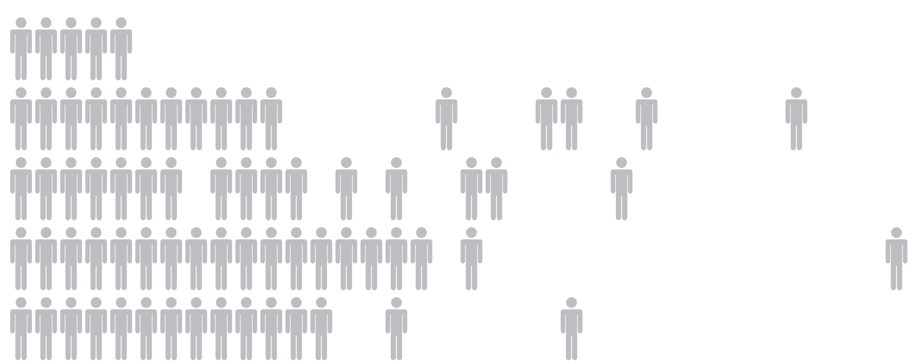
2014 Egon Zehnder Global Board Index™

Achieving Global Board Capability:

Keeping pace with global opportunity

EgonZehnder

Contents



INTRODUCTION

Companies with global aspirations require boards with global capability. So why don't their boards reflect this new strategic direction?

As U.S. economic growth slowed over the last decade, companies across the country successfully chased and found growth opportunities overseas. Nearly three-quarters of all S&P 500 companies now report some amount of international revenue. So why don't their boards reflect this new strategic direction?

At Egon Zehnder, we call the disparity between a company's global footprint and the ability of its board to guide and advise leaders on global matters the Board Global Capability Gap. We first started tracking the global capabilities of boards in a systematic way in 2008, creating a measurement tool called The Global Board Index™ (GBI™).

We have continued to analyze board capability year over year, and the 2014 index that follows serves both as a snapshot of present-day board practices and composition, as well as a longitudinal picture of an evolving capability among S&P 500 companies.

Not surprisingly, companies with global expertise in the boardroom have a better understanding of how to leverage the opportunities associated with global expansion and are better able to exploit the upside and minimize the downside of operating overseas. The good news is that our research shows that the share of directors with meaningful international work experience among S&P 500 directors is now at 14.1%, up from 8% in 2008. But despite this progress over the past six years, our analysis reveals that even among those companies that have improved their global capability, there is still significant room for improvement.

We work with a number of Nominating and Governance Committees who effectively mind their own "Board Global Capability Gap" with objective and proactive board succession planning. These are the companies, willing to embed global expertise at the board level—or enhance what they've already got—who will create real competitive advantage and generate accelerated gains in the years ahead. I hope you find the insights from our 2014 index relevant and useful in your discussions about board composition and succession planning.

George L. Davis, Jr.
Co-Leader, Global Board Practice

THE CONTEXT: WHY IS GLOBAL CAPABILITY KEY?

The current focus on global growth and global capability can be attributed in large part to the U.S. financial crisis of 2008. In the wake of the collapse, domestic growth stagnated, especially among the S&P 500.

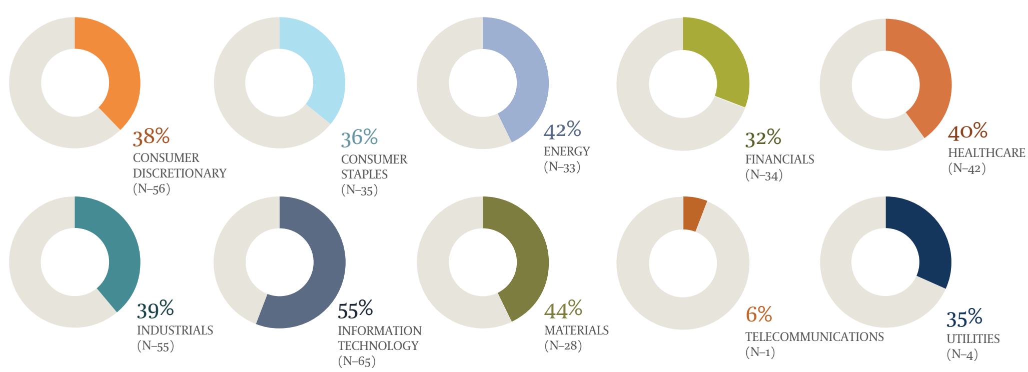
To their credit, U.S. companies chased and found growth opportunities overseas. As a direct consequence, the U.S. economy today is far more global than ever before, and corporate America's global imprint is vast and expanding. For example:

- 72% of all S&P 500 companies now report some amount of international revenue.
- International revenue as a share of total revenue is 37%, up 5.5 percentage points since 2008.

Of course, this picture is far from monolithic. Reliance on international revenue varies considerably by industry. With an average share of international revenue at 55%, the Information Technology sector has the greatest exposure to international revenue sources. Materials follows at 44%.

Globalization also varies extensively by industry. Nearly all S&P 500 companies in Materials, Information Technology, Industrials, and Consumer Staples have international revenue, but a smaller share of companies in Financials, Telecommunications, and Utilities report international revenue.

FIGURE 1: SHARE OF INTERNATIONAL REVENUE FOR S&P 500 COMPANIES REPORTING INTERNATIONAL REVENUE



globalization is the order of the day

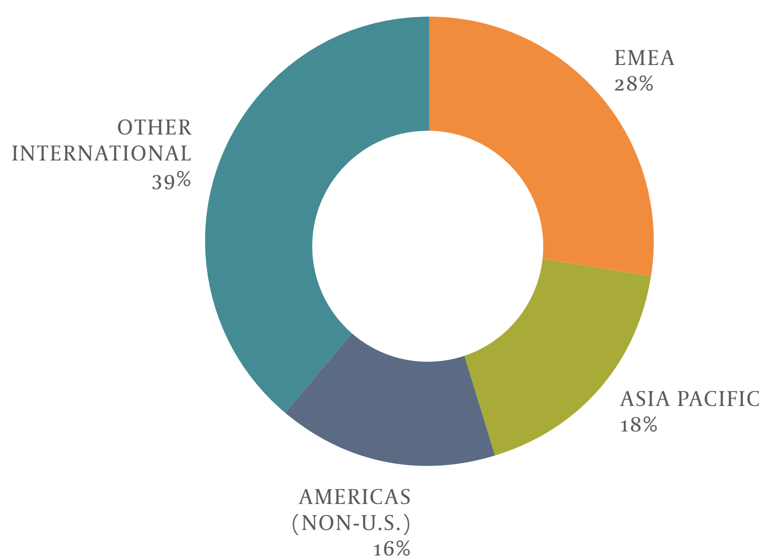
Finally, international revenue varies by region. American companies that disclose international revenue gain the most from Europe, Middle East and Africa (EMEA). Roughly 3 in 10 U.S. dollars of international revenue is generated by EMEA.

It seems clear that globalization is the order of the day—and will only become more important in coming years. To summarize the state of play today: Almost three-quarters of S&P 500 corporations now report international revenue, and among those organizations, almost two out of every five dollars they earn come from overseas.

This is a sophisticated population of companies. Its members are accustomed to competing effectively and efficiently on a number of fronts at once, ranging from sourcing to logistics to finance. In the continuing quest for the next competitive edge, many firms have now begun examining their own boards. Can the right board, purposefully assembled, provide such an edge?

The answer is an unqualified yes.

FIGURE 2: INTERNATIONAL REVENUE FOR S&P 500 COMPANIES BY REGION



THE 2014 GLOBAL BOARD INDEX

companies with global aspirations need boards with global capabilities

Egon Zehnder created the Global Board Index (GBI) in 2008 to track and evaluate trends among S&P 500 boards relative to board composition, global capability, and business performance.

The 2014 Egon Zehnder Global Board Index (GBI 2014), like its predecessors, provides an assessment and analysis of global capability in the present-day S&P 500 boardroom. Where possible, GBI 2014 makes comparisons across past data to reveal trends. In addition, the 2014 report offers new analyses and ways of interpreting global board capability, strategic resonance, and the deficit of global talent in corporate America.

In GBI 2008, Egon Zehnder identified this deficit of globally minded board talent and framed it as the "Board Global Capability Gap." Defined as the disparity between a company's global footprint and the ability of its board to guide and advise leaders on global matters, the Board Global Capability Gap underscored the need for change in the board composition of U.S.-based companies.

In 2008, the Egon Zehnder team hypothesized that increased awareness of the Board Global Capability Gap would engender corrective action in American boardrooms. The rationale was that calling attention to the shortage of global talent—and also linking board composition to business performance—would prompt and inform actions to close the Board Global Capability Gap.

But as the GBI 2014 data presented in the following pages illustrate, change is slow. The reforms needed to optimize board composition and effectiveness in the fast-moving global construct are difficult to address. Creating boards with directors who have the right mix of skills, experiences, perspectives, and mindsets requires fundamental overhaul that starts, but certainly doesn't end, with recognition alone.

Given the importance of global board capability and the lack of progress toward reducing the global talent deficit, more direct treatment seems warranted. In addition to framing the current data analysis in terms of opportunities and imperatives, GBI 2014 presents a conceptual analysis addressing the barriers to change that may exist for companies seeking to develop boards with more global directors.

closing the Board Global Capability Gap requires an effective process—one that recognizes the value of global talent and how to identify and attract it

Closing the Board Global Capability Gap requires an effective process—one that recognizes the differentiated value of global talent, and fosters an understanding of how best to identify and attract it. Building boards with global capability is clearly not about checking a box. If it were, the U.S. boardroom would already look very different. Building boards with global capability for today and tomorrow demands expertise—including skilled reconnaissance—knowledge, and resourcefulness.

Companies with global aspirations need boards with global capabilities. And in turn, boards need directors with global mindsets who can add diverse perspectives of thought and experience. Ultimately, GBI 2014 provides data-driven insight to motivate board assessment and recommendations for development activities so that with ongoing effort, American corporate leadership can close the Board Global Capability Gap and enhance the competitiveness of U.S.-based companies.

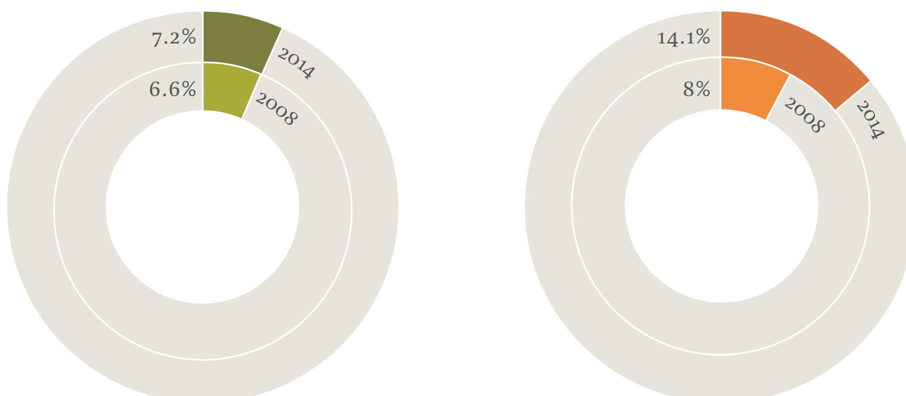
from the data: a mixed report card

Now let's turn to the data. What does the American boardroom look like today in terms of global capability? What's changed since 2008? What do the numbers suggest?

The shortage of global talent identified in the GBI 2008 continues in 2014. Although change is happening, it is incremental and the pace is slow.[1]

FIGURE 3:
S&P 500 DIRECTORS WHO ARE FOREIGN NATIONALS

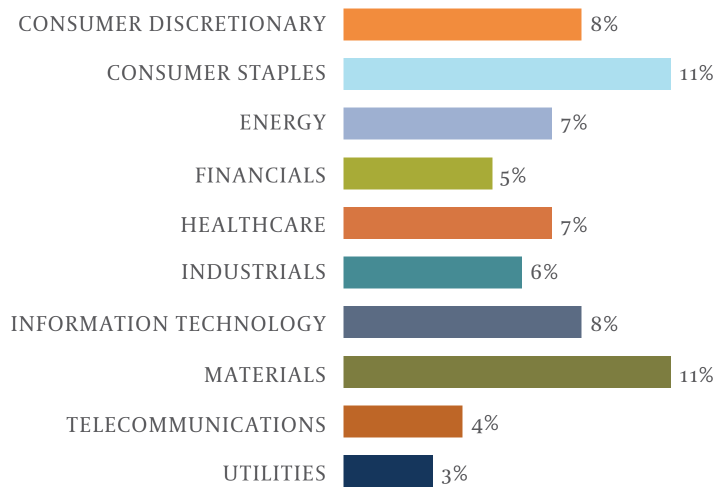
S&P 500 DIRECTORS WITH INTERNATIONAL WORK EXPERIENCE



Six years ago, percentages of foreign nationals with board seats and directors with international work experience measured 6.6% and 8%, respectively. In 2014, 7.2 % of all directors are foreign nationals and 14.1% of directors have meaningful international work experience—even though nearly three-quarters of all S&P 500 companies report international revenue. As the following two graphics indicate, these measures vary marginally across industries, with Consumer Staples and Materials reporting the most foreign-national directors, and Consumer Staples companies reporting the most directors with international work experience.

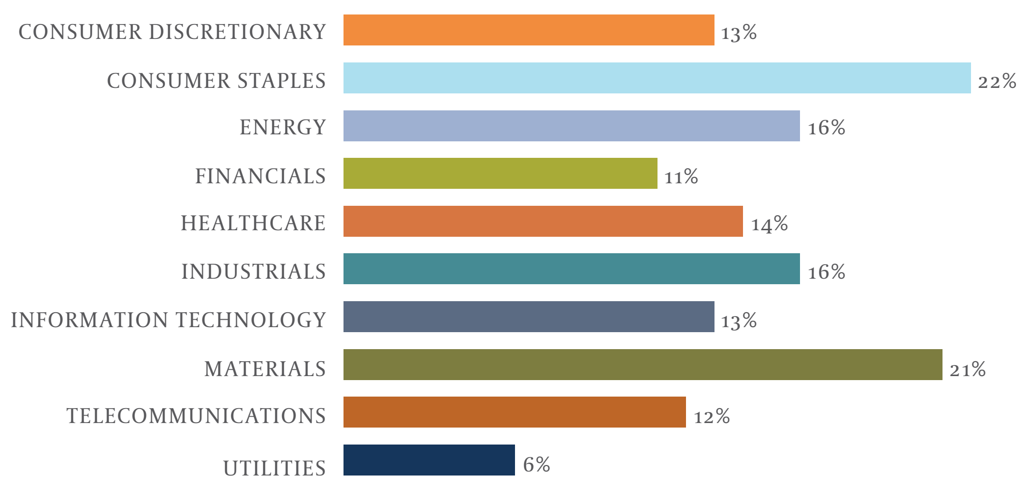
1 Direct numerical comparisons for board global capability between 2008 and 2014 are not possible because the measure of board global capability in GBI 2014 is a new formula. But comparisons between the two variables that make up the construct are possible, so when looking for trends in board global capability, we compare over time the shares of foreign nationals and the shares of directors with international work experience.

FIGURE 4: SHARE OF S&P 500 DIRECTORS WHO ARE FOREIGN NATIONALS



Over time, the major source of improvement in global board capability has come from the placement of more directors with international work experience. There is therefore a growing recognition of the need for companies to build pools of local-national talent, which over the long term will fill this pipeline.

FIGURE 5: SHARE OF S&P 500 DIRECTORS WITH INTERNATIONAL WORK EXPERIENCE



better than four in ten—44%—of companies have at least one foreign national director, but only 17% have two or more

Companies that operate only in the U.S., not surprisingly, have minimal foreign-born representation on their boards (3%), and somewhat more respectable numbers of directors with meaningful international work experience (8%). Among companies who report international revenue, the share of foreign nationals increases to 9% and the share of directors with meaningful international work experience is 17%.

FIGURE 6: BOARD COMPOSITION, GLOBAL CAPABILITY, AND INTERNATIONAL REVENUE

Clearly, the aggregate portrait of global expertise among the S&P 500 improves slightly when we look only at companies with revenue from abroad. Nevertheless, given the clear need for this type of capability in the boardroom, even within this subgroup the average distribution of global talent is still considerably lower than expected. We can safely infer that modifications to board global capability prove challenging even for those companies best served by it.

GBI 2014 numbers show that the largest S&P 500 board has 19 directors and the smallest 5, with the average number of directors per board being 10.7. (There was no difference in the size of boards based on whether or not their companies had international revenue.) The number of foreign nationals on a board ranges from 0 to 7. The number of directors with international work experience on a board ranges from 0 to 8. Better than four in ten—44%—of companies have at least one foreign national director, but only 17% have two or more.

To see what is happening on the boards of America's 100 most global, large publicly-traded companies—those who earn more than half of their revenue outside of the U.S.—we ranked boards by their share of international revenue. The numbers for board composition didn't change. Even among this group of "most global" companies, only:

- 1 in 10 directors is a foreign national
- 2 out of 10 directors report significant international work experience

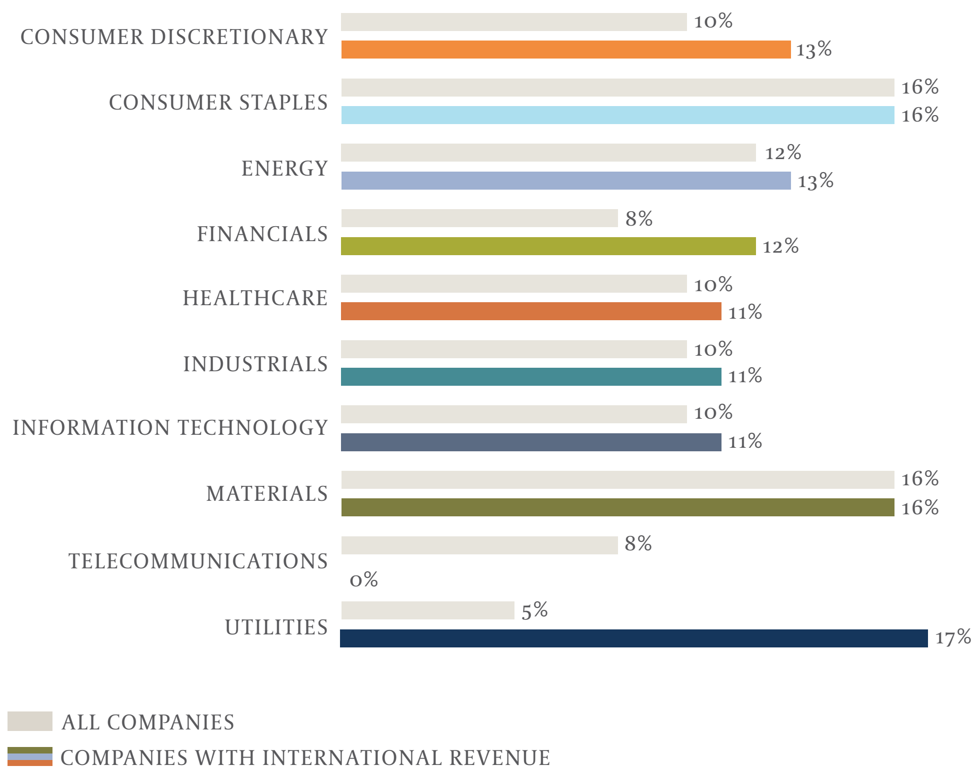
Even among companies who depend significantly on overseas markets for revenue and revenue growth, very few American companies have truly global boards capable of advising and guiding the leadership team on global matters.

introducing the Board Global Capability Score

GBI 2014 introduces a new Global Board Capability Score, an expression of a board's global expertise that is defined by the percentage of board members who are foreign nationals and/or who have meaningful international work experience. The score can be used to track and evaluate the overall board global capability score of the S&P 500, of industries and sectors, and of individual companies.

To see if there was a difference in board global capability at the industry level based on whether or not companies derived sales from overseas, Board Global Capability Scores for each industry were compared for companies with international revenue, and for all companies in each industry.

FIGURE 7: BOARD GLOBAL CAPABILITY SCORES



Again, global capability varies by industry—this time, more dramatically. Companies with international revenue tend to have more global capability on their boards. It's worth noting again, in this context, that Consumer Staples and Materials have the highest shares of directors with meaningful international work experience.

But regardless of whether or not companies have international revenue, we must once again reach the same conclusion: Board Global Capability remains low.

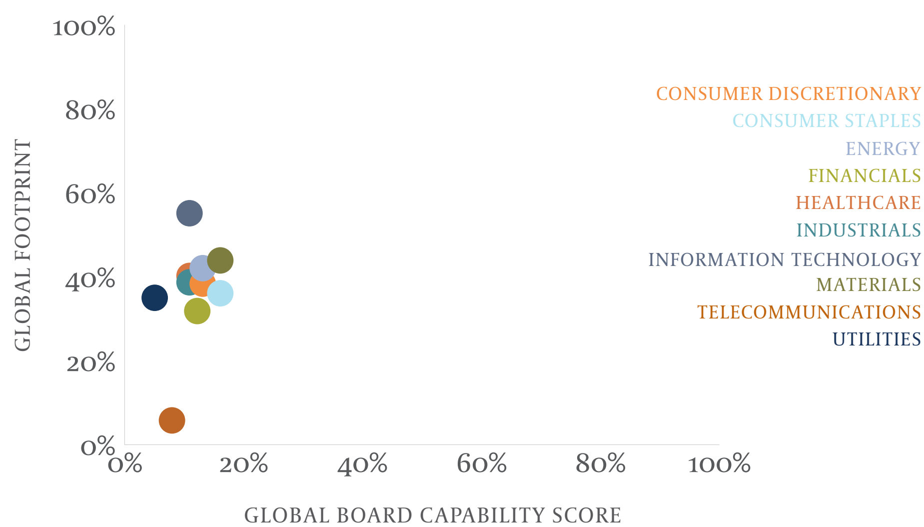
assessing the Board Global Capability Gap

We have defined the Board Global Capability Gap as the difference between a board's global talent and its global footprint. To fully understand and assess the Board Global Capability Gap, we need to define the concept of global footprint. For this analysis, Global Footprint is a representation of the extent to which an industry's revenue is generated internationally. To calculate the Global Footprint, for each company in an industry we calculated the percentage of international revenue to total revenue. We then took averages for each company within an industry.

By creating and categorizing industry scores for Board Global Capability and degrees of Global Footprint, comparisons can be made between optimal board composition and what exists for each industry. Quite simply, the difference indicates a collective Board Global Capability Gap among companies in that industry.

It is important to note that in all cases, global board talent is low. Even industries, such as Consumer Staples, where the Board Global Capability Gap is relatively small, there is still a 20 percentage point difference between the industry's Global Footprint and its Board Global Capability Score.

FIGURE 8: BOARD GLOBAL CAPABILITY GAP
FOR COMPANIES WITH INTERNATIONAL REVENUE



We find capability gaps when the Board Global Capability Scores for companies in an industry lag behind the industry's Global Footprint, or percentage of international revenue. In essence, the need for global talent exceeds what exists on boards.

Today, all industries are experiencing a Board Global Capability Gap. For the purposes of this analysis, we will focus on the areas where the gap is the most significant.

- Information Technology reports the highest percentage of global revenue (55%), and has among the lowest levels of Board Global Capability (11%).
- Healthcare, Consumer Discretionary, and Financials report moderate degrees of global penetration (40%, 38%, and 32%), but below-average levels of Board Global Capability.

implications of the Board Global Capability Gap at the enterprise level

To bring the concept of the Board Global Capability Gap to the company level, it is useful to ask three questions:

- Am I addressing the gap at the company or industry level?
- How big is the Board Global Capability Gap as it relates to my interests?
- What lens am I looking through—functional, strategic, financial, etc.?

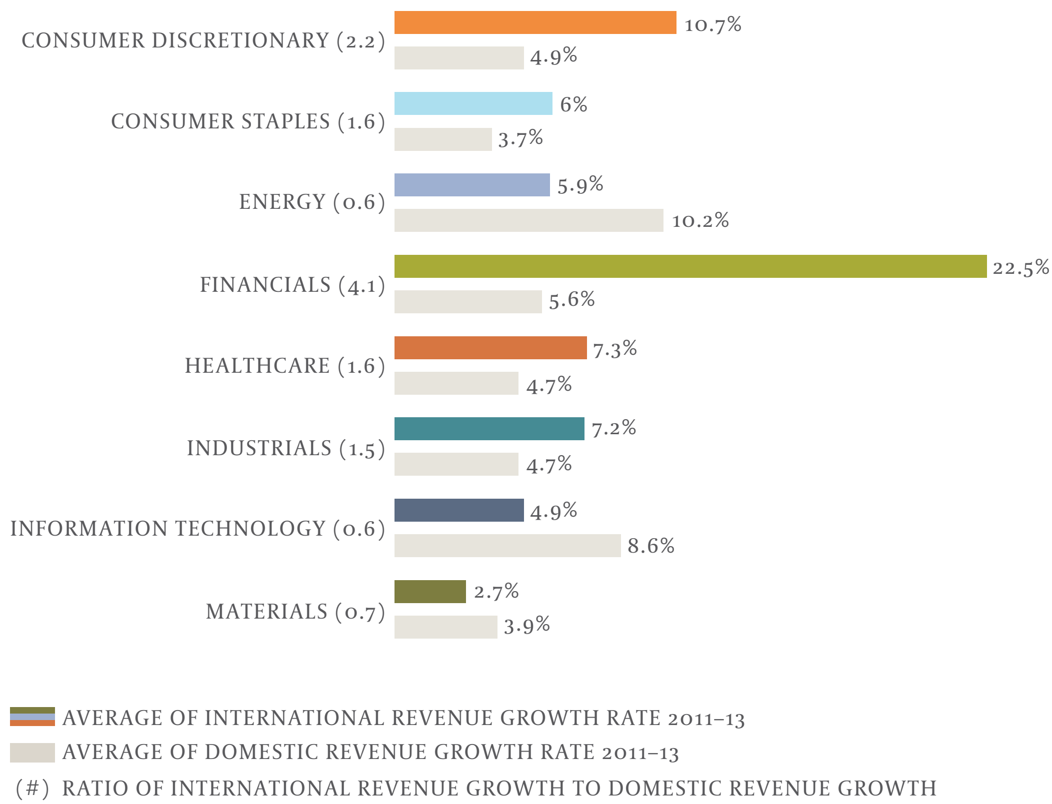
At the industry level, a gap between Global Footprint and Board Global Capability signals real opportunity for the companies within that industry. Here, the mantra should be full speed ahead. Companies willing to engage in board development work and create global capability at the board level—or enhance what they've already got—have greater opportunity to create competitive advantage and generate real gains.

companies with the talent to identify and seize global opportunities are more likely to experience more rapid economic growth overseas

To those companies operating in industries whose gap is comparatively small—or seemingly nonexistent—the watchword should be proceed with caution. Potential gains may be outweighed by potential risks, a concept we explore in the next section of this report.

Leaders need to continuously assess the degree to which their board composition addresses the company's ongoing operational needs and strategic vision, especially vis-à-vis international growth and global competitiveness.

FIGURE 9: REVENUE GROWTH COMPARISON FOR S&P 500 COMPANIES REPORTING INTERNATIONAL REVENUE



It comes as no surprise that companies are increasingly focused on international expansion. Our quantitative analysis highlights the benefits of doing business internationally. We can quantify the boost that companies get by operating globally by looking at the ratio of international revenue growth to domestic revenue growth.

Across the S&P 500, we see a ratio of 1.5, which means that international revenue grows at 1.5 times the rate of domestic revenue. Among companies in the Financial sector, revenue growth rates are more than 4 times domestic revenue growth rates. For the Consumer Discretionary sector, the ratio is 2.2:1.

International operations are not without risks. For industries that report revenue decline, international revenue declines considerably faster than domestic revenue—most notably in IT where international revenue declines at nearly 10 times the rate of domestic revenue.

However, even with this increased rate of decline, the companies that operate internationally experience slightly lower rates of contraction for revenue overall. This analysis confirms that with the right leadership team in place, there is increased revenue upside without additional downside to operating overseas.

in summary

GBI 2014 verifies that U.S. businesses continue to be exposed to the Board Global Capability Gap at both the company and industry levels. What companies need—defined by their strategic direction and level of global penetration—does not match the mix of global talent comprising current board composition.

The implications of the Board Global Capability Gap are as numerous as there are companies. To determine the significance of the gap, the urgency with which it is to be addressed, and the opportunities it produces, leaders need to assess their current and future board requirements—as well as the operational and strategic direction of the company—in the context of an evolving and increasingly global business environment.

CONCLUSION

the growing importance of "globality"

Perhaps the most important finding from the 2014 Global Board Index is the critical importance of "globality"—the degree to which a company has a global mindset, and leaders with global capability and expertise.

In our work advising the boards of multi-national organizations around the world, we see first-hand the direct correlation between global opportunity and global talent. In an increasingly globalized world, companies will come to rely more heavily on emerging markets and overseas opportunities to deliver sustainable, long-term growth.

The companies that succeed will be those who act quickly to embed global capability into the boardroom and throughout the organization. This requires a strategy for board succession that reshapes and enhances the Board's global expertise and diversity of perspective—bringing in agile, multi-cultural leaders with frontline operational experience in global markets, who understand the organization's immediate and long-term strategic needs and are attuned to the changing order of the day.

We hope the findings in the 2014 Global Board Index help inform your thinking about board leadership and governance in this highly competitive, global marketplace. We welcome the opportunity to discuss these issues further and to help you strengthen your organization's global impact.

Regards,

Rajeev

Rajeev Vasudeva
Chief Executive Officer
Egon Zehnder

APPENDIX A: RESEARCH NOTES

data sources

Egon Zehnder's portrait of global capability in the boardroom comes from an extensive analysis of information contained in a proprietary database on directors, boards and companies of the S&P 500 companies. The GBI 2014 research sample includes data from 5,241 directors and 488 boards. Companies that did not meet research criteria were excluded from this list of large publicly traded companies.

Company websites and annual reports provided reliable sources of information on board composition and financial performance. SEC filings, including 10-Ks and 14-Defs, offered additional data. Specific financial metrics were provided by the data service, CapIQ. The geographic basis of international revenue was determined using corporate proxy statements. Biographical information on directors was culled from numerous websites, reports, news articles and other sources.

The Egon Zehnder GBI 2014 research team makes every effort to create the most accurate and complete overview of the global capabilities of S&P 500 board members available, given limited public information on board members' nationalities and international backgrounds. To the extent that the information is available, the database represents the most accurate and timely portrait possible.

measures

Industry Global Footprint is an average of each company in an industry's share of international revenue to total revenue.

Global Board Capability Score represents a board's global expertise, and is determined using a tally for members who are either foreign nationals, or have meaningful international work experience or both. Each Industry Global Board Capability Score is an average of the scores for all companies in that industry.

The Global Board Capability Gap is the difference between the Global Footprint and Global Board Capability Score.

Revenue Growth Rate Ratios are calculated using the 3-year average for international revenue growth rates among all companies in the industry in comparison to the 3-year average for domestic revenue growth rates of the same companies. In brief, it is the ratio of two revenue growth rates—international to domestic.

APPENDIX B: DATA TABLES

TABLE 1: ALL COMPANIES

	(n =)	Global Board Capability Gap	Share of International Revenue	Global Board Capability Score	Share of Directors who are Foreign Nationals	Share of Directors with Meaningful International Work Experience	Average Board Size
CONSUMER DISCRETIONARY	81	17%	27%	10%	8%	13%	10.5
CONSUMER STAPLES	39	16%	32%	16%	11%	21%	11.5
ENERGY	43	19%	31%	12%	7%	16%	9.9
FINANCIALS	75	7%	15%	8%	5%	11%	11.5
HEALTHCARE	54	21%	31%	10%	7%	14%	10.3
INDUSTRIALS	60	25%	35%	10%	6%	15%	10.7
INFORMATION TECHNOLOGY	71	40%	50%	10%	8%	13%	10.0
MATERIALS	30	27%	43%	16%	11%	21%	11.0
TELECOMMUNICATIONS	7	-7%	1%	8%	4%	12%	11.3
UTILITIES	28	-1%	4%	5%	3%	6%	12.0

TABLE 2: ONLY COMPANIES REPORTING INTERNATIONAL REVENUE

	(n =)	Global Board Capability Gap	Share of International Revenue	Global Board Capability Score	Share of Directors who are Foreign Nationals	Share of Directors with Meaningful International Work Experience	Average Board Size
CONSUMER DISCRETIONARY	58	24%	38%	13%	10%	16%	10.6
CONSUMER STAPLES	35	20%	36%	16%	11%	22%	11.5
ENERGY	32	29%	42%	13%	9%	17%	10.2
FINANCIALS	35	21%	32%	11%	8%	15%	11.7
HEALTHCARE	42	29%	40%	11%	8%	14%	10.4
INDUSTRIALS	55	28%	39%	11%	6%	16%	10.7
INFORMATION TECHNOLOGY	65	44%	55%	11%	9%	14%	10.0
MATERIALS	29	28%	44%	16%	11%	21%	11.0
TELECOMMUNICATIONS	1	6%	6%	0%	0%	0%	10.0
UTILITIES	3	18%	35%	17%	15%	20%	13.0

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