Lessons from Oz: Where listed companies can get it wrong

I have just returned from a fabulous few weeks in Australia and would like to share some observations with you – as there are some great lessons to be had, namely:

- The law of unintended consequences
- The dangers of short-termism
- Don't forget to innovate
- Put the needs of your customers ahead of your executives
- Leaders get the culture they create
- Find your Change Catalyst

Australia's is a fascinating economy. The last time it went into recession was 1992. Growth in 2018 is forecast to be close to 3%. Yet cost of living and wages are so high that every single auto manufacturer has ceased making cars in the country. Its government debt to GDP ratio is one of the lowest in the western world and its personal debt one of the highest. House prices in its major cities are astronomical.

But it is the nature of its stock markets that is of particular interest. Australia is the highest paying dividend country in the G20 group of major global economies with an average yield of 5.64 per cent - almost three times that of the US and 50% higher than the UK. But these strong dividends paid to investors in Australian companies can mean lower capital returns and the potential for companies to underinvest in their future.

The law of unintended consequences

This situation is an unintended consequence of compulsory pensions.

Superannuation (pension) has been compulsory in Australia for many decades and today employers pay 9.5% of everyone's salary into pension savings every month. Consequently, Australia is the fourth largest pension investment market in the world.

Driven by the income-generating demands of current and future pensioners, the ASX is full of companies that will do almost anything to make sure they pay their high annual dividends. The thought of lowering the dividend payment is anathema to many boards. Some will go to extraordinary lengths to avoid it, even borrowing and occasionally employing incredibly creative accounting methods to protect the payments.

Three key down-side consequences of such a dividend-obsessed ecosystem are:

Short Termism. It encourages boards to focus on short-term performance, and as regular readers of my blogs will know short-termism destroys shareholder value. The CEO of a major Australian FS firm recently announced a complete U Turn in the company's strategy. It was investing in a major customer-centric transformation program with the power to be a genuine long-term differentiator for the firm. However, seeing that this was not being appreciated by the short-term-obsessed market, the CEO has put the transformation program on hold and resorted to good old-fashioned

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cost-cutting measures instead. The share price has started to tick upwards – I assume towards the level he needs it to be to maximise his pay out when his contract ends some time soon.

Where's the innovation? It has a stifling effect on growth and innovation. '*Investing in growth is fine – as long as it doesn't affect short-term performance!*' At a recent business conference in Sydney, the US partner of a major strategy firm asked the audience to name "a truly transformational current Australian business leader". The silence was deafening.

Executives first. The third thing I noticed is that too many listed companies seem to have their priorities in completely the wrong order – something not unique to Australia I hasten to add. Too many are run for the benefit of the executives first and foremost. Customers, employees and even shareholders all rank lower on the list of priorities. Australia is currently in the midst of a Royal Commission into retail banking and insurance. Consequently, the public has been given a chance to witness the self-centred behaviour and hubris of some of its most highly paid executives up close and personal. Every day brings new revelations of customers being ripped off (eg charged for services they didn't receive), the regulator being treated with contempt and boards (who should be acting on behalf of the shareholders) scrambling to cover up wrongdoings. "It's the culture, Stupid." (as Bill Clinton should have said). A company gets the culture its leaders create; the culture its leaders deserve.

But let me be clear - none of these three attributes is unique to Australia.

Listed companies worldwide suffer from one, two or all three.

A Change Catalyst to bridge the gap between the shareholders and the executives

The solution is to realign the corporate priorities – customers first, employees second, shareholders and executives third. This requires a change of culture - removing short-termism from decision-making and ensuring the entire organisation is focused on creating a long-term, sustainable company - for the benefits of all. It will also require taking a new approach to executive remuneration.

And as I detail in the book, this is the job of a Change Catalyst – someone to work for the board and with the executives to make all of this happen.

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