

THERMO ELECTRON TALK TO MANAGEMENT

Minneapolis, Minnesota

October 19, 1995

Thanks Bill. Ladies and gentlemen, it is a great pleasure to be with you today.

And I certainly appreciate all of Bill's very complimentary remarks which will make my wife have to work even harder at trying to keep me humble.

She's a lot like the wife of a man who received an honorary degree from a university.

As the degree was being conferred, many glowing and wonderful things were said about the man.

After the ceremony was over, he and his wife were strolling across the beautiful tree-shaded campus.

Still elated, the man said, "I wonder how many great men have received honorary degrees from this university like I just did?"

His wife answered dryly, "Well, there is at least one fewer than you think."

When Bill Rainville invited me to talk with you about "Thermo Electron from a Director's Point of View," such a broad topic was a bit risky because I could talk for several hours about my tremendously favorable opinions of the company and its management and the great enthusiasm with which I view its future.

Fortunately, I don't intend to repeat the mistake of a politician who was noted for excruciatingly long and boring speeches.

As he droned on and on before a very large audience, he noticed that people were beginning to leave the auditorium.

Undaunted, he kept orating and people kept filing out of the hall.

They continued to leave even faster and by the time he had finished talking there was only one man left seated.

The politician — sensing a loyal voter — left the platform and went down to shake the hand of the lone survivor saying, “Thank you so much for listening to my entire speech.”

The man replied, “Don’t thank me, I’m the next speaker.”

So in deference to the next speaker I am going to confine my remarks to just three of the fundamental strengths that I think have contributed to the success the company enjoys today.

Then I want to touch briefly on what the future may hold as Thermo Electron gets ready to move into the 21st century.

The first basic strength is the strategic long-range point of view that Thermo Electron’s management has used to guide the company over the years rather than relying on transitory short-term considerations.

The company’s second great strength is the creation by management of a corporate culture that encourages and fosters creativity and innovation.

And, the third strength is the unwavering commitment of Thermo Electron's management to an extremely high set of principles and the adherence of the entire company to the highest standard of business ethics and integrity.

I want to start with management's focus on the long-range point of view because it is so vitally important to the company's ongoing success and because it is so increasingly rare in the current business environment.

Too many businesses today concentrate almost exclusively on the short-range point of view.

They are concerned with what the next quarter's earnings per share will be that they lose sight of the bigger picture and fail to invest in the long-term growth that supports a company's future stability and sustainable profitability.

Thermo Electron management, on the other hand, has always taken the long-range point of view.

They have been willing to make investments that they knew would not produce a payoff or reward for two or three or even more years.

There are many examples of such investments — one is the research and development of the heart pump.

The company has been working on this breakthrough product for some 20 years and only now is the heart pump on the threshold of payoff.

Other examples of such investment are the bomb and drug detectors which required major research and development investments over five years with no payoff.

An example with which I am personally familiar was the dirt burner.

This required not only investments in development work to improve the dirt burner, but also the commitment of a great deal of time and effort to obtain the necessary operating permits from municipalities.

I am sure that all of you can cite similar instances where the company has made significant investments in research or in developing a new idea that depressed earnings for a period of time but resulted in a much greater payoff down stream.

As a director representing all of the company's stockholders, this forward-looking attitude is one that I like to see.

There are some stockholders, of course, who primarily want a rapid surge in profits so they can sell their stock and get out with a quick profit.

These are not the stockholders that I would like to think I represent because I believe they are very much in the minority although they make the most racket and the most noise.

I think that the majority of stockholders are willing to wait for a much greater profit two or three years down the line.

Thermo's approach to acquisitions is another example of management's commitment to the long-range point of view.

Most businesses acquiring companies want an immediate contribution to earnings per share.

By contrast, in many cases Thermo management is willing to take some immediate dilution in earnings because they believe that applying Thermo's principles and management methods will improve the operations of the acquired company.

At a Thermo board meeting four weeks ago at Nicolet in Madison, Wisconsin, I learned a new word — "Arvinizing".

I knew immediately what the word meant and I think most of you also know what it means.

It's a short-hand way of referring to what Arvin Smith teaches the management of an acquired business.

I'm not smart enough to tell you how he does it, or what he teaches, but I do know that Arvinizing is very effective and produces results, often changing an acquired business from mediocrity to excellence.

I think some of what Arvin does is to give focus and direction to an organization that previously has lacked both of those vitally important management tools.

Instead of well-intentioned managers trying to do the right thing but actually pulling in different directions, Arvin gets the management team of the acquisition to focus on common goals and then pull together to achieve those goals.

The key to the success of Arvinizing an acquired company may simply be that Arvin sets goals for the management team and then lets every member of the team know what those goals are, both their individual goals and the team's collective goals.

That may sound pretty basic, but often just knowing what their specific goals are gives a management team a sense of purpose that can make a big difference.

Others in top management do this same thing with new acquisitions, but Arvin Smith set the pattern.

Many years ago, something happened at Rubbermaid that gave me a lasting impression of the very important difference between a long-range point of view and a short-range outlook.

For several years after I became CEO of Rubbermaid in 1959, many companies were attempting to acquire us.

Our major stockholders were undecided as to whether their best interests would be to sell or to continue operating as an independent company.

The problem was that those stockholders who really did not want to sell would not come out and say so.

Instead, they said that they were willing to sell but at a price that was always twice as much as the company's market value.

And, of course, as the market value of the company increased, their price increased in direct proportion.

So each time there was an offer, those stockholders who were in the majority took the position that the price was not high enough.

After we had considered more than 20 such offers, one of my very best friends in business, Lee Waterman, the Chairman and CEO of Corning Glass Works, came to me and said that Corning would like to acquire Rubbermaid on a friendly basis.

Lee said that Corning would offer 140 percent of the then market price of Rubbermaid stock in the form of Corning stock.

I called a special meeting of the Rubbermaid Board of Directors and told them about Lee's offer.

My recommendation to the Board members was that if they were going to consider any offer in the next five years, they should accept Corning's offer.

I knew Corning to be a growth company with management committed to high principles and the highest standards of ethics and integrity — people with whom I was sure we could work well as true partners.

A portion of Corning's business was in the housewares industry and, therefore, I believed they would bring to the table a better understanding of our business than any other potential buyer.

I added, however, that our own Rubbermaid management team — the Operating Committee — felt that if we were given a chance, we could increase the market value of the company's stock to produce a better deal in the future than would result now from acceptance of the current Corning offer.

Essentially, I told the Board members that if they would give us an opportunity to manage the company without taking the time to review other acquisition offers, we were confident that, within five years, we could increase the value of their Rubbermaid stock more than 140 percent of the value of Corning's stock.

After a day and a half of meetings and deliberation, the Board decided not to sell and to give us the chance to prove ourselves.

Because we had announced Corning's offer, arbitrageurs and brokers were busy acquiring Rubbermaid stock.

The day after our Board turned down the offer, I was on the telephone most of the day taking calls from brokers.

Each of the callers basically asked the same question: "How could your Board turn down an offer of 140 percent of the market value of your stock?"

My response was, "It's easy.

Our Board felt that we could make Rubbermaid stock worth more than 140 percent of Corning stock in five years."

This statement typically evoked a bombastically loud and incredulous, “Five years?”

It was an alien timeframe concept for a financial community that even then seldom looked beyond next quarter’s results.

But having established that target made it possible for me to take a long-range point of view in managing Rubbermaid because I knew, in no uncertain terms, that I was working for stockholders whose timeframe of success was five years.

I would not be standing here telling you this story if we had not succeeded in meeting our deadline.

As a matter of fact, we greatly exceeded it.

In five months, Rubbermaid stock was worth more than 140 percent of the value of Corning stock and has had a higher value in relation to Corning stock ever since.

That experience gives me an unusually strong appreciation of the role that a long-range point of view has played in helping Thermo Electron management build a strong company.

Now I want to turn to the second basic strength — a corporate culture that encourages and fosters creativity and innovation.

Creativity and innovation are both dependent on management's allowing employees to try new things, to take risks, and ultimately their willingness to accept graciously some failures along with the successes.

The elements of risk and possible failure are why it is so difficult to create a culture today that fosters creativity and innovation and why such cultures do not exist in most companies.

Instead, in those companies people waste a lot of time defending the status quo, clinging to their old ways, and defending their turf against new ideas.

At Thermo Electron, management took the lead by rewarding employees for trying new product ideas, new methods, and new business practices.

And when the new approaches did not work, management responded with encouragement rather than punishment or harsh criticism.

The culture that resulted has enabled Thermo Electron and its divisions and subsidiaries to develop new products, enter new markets, and even create a new organizational structure.

Among the new products that have resulted from a culture in which creativity flourishes is the bottle sniffer developed by David Fine.

This innovative product rapidly and accurately detects any contaminants in plastic Coke bottles as they are being cleaned for recycling.

Other recent examples include a laser method for removing unwanted hair and a flashlight that uses compressed natural gas.

This climate, favorable to new ideas, also many years ago enabled the financial people at Thermo to develop and use a new management tool for measuring performance. The new tool was “Return on Assets” which in my opinion has made a tremendous difference in Thermo’s success.

A culture that fosters new ideas also helped John Hatsopoulos to originate the idea of spinouts which has become an organizational strength for Thermo Electron.

The spinout concept, which would not have worked in most companies, has worked at Thermo because of the unique capabilities and character of George Hatsopoulos.

Very few CEO’s would have been either able or willing to delegate authority to the extent necessary to make the spinout concept work.

It takes an executive with tremendous self confidence and an unusual ability to appraise what is being done and to give the right level of counsel and advice while letting the managers of the spun out operations truly run their businesses.

And while they are running the spun out businesses with a great deal of entrepreneurial autonomy, they can draw on the tremendous resources that are available from the parent company — resources that include financing, counselling, and manpower.

Because of the Thermo's sterling reputation, financing is not only available in large amounts, but also at lower cost.

In some cases, Thermo Electron actually guarantees the principal, which further reduces the cost of financing the subsidiary.

Few, if any, new businesses have the high quality of counselling and advice that's available to the Thermo spinouts, from both the parent and sister companies.

And, finally, there is the availability of manpower. The fledgling subsidiaries are able to call on the parent company for executives with many years of experience and highly developed skills.

It's as if a sandlot baseball team located in Concord, Massachusetts were able to draw on the Boston Red Sox for their players.

What chance would another sandlot team have against such a line-up?

By encouraging new ideas and refusing to accept business as usual, Thermo Electron's management has created a strong and highly productive culture which has generated everything from innovative new products to a bold new organizational structure.

Now I want to turn to the third basic strength of the company — its principles and its high standards of ethics and integrity.

These principles and standards are embodied in one of the written policies of the company, one entitled “Business Conduct Policy”.

The very first sentence of that policy reads as follows:

“It is the policy of Thermo Electron Corporation and its subsidiaries and divisions to require the highest standards of business ethics and integrity on the part of all officers and consultants.”

Note it does not say “high standards of business ethics and integrity”.

It says “THE highest standards,” so there is absolutely no question as to what is meant.

In the letter George Hatsopoulos wrote to accompany the policy when it was distributed to all employees, he started with this paragraph:

“Since our organization in 1956, Thermo Electron Corporation has required the highest standard of business ethics and integrity of its officers and employees. Our adherence to strict ethical standards has contributed directly to the success of our company.”

To me, it is very significant that George recognizes ethical standards as an important contributor to Thermo Electron’s success.

In other words, adherence to the highest standards of ethics and integrity goes beyond the code of behavior by which George and the other employees of Thermo Electron choose to live their lives.

It is a potent market force that supports and fosters the company's reputation for excellence and fair dealing with consumers, customers, suppliers, governments, and local communities — in short, all those who deal or may deal with Thermo Electron.

From my personal point of view, this is an important point because I would not want to be a director of a company that did not subscribe to the very highest standard of business ethics and integrity.

I also think one of the most important factors in Rubbermaid's success over the decades has been the re-dedication by each generation of management to conducting the business in accordance with a philosophy based on ethical principles and standards.

I inherited an unwritten but well-developed philosophy and set of operating principles from James Caldwell, my predecessor as CEO.

Because I thought they were important concepts that should be communicated to all employees, I had the philosophy and operating principles published as a printed statement.

Over the years, that statement has been updated but essentially the same concepts are in the latest version which is prominently displayed in our headquarters lobby in Wooster, Ohio, and has been distributed to all our employees, suppliers, and customers.

That's why the "Arvinizing" concept resonates so strongly with me.

Setting goals and laying out the ethical guidelines to be followed in achieving those goals is an integral part of the Rubbermaid culture in which I have spent my working life.

George tells me that one of his concerns today is how he can best communicate to newly hired employees and the employees of acquired companies the importance of operating in accordance with the highest standards of business ethics and integrity that have become such a vital part of Thermo's traditional culture.

Some months ago, he asked me to come to participate with the operating committee discussing how this could best be done.

During that discussion, I developed some thoughts I want to share with you now about how Thermo Electron can build on the firm foundation of its basic strengths to continue its success in the future.

A key concept for success in the emerging global marketplace of the 21st century is value.

For the first time in history, consumers are able to buy goods made anywhere in the world and value is the main driver of their buying decisions.

Value does not always mean the lowest price — true value consists of the optimal combination of price, quality, service, timeliness of delivery, and innovation.

One of these key elements in creating and maintaining value is innovation — one of the Thermo Electron culture's basic strengths and a market advantage on which you can build.

Continued investments to support constant research and development efforts will create the new products that provide enhanced value for customers by meeting their needs in innovative ways — the bottle sniffer, for example.

Another and often overlooked aspect of innovation is the willingness to obsolete your own products when they no longer represent the best possible value.

It is far better for you to do it yourself than to allow a competitor to obsolete your product by leapfrogging you in any aspect of product value — price, quality, innovation, or service.

Culling out obsolete products also can produce substantial bottom line savings by paring back on slow-moving inventory.

Advanced technologies, especially those based on computers, are powerful tools for achieving Thermo Electron's long-term growth during the new century that is just around the corner.

Part of Thermo management's focus on long-range opportunities will certainly involve assessing the appropriate levels of investment in new technology, not as an end in itself but as the means for achieving the innovation, quality, and timeliness that are key value elements.

Another area of future increased strength for Thermo Electron is customer service.

Improved service goes way beyond delivering the product on time.

It means discovering the customer's needs and working to satisfy those needs quickly and efficiently.

It may mean changing a product to improve it or even developing an entirely new product.

There are plenty of opportunities for Thermo Electron to apply its innovative skills to improving customer service.

So who is going to do all of these things? Developing innovative new products, identifying and applying advanced technologies, improving customer service?

The answer is simple and the same as it has always been — people.

People like those of you in this room.

People like your counterparts who are meeting in two other regions of the country.

And ultimately all of the people who together make up the corporate entity called Thermo Electron.

And here again Thermo Electron enjoys a cultural advantage in dealing with people.

That advantage can best be summed up in one word — "caring."

Thermo's management has been willing to go way beyond what is required by labor laws and federal regulations.

They have gone way beyond what might be considered fair.

They have respected the dignity of the individual.

I have seen George and other top Thermo executives find ways to redefine a person's job to make better use of their strengths where they may have failed previously because of weaknesses in some areas. That is caring.

Employees have responded to this "caring" approach from management with intense loyalty and with extraordinary effort.

Caring about employees has resulted in a very low turnover rate of Thermo employees at all levels, including management.

In addition to paying off in terms of avoiding the high cost of hiring and training new employees, caring about people will help Thermo Electron get and keep its fair share of the shrinking pool of skilled workers expected by the year 2000.

In summation, that's my view as a director of Thermo Electron as I see it today — a successful company blessed with a management that takes the long-range view, a management that encourages and fosters innovation, and a management that adheres to the highest principles and standards of business ethics and integrity.

My ideas concerning the company's future are based on a future that can be achieved by building on the integral strengths of Thermo Electron's traditional culture.

I am proud to be associated with this company and with all of you.

Thank you.

Noble\TE-Talk