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A "Hands-on" Approach to Surviving the Recession

by Art Kleiner and Laura W. Geller

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A “Hands-on” Approach to Surviving the Recession

Noble Group CEO Richard Elman discusses risk, opportunity, and his growth strategy for the commodities business.

by Art Kleiner and Laura W. Geller

The Noble Group Limited, a Hong Kong–based leader in global supply chain management for agricultural, industrial, and energy products with revenues of US$36.1 billion in 2008, has a telling corporate motto: “hands-on.” This describes not just the company’s collaborative approach to doing business, but also its philosophy on growth. And it may provide a key for any company that is seeking to manage its way to recovery, even in uncertain enterprises such as commodities and logistics.

As founder and CEO Richard Elman explains, “We have to consider every morning that our business is fragile, and that it can break very easily.” He places risk analysis at the core of his business model and makes well-calculated decisions on a case-by-case basis. Over the years, commodities-based businesses have experimented with primarily vertical structures (owning every part of the supply chain) or with horizontal approaches (seeking global reach only in one or two parts of the business). Both have their vulnerabilities; vertical structures are expensive and difficult to control, and horizontal structures are dependent on suppliers and customers.

The Noble Group approaches the business differently — perhaps even counterintuitively — by owning assets and controlling selective pieces of the supply chain in both directions, choosing each component based on the judgment of the firm’s top decision makers and supported by rigorous analysis. Continuously honing their acumen, and exercising it actively, is the heart of their strategy. This approach controls the company’s scale and means that it is only as successful as its last accurate insight, but it also gives Noble Group a flexibility and capability that companies with a more formal strategy may lack.

Despite the downturn, Noble Group recently reported solid financial results for the first quarter of 2009. Although revenues and profits were down, reflecting the weakened commodity price environment, Nobel Group’s net profit margin increased and it maintained high liquidity with a cash position at near-record levels. Elman spoke with *strategy+business* in March 2009 about his company’s approach.

S+B: How did Noble Group develop its unique approach?

ELMAN: We are fundamentally merchants. We recognized many years ago that our business was not based on assets. It was based on arbitraging information from different places and industries. With the advent of the Internet and cell phones, those opportunities for arbitrage disappeared rapidly. We knew we had to do something else. We understood that we had to add some value to the transaction, and one of the ways to do that

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is to control part of the supply chain. We also saw that, in some of the businesses — agriculture, in particular — if you don't control the whole chain, you're not fully in the business.

We did not have the resources to compete with the likes of Cargill Inc., 150-year-old companies with billions of dollars in assets. So we were selective, developing what we like to refer to as a global niche business. We identified areas where we could build a chain and put the assets in place that should be rewarding: not always rewarding in the same spot in the chain, but rewarding overall. And that put us in a position to capture the margin.

For example, if you grow soybeans in Argentina and then crush the beans in China and sell the oil in China, somewhere along that chain there should be a margin. Let's say that another company comes along and says, "We want to buy your beans for North Africa." If there's a premium over what we can get in China, we will sell into North Africa and then look at the market to see if we can buy the beans from someone else to satisfy our Chinese crushing business.

S+B: So it's a matter of constantly assessing and reassessing your position?

ELMAN: Yes, it's a question of making your best judgment. We also have to make sure that our production assets are world class and produce the best of class. The production rates have to be absolutely phenomenal. We developed these capabilities over a long period of time, and I think the biggest distinguishing factor is risk management. We understand risk. We like to buy and sell it. For example, if I buy a cargo of steel, I have a delivery risk, a price risk, a customer risk, and so on. If I know the risks well enough, I can set my prices accordingly. And that's a fundamental driving force of the company.

Globally, we have 42 full-time employees focused entirely on risk assessment. And they are layered with 25 people who do original research. As a result, we get a lot of guidance and control. We know what's happening on a daily basis and that's how we make decisions; it's as simple as that. We check the profit and loss figures for our operations every day, and we get a value at risk — for the company as a whole and for individual businesses — every day.

We have to consider every morning that our business is fragile, and that it can break very easily. So you'd better look at all the risks and make sure that they're mitigated as much as possible. If we see something we don't like, we immediately suggest to the people in charge that they do something else. If there's no margin in crushing soybeans today, we will slow down the crushing. Or we might even stop the crushing for a week or two. However, if the margin is good, we go full blast. We run 25 different businesses here, and it's a whole bunch of verticals.

S+B: How are you positioning your company for growth during the current global downturn?

ELMAN: Right now, we're hiring a lot of people. I think we're one of the few companies in the world that have been hiring people at this pace in the last couple of months. We're continuing our education programs, even though they're expensive. We're continuing to hire business school graduates — we're not the only company doing this, but we're one of the few that do it en bloc.

I've often thought about why our chain works and other companies' don't. If I were an auto manufacturer, and all I produced were cars, I would have a problem today. But I produce maybe 30 percent of what I trade. So even if marginally one of my assets is impaired or squeezed from a profit point of view, I still have the other businesses. I trade other people's cars, to put it simply. And that's a big difference. Because we have a strong ability to take market share, we continue to grow our business when others might be declining.

I also happen to be in businesses that are recession-proof. No matter what, people have to eat. They may eat less or eat cheaper, but they still eat. And despite the global recession, there is still some growth in the world, particularly in Asia. I think the Asian economies are in far better shape than the U.S. economy, and the Asian banks are certainly not in as bad shape as most U.S. banks.

S+B: What about opportunities for growth through M&A?

ELMAN: We haven't bought any businesses. We've bought assets, usually distressed assets, and have built businesses around them. I think that is a fundamentally sound approach. Our company is pursuing growth the hard way, and it takes much longer than growing through M&A. At one point, we bought the inventory of a company, and a number of its employees joined us. But within 24 months we didn't have a single one of those people left. The company was in liquidation because of its culture. This episode made us realize that, if we're going to make mistakes, let's do it ourselves in our own culture.

Also, we never look for a quick shot of financial energy to bolster the bottom line, balance sheet, or the P&L. A lot of companies buy companies just so they can get a P&L boost. We don't think that's a very good thing to do.

Finally, even as we expand, we don't need to buy other companies. We have more opportunities today to buy distressed assets than we've ever had. Because there are so many undercapitalized and badly financed companies out there right now, we are presented with four or five opportunities every day, around the world. Although 90 percent of them aren't worthwhile, there are still some serious opportunities on that list. And that means a lot of distressed assets.

S+B: Do you see changes coming in the nature of supply chains around the world?

ELMAN: Chinese companies are eager to acquire raw materials or to buy the assets to produce the raw materials to meet the country's large and growing demand. I was concerned when the Australian government turned down China Minmetals Corporation. [The Australian government blocked Minmetals' bid for OZ Minerals Ltd. in March 2009, but later agreed to a revised offer.] But I was equally disturbed by China's rejection of Coca-Cola Company's bid to acquire China Huiyuan Juice Group Ltd. These deals struggled for different reasons, and they may be right or wrong. But in the reaction to them, I see protectionism creeping in. In the United States a controversy erupted early in 2009 over "Buy American" provisions in the stimulus package. If the leader of the free world starts to be protectionist, others will follow.

I've also noticed other changes. We have 10,000 people working at Noble, and we have 100 offices in 45 countries. We like to move people around. But my HR department has told me that it's getting more and more difficult to get visas. Things that took two weeks to handle are now taking four weeks and are being scrutinized in greater detail than ever before. I thought the world had been well on its way to globalization, but there is a danger that fear-based policies could cause the pace of international trade to stall, or even to reverse. That wouldn't just be a problem for our company, but for everyone's prosperity. +

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