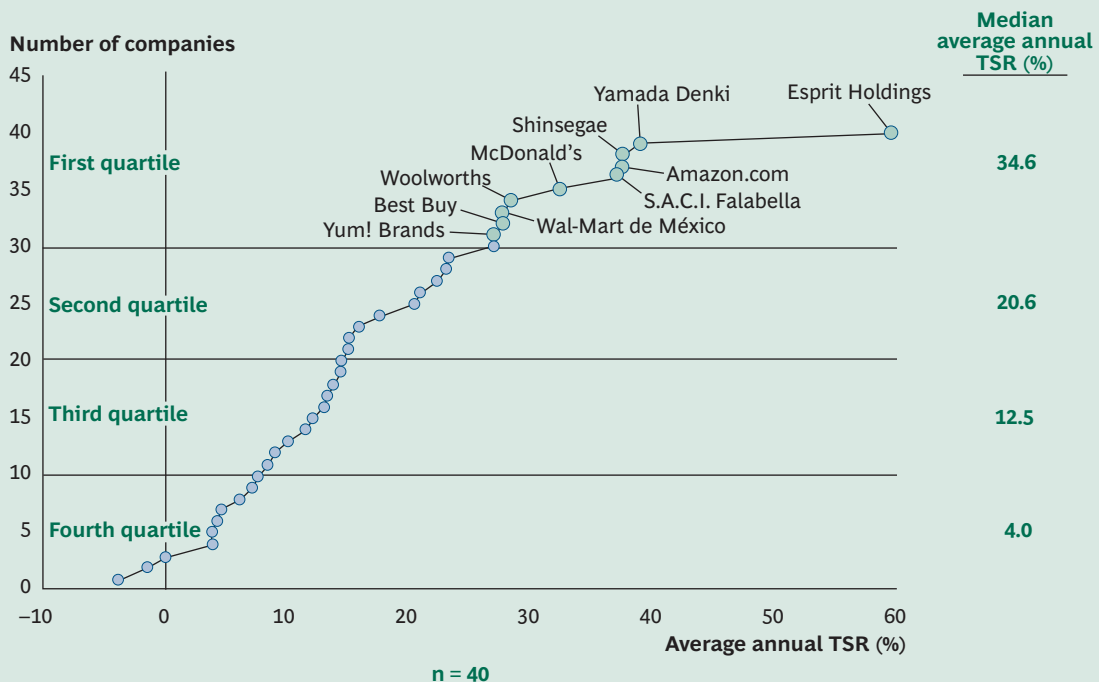
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

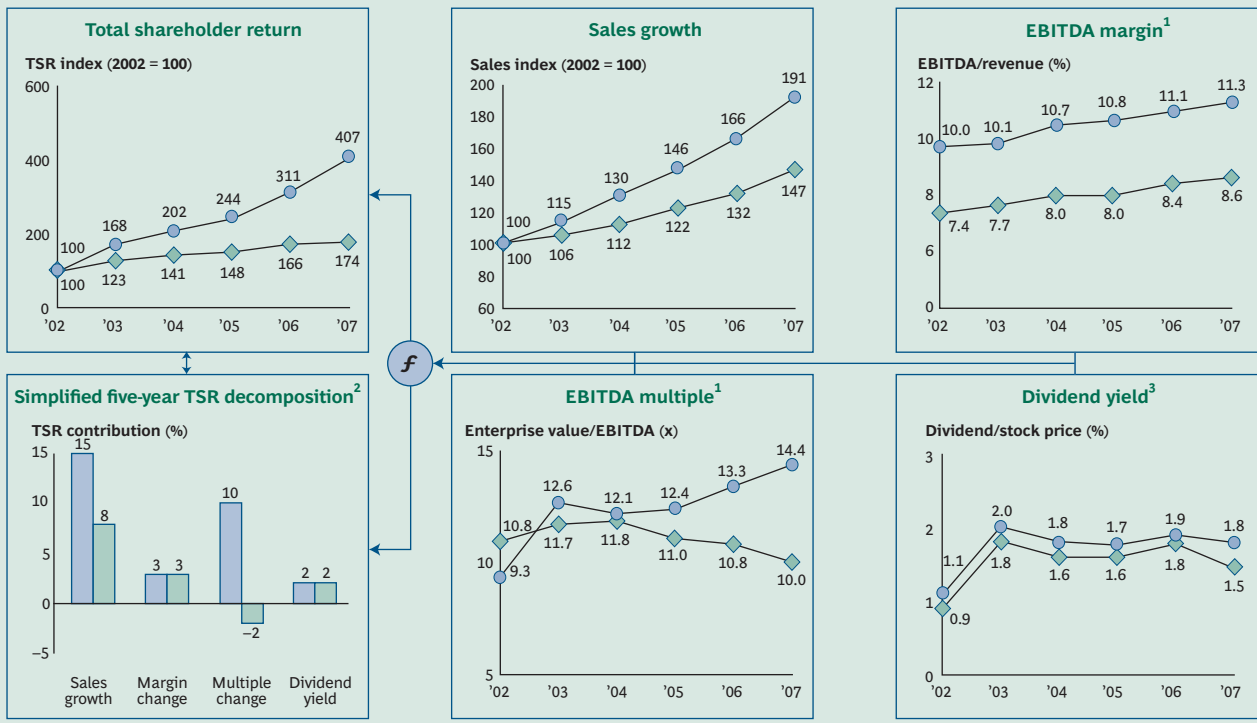
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Retail top ten    ◆ Total sample, n = 40

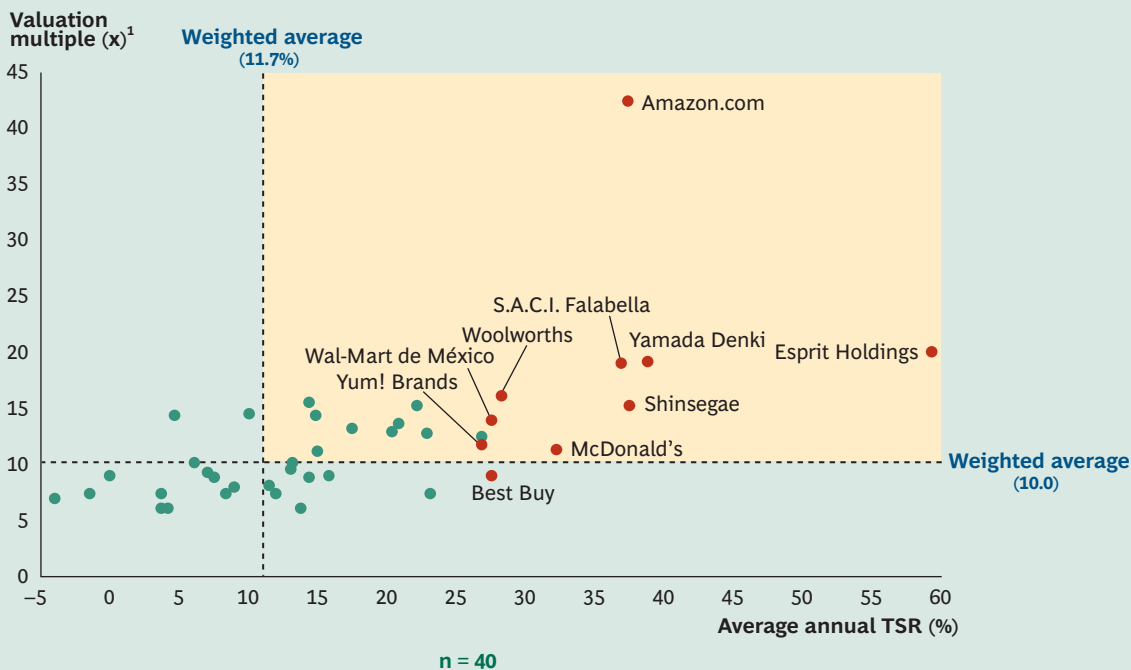
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Technology and Telecommunications

## The Technology and Telecommunications Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Bharti Airtel	India	110.7	47.840	78	26	0	0	0	7	-25.4
2	Apple	United States	94.2	172.791	34	49	39	0	-4	-24	-15.5
3	América Móvil	Mexico	68.9	107.050	42	3	14	1	2	7	-18.2
4	MTN Group	South Africa	61.5	34.875	46	13	0	1	-2	3	-1.8
5	China Mobile	Hong Kong	53.1	354.272	25	-1	23	4	0	2	-23.4
6	Rogers Communications	Canada	44.4	29.150	20	7	2	1	-7	22	-11.0
7	Telenor	Norway	40.6	40.151	15	3	11	3	1	7	-23.8
8	China Telecom	China	38.1	68.698	11	-1	23	3	-1	4	-30.5
9	Hon Hai Precision Industry	Taiwan	33.6	39.178	43	-7	3	2	-5	-1	-26.0
10	Singapore Telecom	Singapore	32.4	44.154	13	-5	12	6	0	7	-9.5

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 44 global companies with a market valuation greater than \$25 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

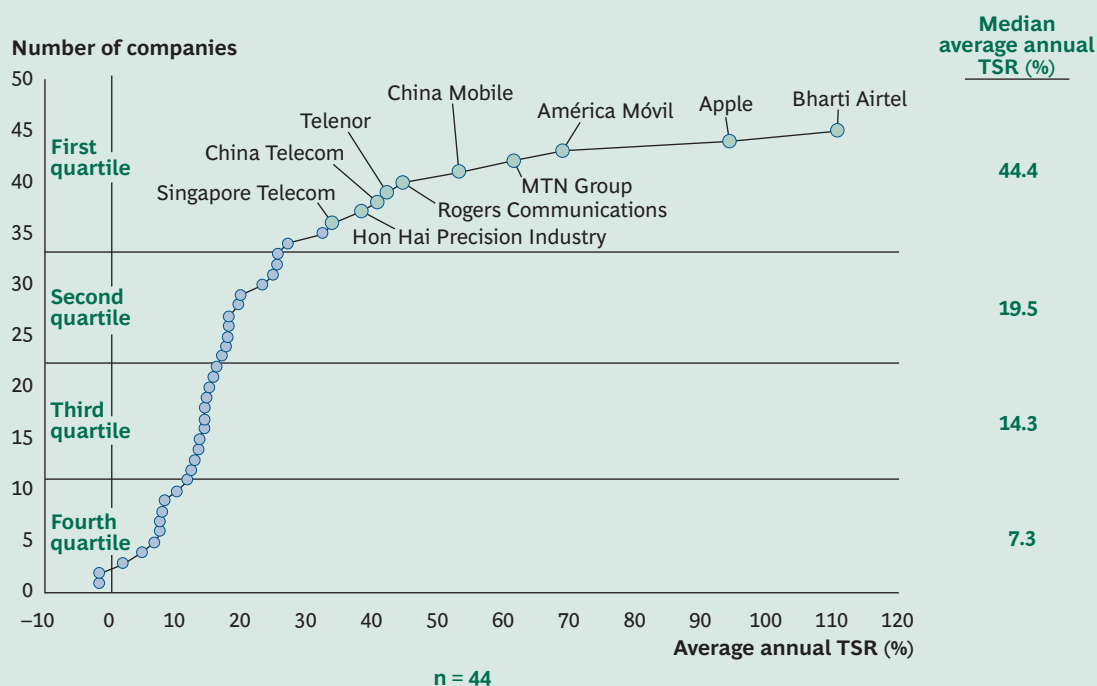
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

## Average Annual Total Shareholder Return by Quartile, 2003–2007

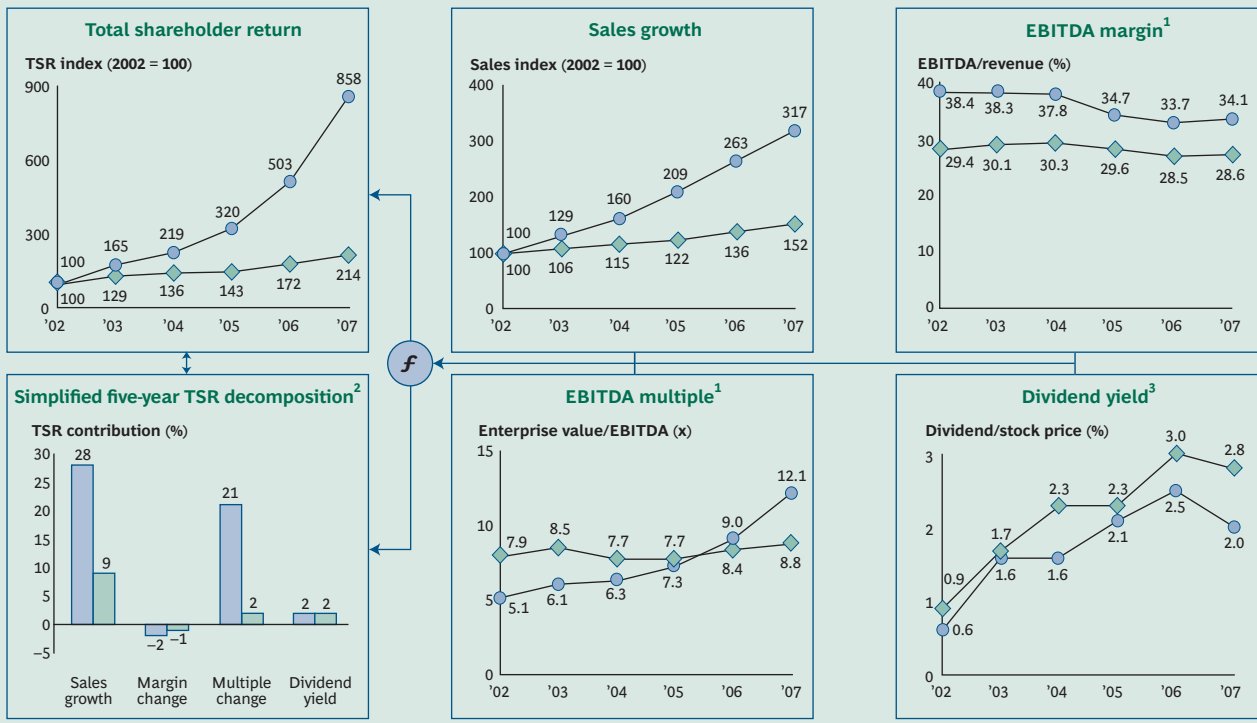


Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

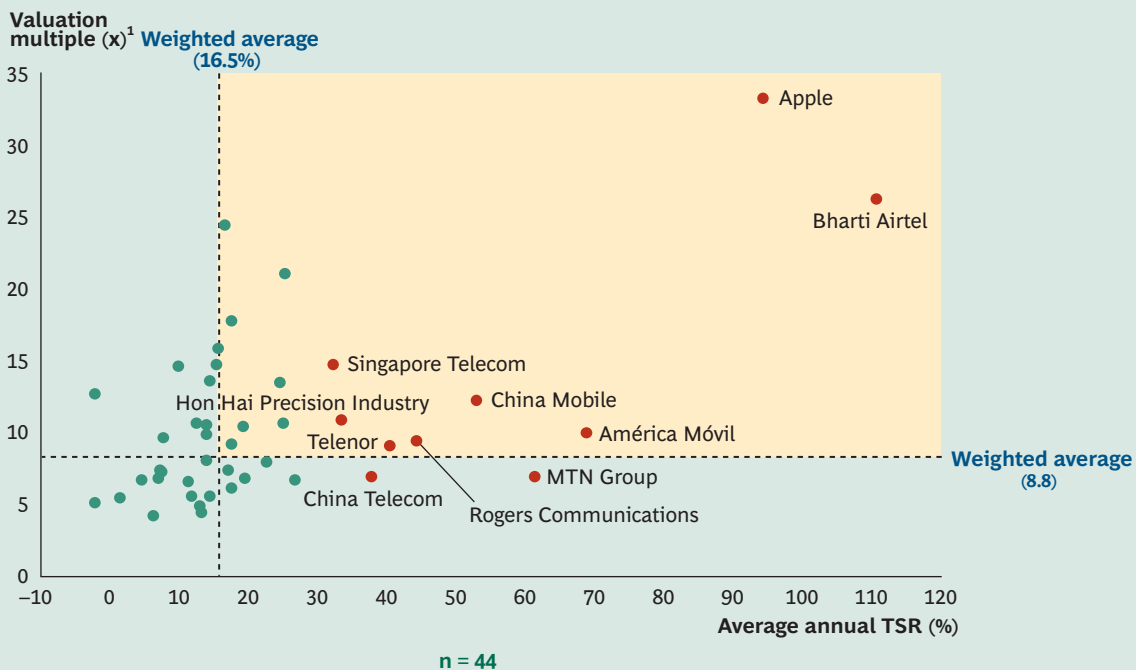


# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.  
<sup>1</sup>Industry calculation based on aggregate of entire sample.  
<sup>2</sup>Share change and net debt change not shown.  
<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.  
<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Transportation and Logistics

## The Transportation and Logistics Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	COSCO	Singapore	143.6	8.985	98	-8	20	4	-7	36	-43.4
2	Hyundai Merchant Marine	South Korea	92.8	5.999	3	27	3	2	-16	73	-8.7
3	Grupo CCR	Brazil	79.9	6.228	22	7	18	9	-3	27	17.4
4	China Shipping Development	China	71.7	8.787	28	2	31	7	0	3	15.9
5	China Merchants	Hong Kong	59.4	14.966	33	3	22	5	-3	0	-37.1
6	CIMC	China	58.0	5.099	40	-8	19	3	-4	7	-31.9
7	Beijing Capital Int'l Airport	China	53.8	6.870	10	1	39	4	-1	1	-50.4
8	Kuehne + Nagel	Switzerland	47.0	11.500	22	3	21	3	-1	-1	-9.0
9	Mitsui OSK Lines	Japan	45.3	15.128	13	1	6	3	0	21	7.6
10	Kawasaki Kisen Kaisha	Japan	43.2	6.064	15	-1	3	4	-1	23	-7.9

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 42 global companies with a market valuation greater than \$5 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

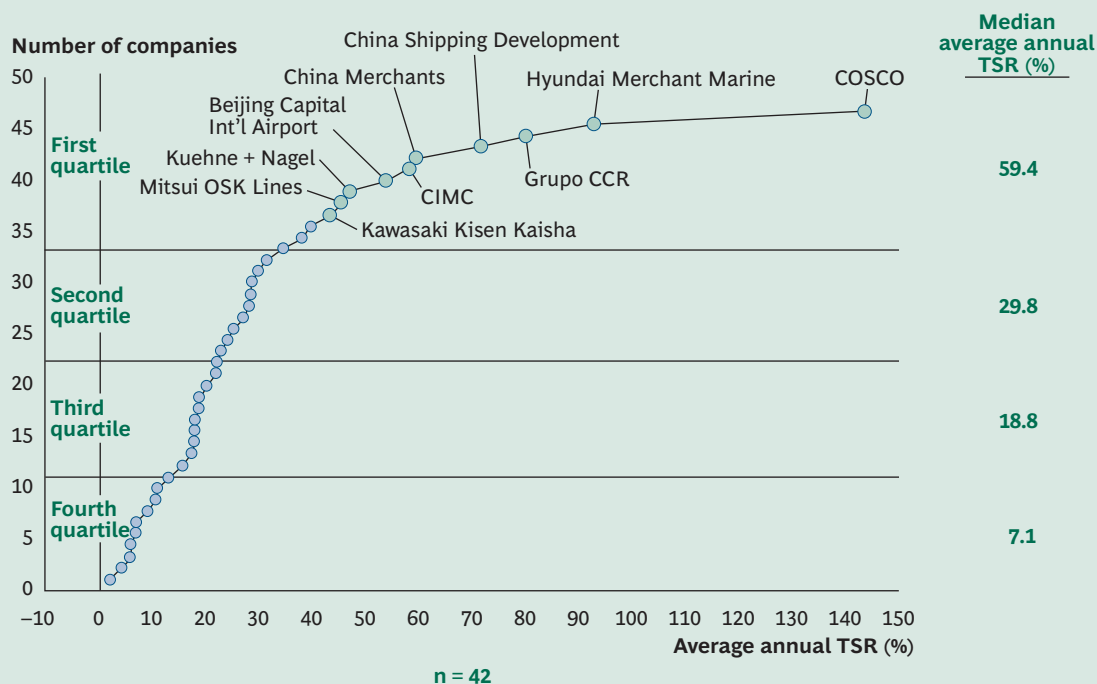
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

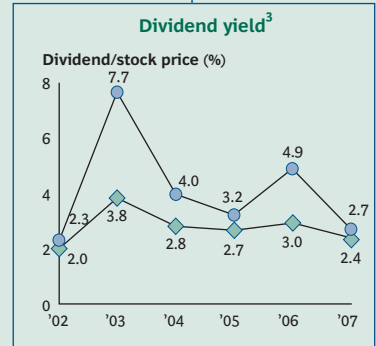
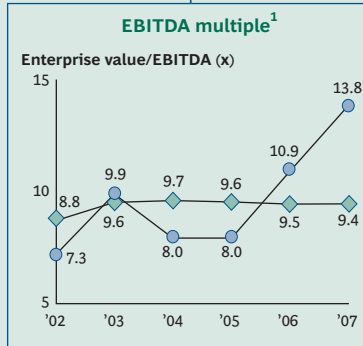
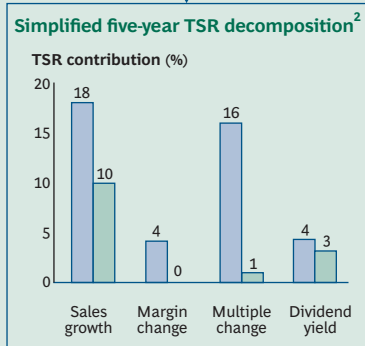
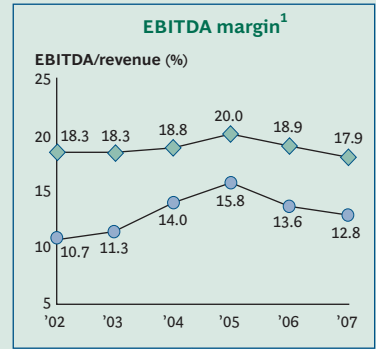
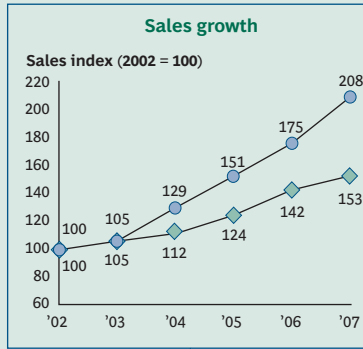
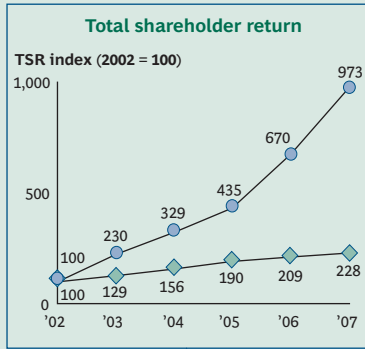
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Transportation and logistics top ten    ◆ Total sample, n = 42

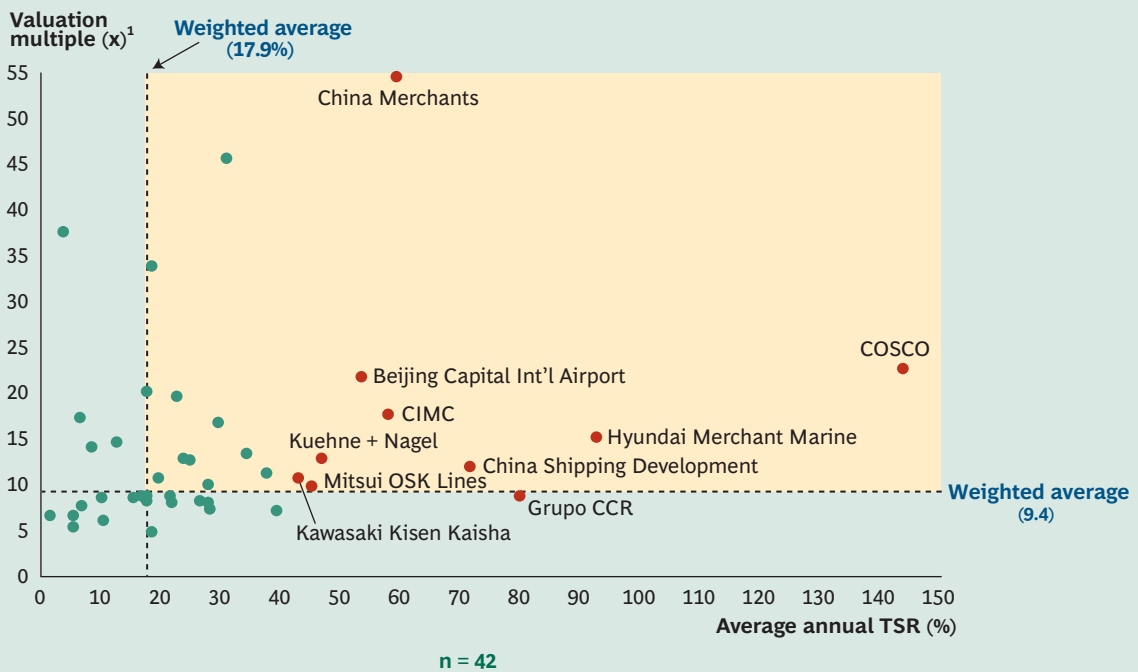
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Travel and Tourism

## The Travel and Tourism Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Stagecoach Group	United Kingdom	62.1	6.233	-4	1	26	6	4	29	-1.2
2	LAN Airlines	Chile	61.2	4.771	21	15	6	8	-1	13	-22.0
3	China Eastern Airlines	China	52.1	5.137	28	-11	17	0	0	18	-68.2
4	Korean Air Lines	South Korea	47.8	5.541	7	-2	5	1	-1	38	-35.9
5	Shangri-La Asia	Hong Kong	38.9	9.054	16	6	8	2	-5	12	-25.3
6	MGM Mirage	United States	38.5	24.682	17	-1	14	0	1	7	-59.7
7	China Southern Airlines	China	37.4	6.156	25	-14	21	0	-5	11	-69.8
8	FirstGroup	United Kingdom	33.0	7.096	12	-5	14	5	-1	8	-35.7
9	Air France-KLM	France	22.4	9.751	13	6	-1	1	-5	7	-36.6
10	Royal Caribbean Cruises	United States	22.4	9.018	12	-3	2	2	-2	10	-46.6

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 28 global companies with a market valuation greater than \$4 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

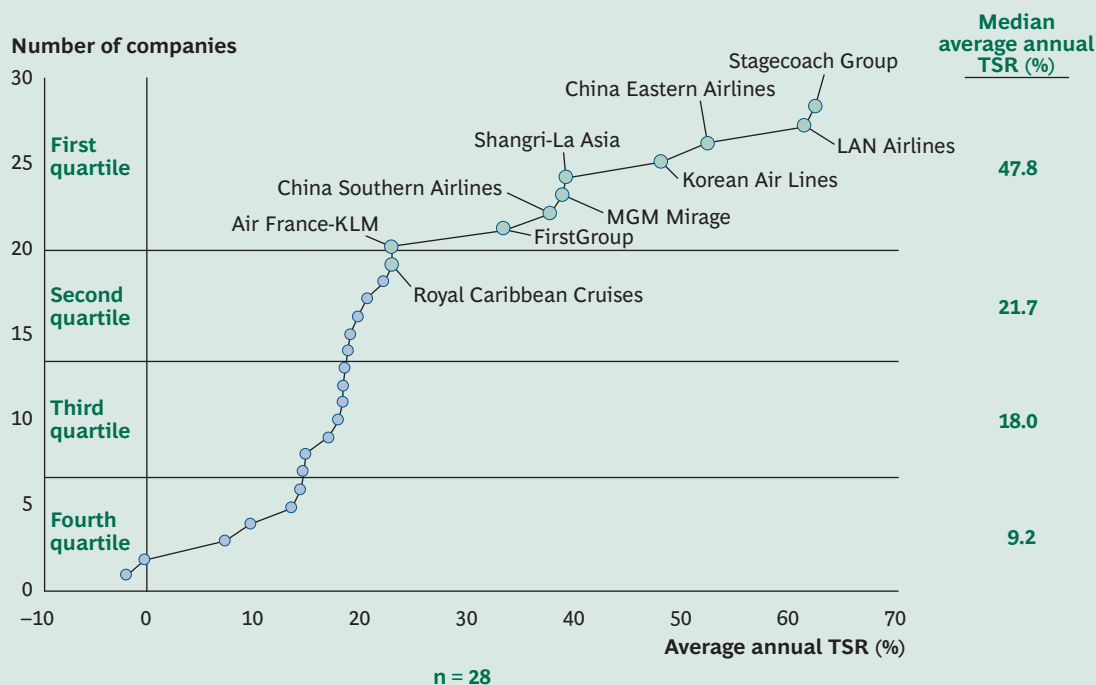
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

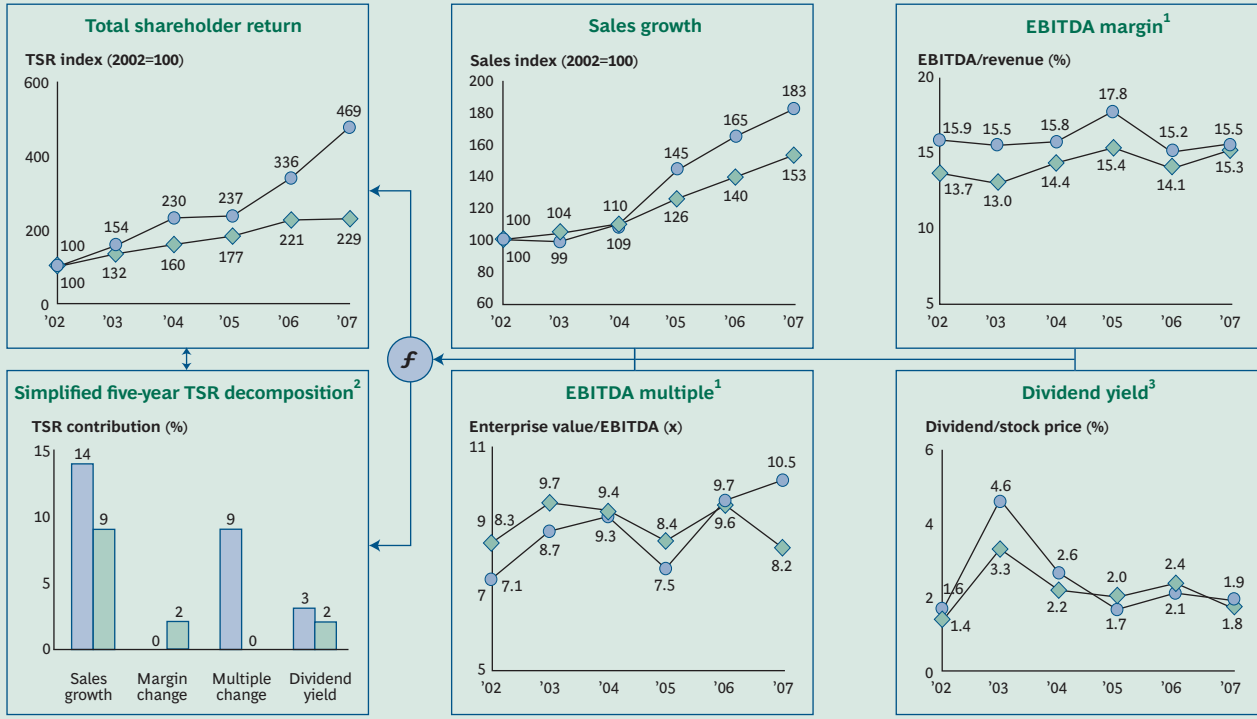
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



● Travel and tourism top ten    ◆ Total sample, n = 28

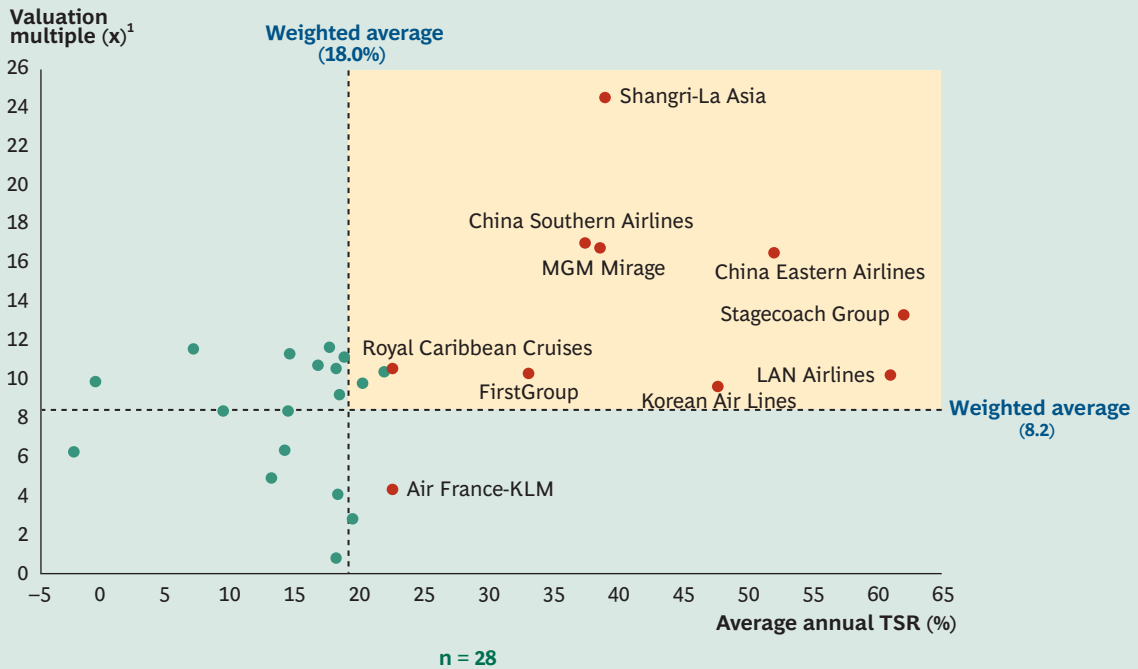
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.

# Utilities

## The Utilities Top Ten, 2003–2007

#	Company	Location	TSR <sup>2</sup> (%)	Market value <sup>3</sup> (\$billions)	TSR Decomposition <sup>1</sup>						2008 TSR <sup>5</sup> (%)
					Sales growth (%)	Margin change (%)	Multiple change <sup>4</sup> (%)	Dividend yield (%)	Share change (%)	Net debt change (%)	
1	Williams Companies	United States	69.4	20.967	24	-6	0	2	-2	52	13.3
2	AES	United States	47.9	14.339	13	-4	0	0	-4	43	-10.2
3	Datang Power	China	45.2	11.181	33	-5	20	5	-3	-5	-31.8
4	Verbund	Austria	45.1	21.575	9	9	6	3	0	19	21.2
5	International Power	United Kingdom	41.2	13.531	30	-13	26	2	-4	1	-3.1
6	Edison International	United States	38.2	17.389	5	-1	5	3	0	26	-2.6
7	E.ON	Germany	36.2	134.465	15	5	-3	6	1	14	-9.2
8	RWE	Germany	36.2	79.308	-1	-1	7	5	0	27	-13.6
9	BG Group	United Kingdom	35.2	81.670	27	1	3	1	0	2	14.2
10	Constellation Energy	United States	33.2	18.295	33	-25	13	3	-2	11	-19.1

Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

Note: n = 57 global companies with a market valuation greater than \$10 billion.

<sup>1</sup>Contribution of each factor shown in percentage points of five-year average annual TSR; apparent discrepancies with TSR totals due to rounding.

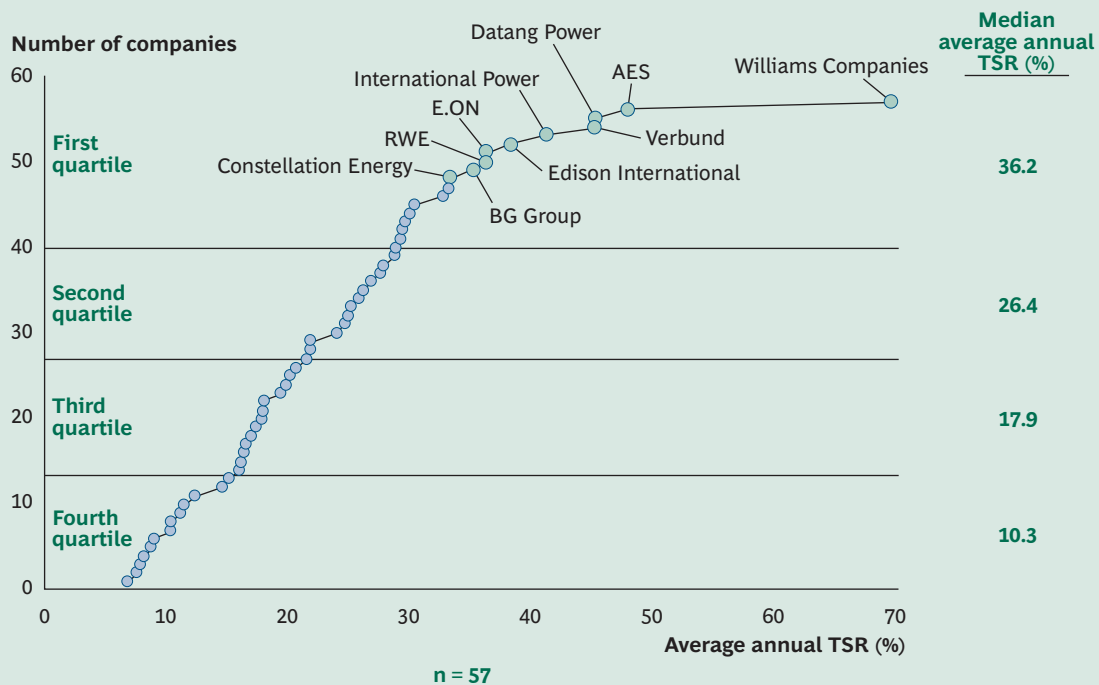
<sup>2</sup>Average annual total shareholder return, 2003–2007.

<sup>3</sup>As of December 31, 2007.

<sup>4</sup>Change in EBITDA multiple.

<sup>5</sup>As of June 30, 2008.

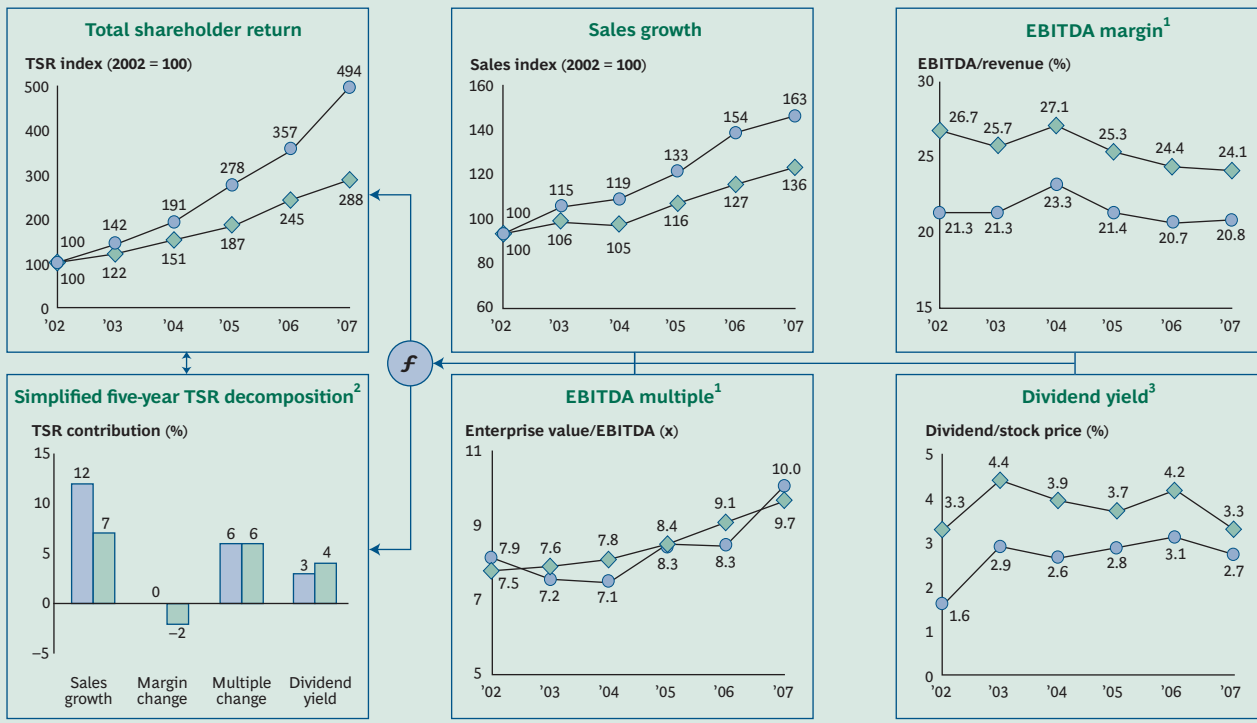
## Average Annual Total Shareholder Return by Quartile, 2003–2007



Sources: Thomson Financial Datastream; BCG analysis.

Note: TSR derived from calendar-year data.

# Value Creation at the Top Ten Versus Industry Sample, 2003–2007



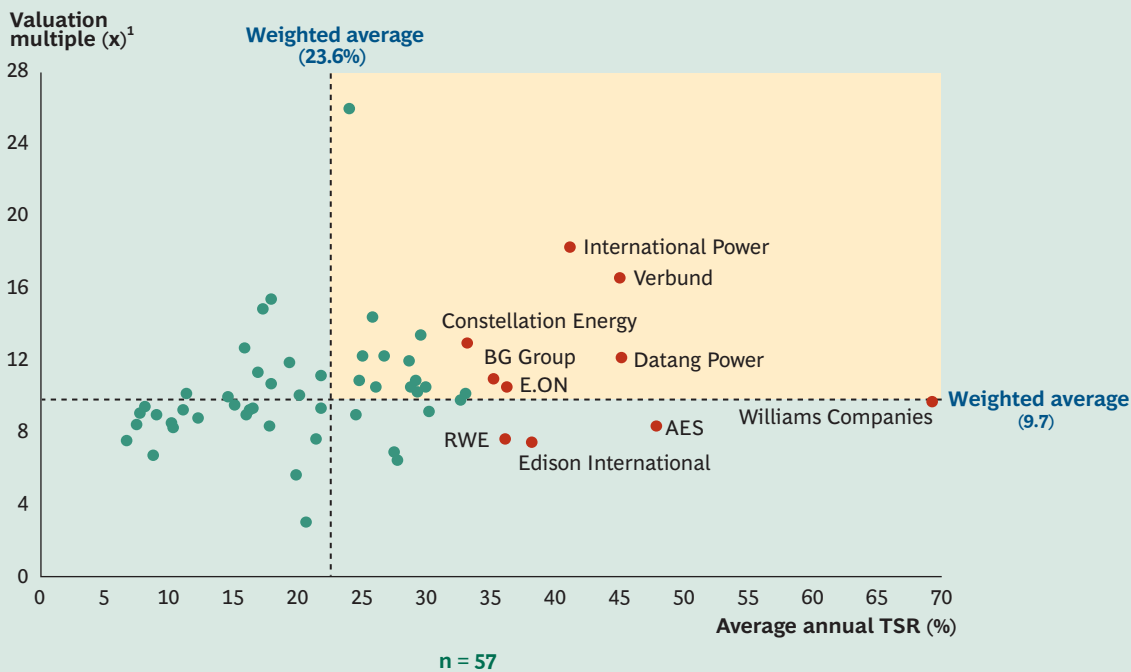
Sources: Thomson Financial Datastream; Thomson Financial Worldscope; Bloomberg; annual reports; BCG analysis.

<sup>1</sup>Industry calculation based on aggregate of entire sample.

<sup>2</sup>Share change and net debt change not shown.

<sup>3</sup>Industry calculation based on sample average.

# Value Creation Versus Expectations, 2003–2007



Sources: Thomson Financial Datastream; Bloomberg; BCG analysis.

<sup>1</sup>Ratio of enterprise value to EBITDA, 2007.



# For Further Reading

The Boston Consulting Group publishes many reports and articles on corporate development and value management that may be of interest to senior executives. Recent examples include:

**The Return of the Strategist: Creating Value with M&A in Downturns**

A report by The Boston Consulting Group, May 2008

**Managing Shareholder Value in Turbulent Times**

The 2008 Creating Value in Banking Report, March 2008

**The Advantage of Persistence: How the Best Private-Equity Firms “Beat the Fade”**

A report by The Boston Consulting Group, published with the IESE Business School of the University of Navarra, February 2008

**Thinking Laterally in PMI: Optimizing Functional Synergies**

A Focus by The Boston Consulting Group, January 2008

**The Brave New World of M&A: How to Create Value from Mergers and Acquisitions**

A report by The Boston Consulting Group, July 2007

**Powering Up for PMI: Making the Right Strategic Choices**

A Focus by The Boston Consulting Group, June 2007

**“Managing Divestitures for Maximum Value”**

Opportunities for Action in Corporate Development, March 2007

**“A Matter of Survival”**

Opportunities for Action in Corporate Development, January 2007

**Managing for Value: How the World’s Top Diversified Companies Produce Superior Shareholder Returns**

A report by The Boston Consulting Group, December 2006

**“What Public Companies Can Learn from Private Equity”**

Opportunities for Action in Corporate Development, June 2006

**“Return on Identity”**

Opportunities for Action in Corporate Development, March 2006

**“Successful M&A: The Method in the Madness”**

Opportunities for Action in Corporate Development, December 2005

**“Advantage, Returns, and Growth—in That Order”**

BCG Perspectives, November 2005

**The Role of Alliances in Corporate Strategy**

A report by The Boston Consulting Group, November 2005

**“Integrating Value and Risk in Portfolio Strategy”**

Opportunities for Action in Corporate Development, July 2005

**“Winning Merger Approval from the European Commission”**

Opportunities for Action in Corporate Development, March 2005

**“The Right Way to Divest”**

Opportunities for Action in Corporate Development, November 2004

**Growing Through Acquisitions: The Successful Value Creation Record of Acquisitive Growth Strategies**

A report by The Boston Consulting Group, May 2004



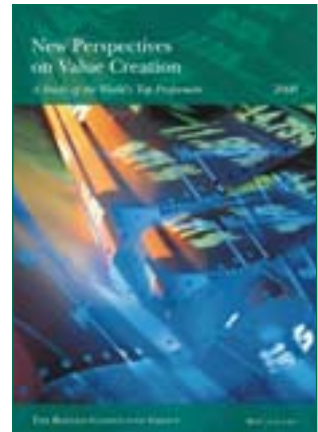
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