Leadership, Model Thinking, and Value Creation

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Our Roadmap

Leadership

Who Does What?

Who are the leaders of a firm and what are their roles?

Shareholders
- Value the enterprise
- Elect the Board

Board Members
- Fiduciary oversight
- Delegate authority to Management
- Engage actively with Management

Management
- Create the model
- Cultivate options
- Engage actively with the Board

Today we will focus on two primary tools used by the Board and Management: Model and Execution Value

Shareholders

Board Members

Management

Decision Making and Communication Tools

The Model

Execution Value

The Model

Our Playbook for Execution

What is a Model?

- A conceptual, ideal representation of a system or organization (in this case, a company)

- Made up of components or "Elements" that can range from abstract to tangible

- NOT a budget

Our goal: Define the Model explicitly to create a useful tool for

- Leadership

- Decision making

- Communication

Building the Model has four key steps

1. Identify the Model <u>Elements</u>

2. Assess our <u>Understanding</u>

3. Evaluate the underlying <u>Volatility</u>

4. Build the <u>Value Creation Roadmap</u>

What are the Model Elements?

- The Elements are individual components that, when taken together, comprise the Model

- Each Element can have sub-models (like Fractals)

How are Model Elements created?

- Data

- Trends

- Analogy

- Comparable Businesses

- Insight

- Aspiration

- Imagination

Best Thinking

"Logic will get you from A to B. Imagination will take you everywhere"

— Albert Einstein

Let's look at some example Model Elements

Broad	Specific
Vision / Mission / Purpose	Product / Marketing
Culture / Talent Development	Revenue
Value Proposition	Cost Curve / EBITDA
Design	Capital
Technology	Return on Capital

Each Element has a Plan, Leader, KPIs, Capital Required, and multiple sub-Models

Once the Elements are defined, we can assess understanding and volatility

Understanding: What do we know?

Volatility: Is it predictable?

For each Element, we can define the level of understanding and volatility to find gaps and build the capital strategy

Element	Understanding *	Volatility
Vision / Mission / Purpose	100	Low
Team Culture / Talent Development	100	Medium
Value Proposition	90	Medium
Design	85	Medium
Technology	75	Low
Marketing	50	High
Revenue	50	High
Cost Curve / EBITDA	75	High
Capital	75	Low
Return on Capital	75	Medium

* Relative to what is knowable

Examples of Understanding and Volatility

	Low Volatility	High Volatility
Low Understanding	Cost Structure	Revenue
High Understanding	Rent	Weather

Now that we have a Model, it becomes our primary Leadership tool

- When communicating with the market, the Model is the chief leadership voice

- Within the company, the Model is also a tool for communication, learning, and decision making

To the outside world, the Model is the primary Leadership Voice

- The Model is the clearest picture of what management is trying to achieve

- External parties will adjust the Model for their own evaluation (security pricing, credit underwriting, etc.)

- However, the Model remains as the voice of leadership and our true benchmark

Internally, the Model simplifies Management's communication with team and Board members into a few recurring questions...

1. Are we on Model?

2. Did we make a mistake?

3. Is it volatility?

4. Is the Model correct?

5. How long to get on Model?

...To drive learning and strategic decisions
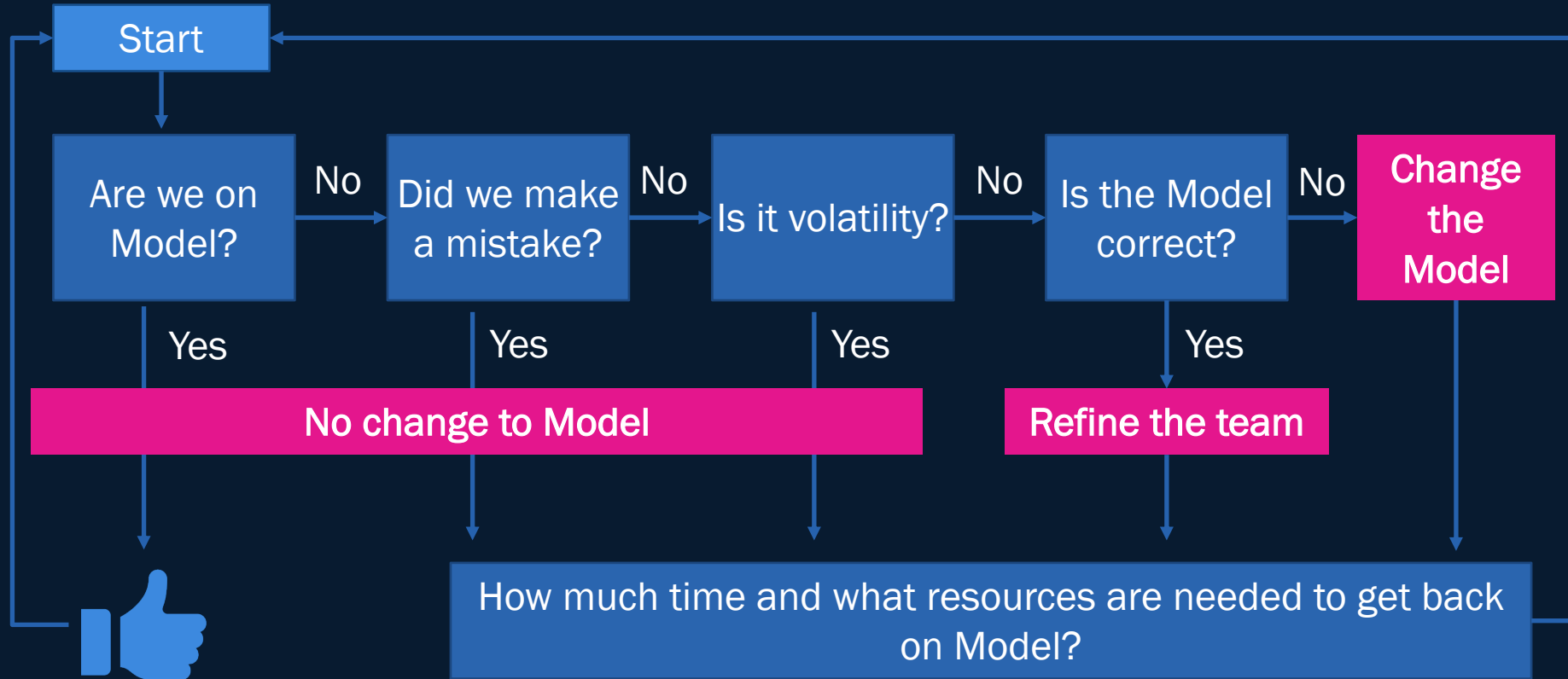
Iteration is key to improving – Faster cycles means faster learning and improving
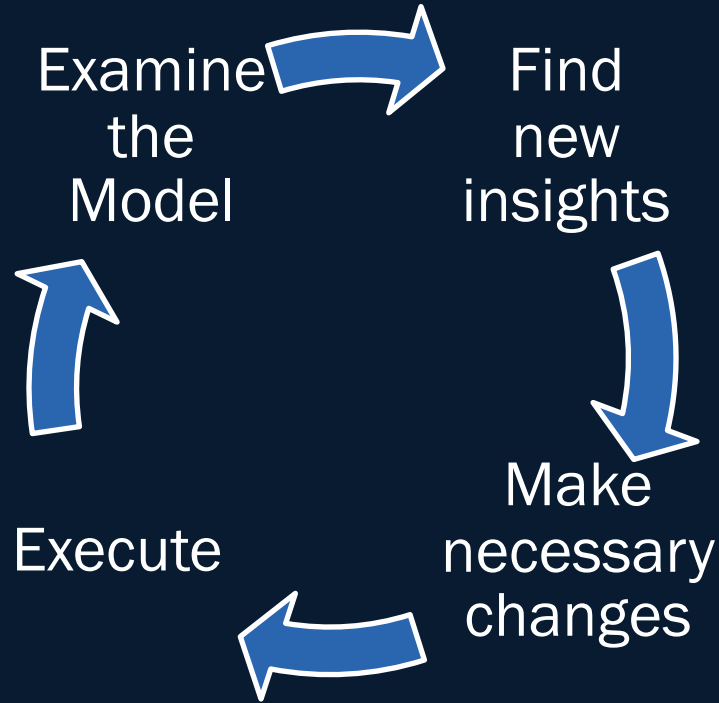
The Model is not set in stone – It changes with our best thinking!

Execution Value

Connecting Strategy and Firm Value

What makes up the value of a company?

Enterprise Value **=** **Execution Value** **+** **Option Value**

- Economic Impact
- Social Impact

Execution Value is the current value of the company's strategy _if executed on model_

Future company performance (On Model) ✖ Valuation multiple ✖ Discount factor

= Execution Value (Today)

With Execution Value, we can measure the value of executing certain strategies and sensitivity to changes in the model
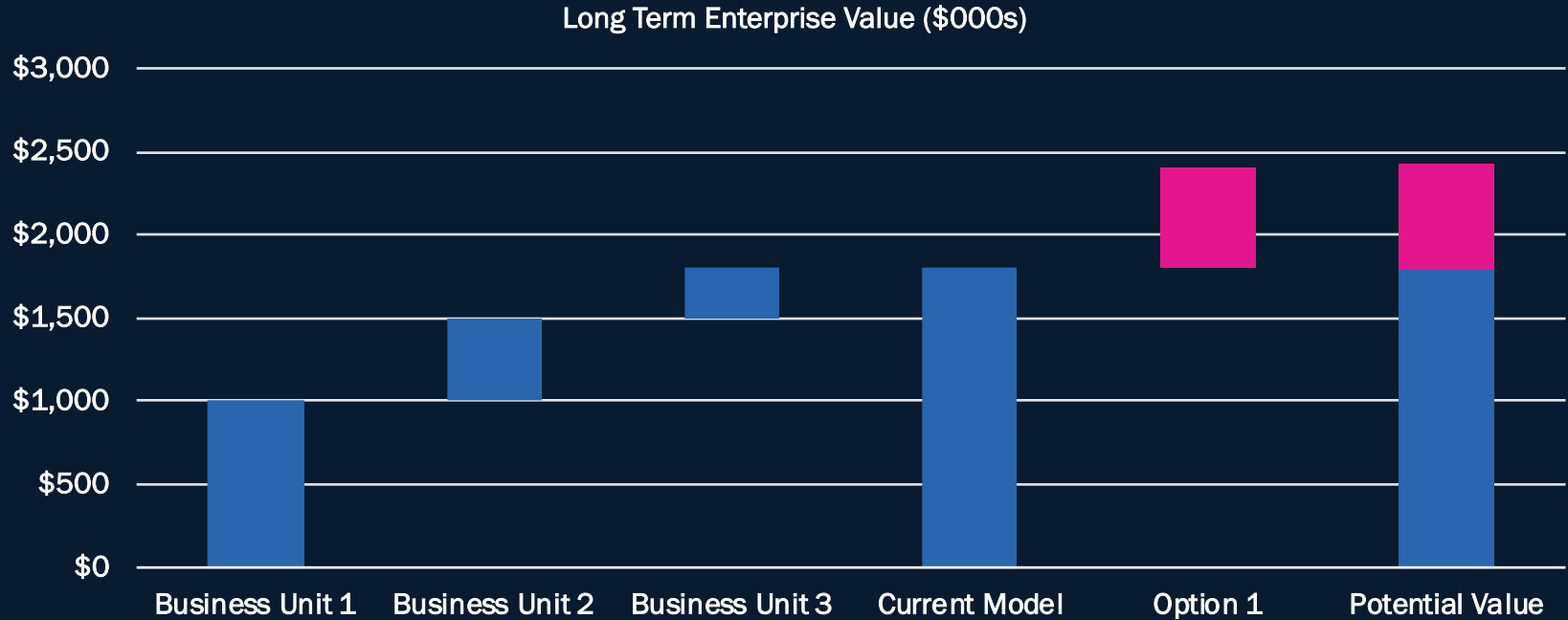

Execution Value
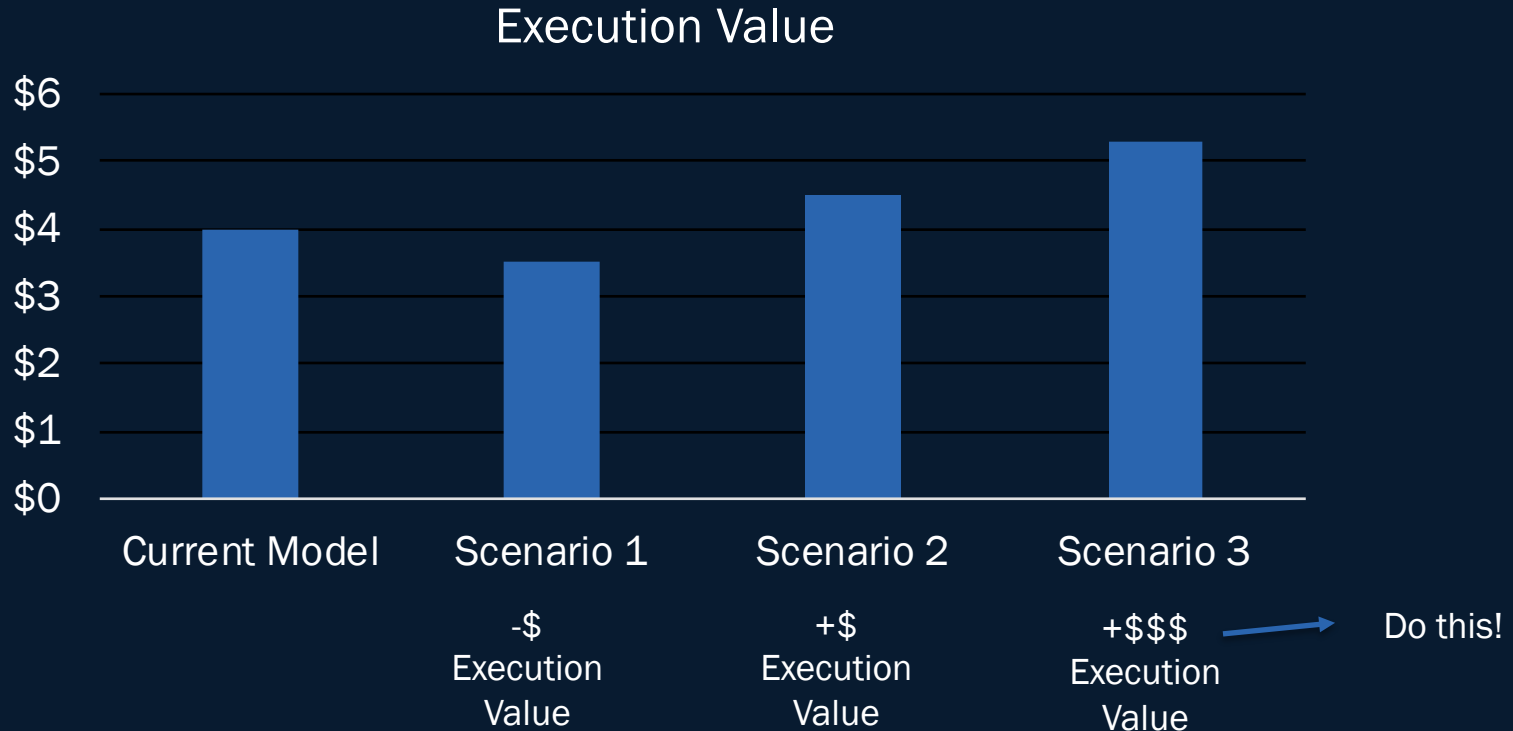
Every firm also has embedded option value

- Everyone in the firm is encouraged to create new options for value creation

- With the Board's guidance, the CEO chooses which options to exercise

- Once an option is exercised, the Model is updated to reflect it

Option

Option

Option

Option

Option

The Company

Value Creation Block

Value Creation Block
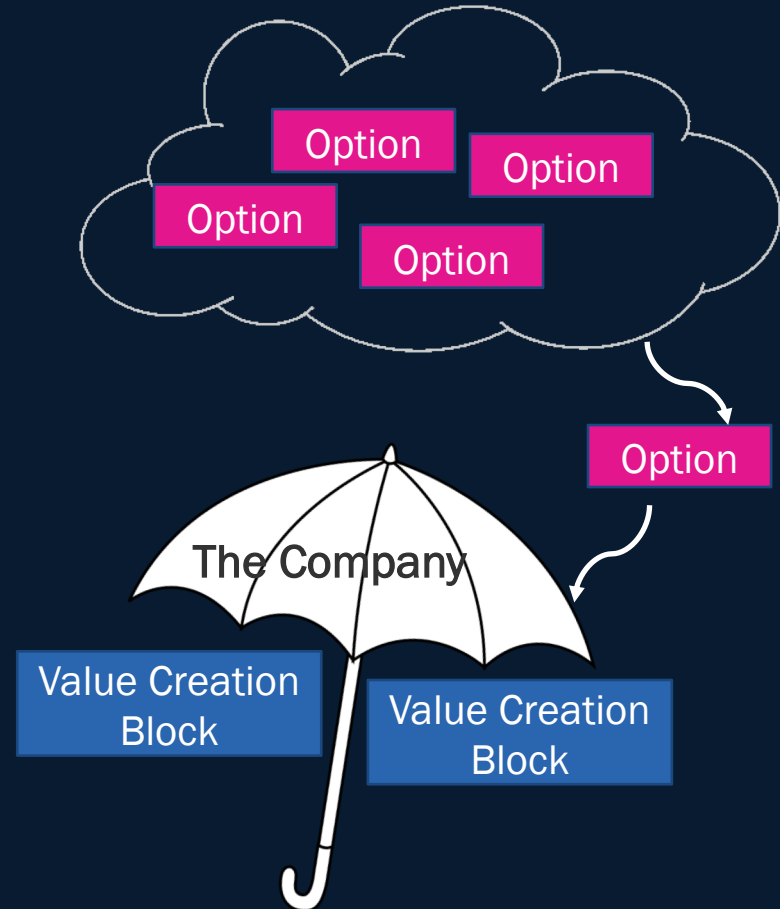
The Value Creation Roadmap quantifies the long term economic value of the Model and Options

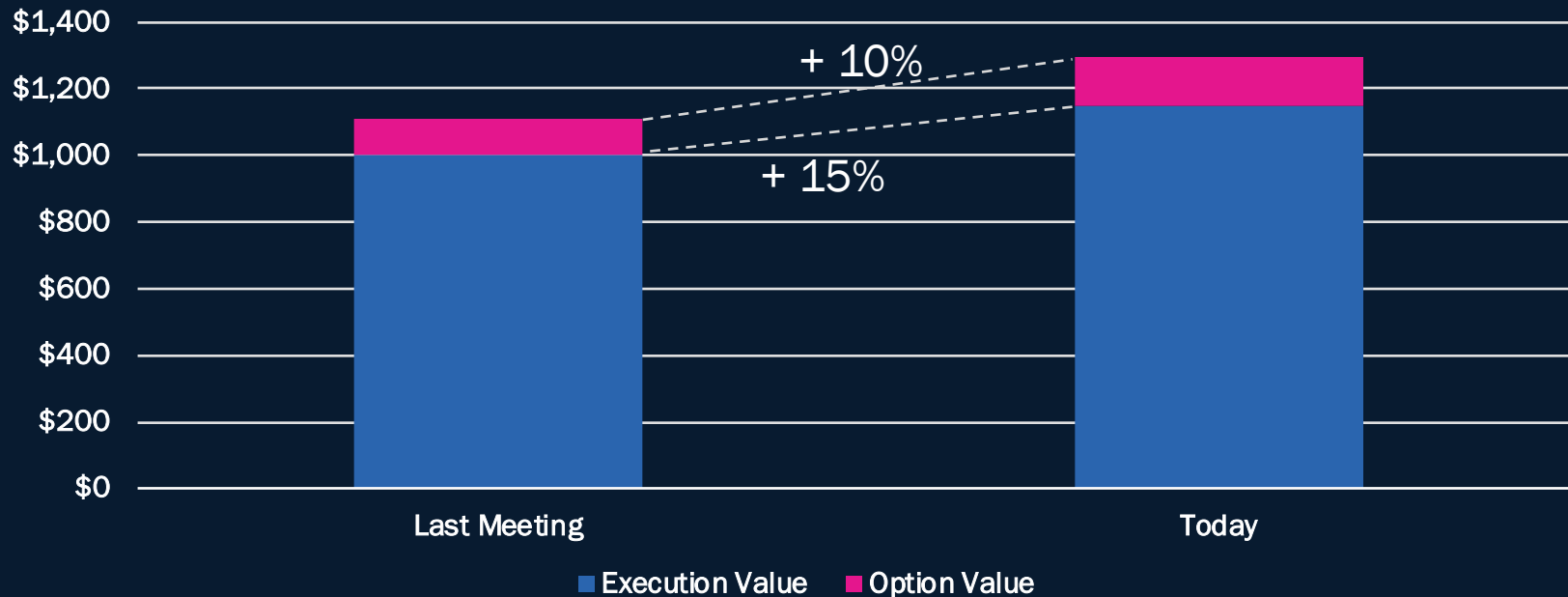Long Term Enterprise Value ($000s)

So what?

The Board and Management dialogue has a new roadmap

- The Value Creation Roadmap (Economic Value and Social Value)

- Performance vs. Model (Not Budget)

- Current Execution Value

- Option portfolio

- Compensation

Here is an example of a board report for ExponentialCo:

Execution Value has increased 15%

Components	Change	EV	EV / share
	Last Meeting	$1,000	$1.00
Time Value	Time Value (3 mos)	$40	$0.04
Existing Model	Revenue Model change	($75)	($0.08)
	Cost Curve Improvement	$35	$0.04
New Models	New Model Added	$100	$0.10
Discount Rate	Discount Rate reduction	$50	$0.05
	Today	$1,150	$1.15

We have added 2 new options

Option	Option Value ($MM)
Launch Exponential Shoes	$10
Expand to Antarctica	$0.05
3-D Print Personal Drones	$100
Birthday Parties on the Moon	+$15
Uber for Cats	+$25
Total	$150

Compensation Scorecard

Section	Payout Model	Award
Execution Value	Standard Comp Model	Cash + Options
New Option Creation	Discretionary Cash Bonus	Cash
Exercise/Capitalize an Option	[X %] of Pre-Money Value	Options
Social Impact	TBD	Cash / Options

Final Thoughts -
What are the outcomes of Model Thinking?

- <u>Inclusive</u> Leadership community driven by creation, insight, and execution

- Focus is on <u>long term success</u>, not short term results

- <u>Common language</u> and tool with which to communicate about the business

- Compensation models change to reflect <u>Value Creation</u>

Thank you