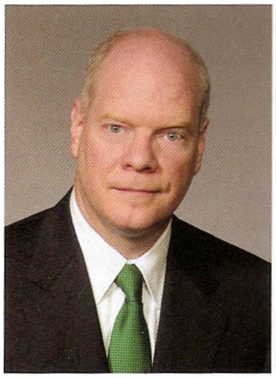
Growing a great business

A growth culture includes exceptional performance — Mike Mack



Mike Mack, Senior Vice President and CFO, Deere & Company

To find out how well John Deere is doing in growing a business as great as its products, *John Deere Journal* asked Mike Mack, Senior Vice President and Chief Financial Officer, to answer some questions.

We've been concentrating on growing a great business for two years now. How are we doing?
We're beginning to see the benefits of the focus and the discipline we've built into the Business Growth Process. More growth ideas are being generated and captured, and they are increasingly customer focused. But we've got a long way to go to sustainably meet our SVA growth goals.

Haven't we already been growing SVA pretty dramatically over that period?
We've certainly created some SVA from growth, but mostly we've been learning how to get it from current operations and from the expansion of current operations. We've done a good job of getting into position to grow a great business. But to get the kind of SVA growth we're targeting, we need other approaches as well.

Industry growth and operating improvements are very important, but they won't by themselves get us to our growth targets. So, we have to become more aggressive seeking growth sources beyond core operations.

What is the target?
Our goal has always been to increase SVA by 7 percent a year. That's an aggressive goal. To accomplish it, we have to generate significant growth of the company, and we have to do it faster than before.

How are we doing that?
Our growth strategy is pretty straightforward: We grow through innovation, invention, and accelerated customer focus. The Business Growth Process and its elements, especially 30/70 Innovative Growth and the Accelerated Innovation Process, are designed to provide a systematic way to focus on growth, generate growth ideas, rigorously analyze them, and find ways to control the risk as much as possible.

Why the focus on innovative growth?
Deere has a strong record of profitable growth from taking the John Deere brand to a growing, global group of customers, and that has to continue. To reach our goals, we must add ideas that go beyond traditional businesses and markets, and we have to accelerate the decision-making process. The reason is that only growth with a strong return on invested capital creates sustainable value, and growth based on innovation typically has a significantly higher ROIC than does growth based on line extensions. But, we need both kinds of growth, because all growth, to be sustainable, has to contribute to the company's core.

What do you mean by contributing to the company's core?
The new growth has to ultimately become part of our core businesses. It's the result of a "virtuous circle" of disciplined growth: While we're strengthening and growing the core businesses, we're also mapping related adjacent business opportunities, those that are in large measure related to businesses we are already in. Those adjacencies are prioritized based on their potential and also on their "fit" with the core businesses. In other words, how well the skills and competencies we use in our core businesses match up with those needed in the new areas we're considering.

Is there ever a perfect fit?
Seldom. If there were, we would probably already be in that business. But the gaps should be as small as possible, and we might even use partnerships and acquisitions, such as the recent acquisitions in water technologies, to fill them. When it all works out, and we're successful

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"Sustained growth is possible only when you delight customers."

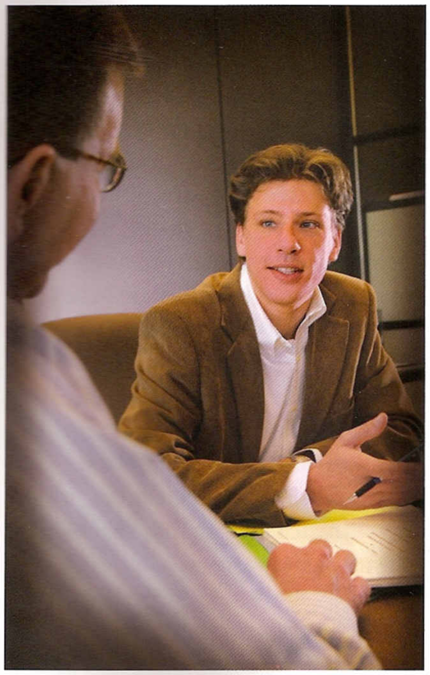
— Mike Mack, Senior Vice President and CFO, Deere & Company

in the new area, we can redefine the core business to include the expansion — and begin looking at opportunities adjacent to the new, expanded core.

How much do we have to grow to meet that 7-percent SVA growth goal?
Our target is $1.5 billion SVA by 2014. Remember, we always talk about these goals in terms of normal volumes. At that level of SVA, we estimate we would be operating at a level of revenues approaching $40 billion. Getting to that level of revenues, incidentally, would be a pretty good indication that you're serving customers very well. That's where operating performance and disciplined growth come together, and that will be the evidence that we've transitioned from a performance culture to a growth culture.

So we concentrate mostly on growth?
A growth culture includes exceptional performance. We started with a focus on exceptional performance because we had to get that right in order to get into a position to grow. For example, we have transformed Deere from being a relative underperformer in terms of ROIC to a top decile performer compared with our peers and with the top 500 industrial companies in the United States.

So, that's where we've gotten our SVA thus far?
It's exceptional performance that leads to SVA, whether through growth or current operations. The important thing about SVA is that it provides higher cash flows more consistently. That funds our growth — and other things, like pensions and dividends and share buybacks. Importantly, our pension and OPEB (other post-employment benefits) obligation funding is in very good shape. Also, we have had six dividend increases since 2004, for a cumulative increase of 155 percent. Additionally, we have repurchased about $5 billion worth



Stephan Formica reviewed 900 potential business deals at a venture capital firm, looking for opportunities for John Deere.

John Deere explores

In its drive for innovative growth, Deere is opening new channels, getting ideas from academia and suppliers, and amassing advanced marketing research and business intelligence.

For the past year, it has also been prospecting in the constant stream of business models, technology applications, and ideas that people take to venture capital funds.

John Deere Ag Division Business Development has been wading in that stream through a €5 million investment in Emerald Technology Ventures Fund II, a venture capital fund managed by Emerald Technology Ventures, LLP, headquartered in Zurich. Deere is one of 29 limited partners in the fund.

"In the beginning, it took awhile to figure out what people at Deere are working on. It took awhile to understand what our innovation needs are, and which are our major R&D areas that could be supported by new ideas coming through venture capitalists," said Stephan Formica, who was seconded to Emerald, meaning he worked for the venture capital firm while remaining a Deere employee.

The venture capital world moves very fast. Formica has screened 900 potential business deals, about 400 of which he has passed to various Deere divisions or the Moline Technology Innovation Center for more in-depth analysis. "Most of the time," he said, "I was looking at technology and companies that have to do with our core businesses and our expansion into water and renewable energy."

Emerald focuses on technologies in energy, materials, and water. It has offices in of stock since 2004, reducing our share count outstanding by about 14 percent.

How does that exceptional performance become a growth culture?
When you look at what employees around the company are most engaged in, you realize everyone is making the move from a performance culture to a growth culture.

Take DPS and DPQS. On the surface, those might appear to some people to be initiatives aimed at exceptional performance, and they do improve performance. But they are growth initiatives, too.

Sustained growth is possible only when you delight customers. That means you have to be committed to continuous improvements in the quality, reliability, and delivery of products and services.

Both DPS and DPQS are explicitly customer-focused. So is our process for delivering new products and services that can help customers succeed in their own businesses and expanding into new customer segments, new channels, and new geographies.

A great business gets great results that are sustainable and reproducible. There are three things we have to do to be a great business: Lower our earnings volatility; achieve sustainable SVA growth; and generate top-line, or revenue, growth.

If, by 2014, we can prove we've lowered volatility in our earnings and sustained SVA growth AND top-line growth, we might have some claim to being a great business.

venture capital

Zurich, Switzerland, and Montreal, Canada. It manages three venture capital funds and two portfolio mandates totaling more than $440 million.

The main tasks during the first year of participation have been to make business development groups at Deere aware of the venture capital work and to learn how to take advantage of the volume of information it produces.

Exploring new businesses and technologies isn't the only reason to have one foot in the venture capital stream, said Jeffrey Nadison, Regional Director, Business Development at John Deere's European Headquarters in Mannheim, Germany. As in all business activities, information flows to those who network, and Deere's exposure to information goes beyond a single venture capital fund. Deere is a member of CleanTech Network, LLC, a consortium of investors, funds, and professional firms interested in clean technology.

CleanTech, which says it founded the clean technology investment category, distinguishes between envirotech, or greentech, and cleantech categories. It says the other categories are more focused on ventures and technology that will help meet regulatory requirements, with high returns a secondary goal. Cleantech, by contrast, is populated by businesses focusing on new technology with the potential for high returns, but that also happen to be able to mitigate global environmental, health, or other challenges.

The growth machine

Growth can't be left to chance, points out Mike Mack, Deere & Company Senior Vice President and Chief Financial Officer. Growth requires a strategy and a rigorous process.

John Deere's strategy is 30/70 innovative growth, an initiative that stipulates that 30 percent of the company's growth will come from products, services, and markets new to the company.

To execute that strategy, the company created a structure and an organization at the enterprise level that operates alongside the divisional business development groups. The basic structure is the seven-phase Business Growth Process announced in the fall of 2006. The process is designed to generate and capture growth ideas, vet them for commercial viability and strategic fit, and track not only growth, but the performance of the growth process itself.

To meet the 30/70 innovative growth requirement, ideas that enter the process have to include a significant number of opportunities based on innovation-based products, services, and markets new to the company.

That's the focus of the accelerated innovation process. AIP is designed to speed up and improve the quality of innovation throughout the company.

The AIP is implemented through two groups, the Enterprise Advanced Marketing Group and the Product Technology and Innovation Group. These groups, operating with the Corporate Business Development Group, track market trends and customer needs, and product trends and technology advances.

Support and oversight for the AIP comes from the Global Technology Advisory Council, a group of academics and industry leaders, and, within Deere, from the Innovation Growth Council.

The entire structure, along with the business development functions at the division and regional levels, ensures that the search for growth is customer focused and the risks well managed.