

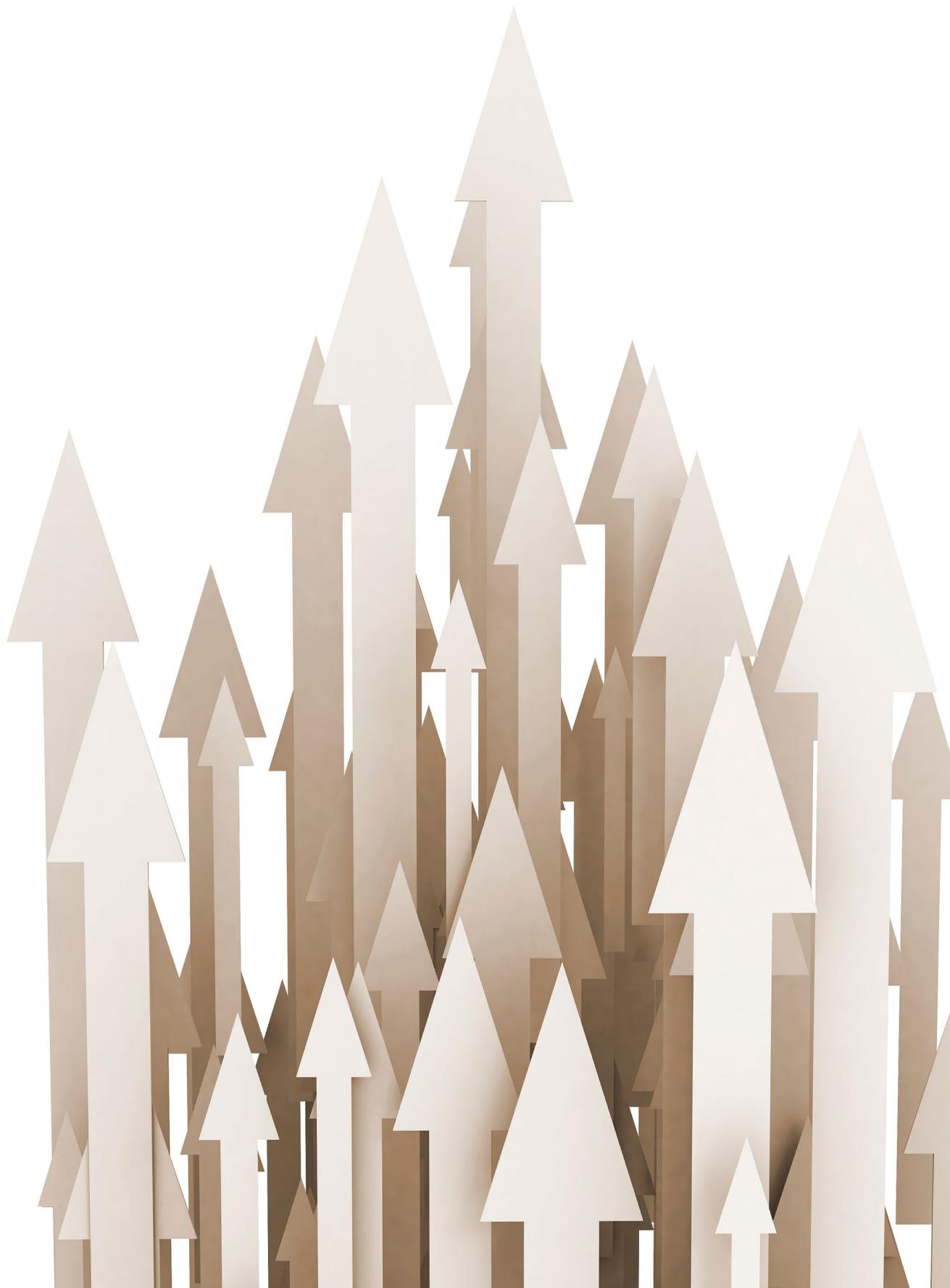


# The Khosla Rules

To accelerate growth, champion the consumer,  
think very big and trust frontline leaders emphatically

By **Gregory S. Carpenter** and **Thomas C. Hayes**

KELLOGG INITIATIVES Markets and Customers



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**S**ales for Kraft Foods' businesses in developing markets had been below expectation for eight years and were approximately \$5 billion when Sanjay Khosla signed on as the group's president early in 2007. The business had been established for more than two decades in the coveted faster-growing economies of China, India, Brazil and others that collectively were adding millions of middle-class consumers, but results faltered over time from disappointing to frustrating.

Khosla identified during his first weeks at Kraft issues in China that over time would strike him as emblematic of the global group's recent

struggles. The existing approach wasn't working. The businesses had too many agendas eating up capital and pulling resources away from core strengths, even masking some of those core strengths.

Senior executives in Kraft's headquarters in suburban Chicago were ready to pull Oreo out of China after 10 years of effort and stalled progress. But Khosla sensed opportunity and called a time-out. He had helped shape and implement growth plans for dozens of business units over the past several decades, initially in his native India and then spanning three continents.

## A Savvy Leader in an Epoch of Transformation

By any standard, Khosla was a savvy participant-observer during this epoch of unprecedented transformation in global markets. Political reforms and digital technology had tilted the balance of economic power toward the developing world and from institutions such as governments to individuals. Market economies and empowered consumers were on the march. Khosla recognized clearly how consumers everywhere were using personal computers, smartphones and other devices to access, compare and respond to information on products and services they cared about.

Yet the Kraft business model that had worked for decades now left executives 12,000 miles removed at headquarters unable to fathom, much less exploit, critical details of how the new forces were playing out among Chinese consumers. If Khosla shifted nearly all responsibility for decisions about Oreo's flavors, shape and sweetness, as well as budgets and marketing campaign strategies and tactics, to Kraft managers in China, he reasoned, wouldn't that make one last try worth a shot?

The answer was "yes" and it came remarkably fast. With local teams calling the plays in consumer tests of 19 variations, the shape, taste and pricing of Oreo were completely made over (more elongated and more layers, less sweet). An Oreo apprentice program at 30 Chinese universities inspired an energizing campaign to promote Oreo, with 300 student "ambassadors" on bicycles handing out small packages to more than 300,000 consumers around Beijing. Brand managers on the scene rolled the dice in other ways, betting big to

sign up Yao Ming, a national hero and then still an NBA basketball star, as a celebrity endorser. The teams continued to leverage Oreo global technology, expertise and know-how.

In his classic book, *The Practice of Management*, Peter Drucker framed more formally what for Khosla was an intuitive understanding that the strategy for any business should have the simple common-sense goal of understanding and championing customers. Drucker's view, published in the 1950s when Khosla was born, was that the practice of management is exercised best when the basic functions of marketing are writ large across the organization. Marketing, Drucker wrote, "is the whole business seen from the point of view of its final result, that is, from the customer's point of view. Concern and responsibility must therefore permeate all areas of the enterprise."

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To execute these concepts, decisions should be made as close to the customers as possible, by people who best understand those customers and local markets. "Command and control died many years back," Khosla says. "Two of the great myths in management are that the boss always knows best and that senior people in headquarters have greater knowledge. Nonsense." What really matters for senior executives at headquarters is getting the right people, principles and metrics in place, and then holding local teams accountable for delivering against aggressive goals.

## ACHIEVEMENT AND A LEGACY *for Leading*

### Marketing as Soul of the Business, with Consumer at the Center

Khosla accumulated these convictions from his broad experience. During the preceding 30 years, he had been a senior leader for major consumer-brand businesses, primarily at Unilever and for a few years as well at Fonterra Brands, a New Zealand-based farmers' dairy cooperative. His strategy of focusing on a few categories, brands and markets had paid off handsomely, expanding revenues, earnings and gross margins by significant leaps.

The Khosla years at Kraft's developing markets operations would repeat those themes, breathing life into a tightly focused strategic framework that quickly became known as "5-10-10": 5 categories-10 brands-10 markets. This 5-10-10 template was ironclad. It had been created and agreed in a series of workshops by all the global market executives. Khosla was the enforcer of this template and would not accept the occasional breach when a willful business leader in certain countries strayed.

Khosla came to Kraft with a mandate to accelerate Chairman and CEO Irene Rosenfeld's strategy to put more focus on the consumer across all Kraft brands in the U.S. and, globally, icons such as Tang, Trident, Nabisco along with Oreo. In effect, he would be pushing even his marketing people to be more consumer-focused along with all other functional leaders, as well as operations leaders, in his developing markets organization. The consumer has to be "at the center of everything you do, with marketing expertise applied in each part of the business. The consumer is king," Khosla says. This is not limited to consumer products

When Khosla retired in March 2013, sales of the Kraft Developing Markets business he had led since January 2007 had more than tripled to \$16 billion in 2012. Organic sales had doubled and profitability improved significantly.

These operations straddled more than 60 countries, with more than 65,000 employees, in Central and Eastern Europe, Middle East and Africa, Asia Pacific and Latin America. They became part of Mondelez International, now with 110,000 employees worldwide and \$35 billion in annual revenues, in the fall of 2012 when Kraft Foods Inc. changed its name to Mondelez International and spun off its grocery business in the United States and Canada, with 23,000 employees and \$19 billion in annual revenues, as the Kraft Foods Group Inc.

or services, he adds. "It could be anything. Marketing as a business approach is how all of this comes together. Marketing becomes the soul of the business. Business leaders now are playing the role of chief marketing officer in their respective business areas. Everyone – in all functions as well as operations – is judged only by the results of the business. The work and the targets are shared. And so are the rewards."

### Growth through Focus, Backed by Blank Checks

In his view, the centralized, function-based organization had proven too slow, too expensive and, in many cases, simply too unfocused and ineffective to succeed in the global marketplace of the 21st century. In addition to being an unwavering champion for the focus on consumers, saying "the core of your initiative is

always the customer," Khosla establishes two other imperatives for his teams in programs to revitalize brands and grow revenues quickly. One imperative is a regimen he calls "Growth through Focus," a process that involves rapidly pruning lagging offerings and channeling freed-up resources and talented leaders into urgent short-fuse campaigns to build on core strengths. Are there certain areas of your business that can grow more than others? Do you have gross margins that are intrinsically healthy, or, can be made healthy?

"You want to create a virtuous cycle of growth," Khosla explains. "You need to invest in brands, distribution and people to complete it. We had been trying to do too many things in China. Too many brands. Too many initiatives – sales, IT and other things. The list went on and on. You have to focus on where you can win

quickly, and on just a few things. We decided Oreo was the brand with the best position to grow. And we put resources behind it.”

Another innovation is his “Blank Check” funding principle, a seemingly improbable method of resource allocation that works almost exactly as the name suggests. Khosla agrees to provide whatever financial resources his local executives determine they need to deliver on plans to meet or exceed aggressive sales growth targets. His purpose is to force local leaders through a crucible of creative tension, a boot-camp process packed by design with such intensity and high stakes that the leaders must identify simple ways to quickly execute staggeringly ambitious growth plans.

The solutions most often are opportunities that simply had been overlooked or unappreciated by the local leaders themselves as well as distant command-and-control leaders who lacked the local teams’ knowledge of markets and consumers. Pushing the planning responsibility to leaders at the front lines, and then giving them whatever authority and resources they say they need to execute, invariably unlocks these opportunities, Khosla says. “You find individuals you trust,” he explains, “you look into their eyes and you say, ‘go for it.’” All the while, Khosla knows his reputation and accountability to meet financial goals are on the line, vulnerable to misjudgments and misplaced trust and confidence.

## **Workshops Establish the Framework**

Setting aggressive specific targets and removing budget constraints are cornerstones of what Khosla characterizes as his “family-dinner approach” to leading global business. “This is the concept of family, of interdependence. It’s not very complicated. You always are going to have mistakes. It’s inevitable. Nothing is perfect. In my experience, mistakes usually happened because I didn’t shut things down fast enough when they were not working. I didn’t want to disappoint the team, to recognize failure and give up.” For each member of the team, he says, the compact implicitly boils down to this: I have

to trust you and I have to be part of the family.

He drills his teams in a growth-through-focus framework in a series of workshops that examine what he regards as seven fundamental elements for effective business planning and implementation: discovery, strategy, vision, people, execution, organization and metrics. Khosla calls this his Focus 7 series.

“These are mechanisms to get alignment and consensus,” he says. “This is all data-driven. My job is to create the process to produce the right facts, select the right people and empower them the right way to produce the right results. It is very important for people in my organization to have a mechanism to say their piece, with a formal, disciplined structure in place to make choices.”

The sea change that is underway in the generation, access and analysis of consumer data in the digital age, means global markets now operate at remarkable speed. For example, it took Apple more than 20 years to sell 50 million Mac computers. With the iPad, the company crossed that threshold in just two years. New product introductions are coordinated on the scale and with the marketing skill of Hollywood blockbusters, ushering in an era when the announcement of a hot new device (or a follow-on paucity of inventory) can prompt news headlines around the world.

Khosla believes his business units must look at consumer research for insights on competitive advantage, but the big question is: How will they act on those insights? Once product teams review the data, they debate and start taking decisions. “We can disagree violently — if we agree with each other all the time then something is wrong. If we agree, we don’t need everybody who is there. An objective set-up of the facts is important for the situational assessment by different people around key stakeholders. But it is a very short process.” After they decide — Khosla says being right at least 70 percent of the time is more than good enough — teams are expected to lock arms and march ahead. “Once we go out, there is no dissension. Of course there is flexibility to make adjustments. But the

framework stays the same. We have to act as one. We have to trust each other. It's how families operate."

### **Front-line Local Leaders Make the Consumer Connection**

Khosla sees his role in these sessions as the facilitator and process coach, not the boss. "The boss is the local leader, not me," he says. "It is critical that I not be in that role and not hint even in the slightest way through body language, asides or jokes that I really think I am. My main role is inspiring and building talent. When people ask me about a particular product or project, most often I actually wouldn't know how to answer."

removed from developing markets. Their takeaway is that the devolution of decision-making power to leaders on the front lines in local markets, far removed from corporate headquarters, is mandatory to court, win and retain loyal consumers in 21st century global markets.

The challenge is to strike a proper balance, as Khosla puts it, "between hopelessly local and mindlessly global." Global companies most often have strong competitive advantages in several core processes that never should be abandoned. It is a game of execution and "the people who get the balance right win," Khosla says. "Then, once you get the consumer connection right, you can create a brand with soul... something with an eternal essence."

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Khosla's passion for "blank-check" funding is rooted in his conviction that removing resource constraints is essential to unlocking self-imposed inhibitions and long-standing corporate practices built around disciplined resource allocations procedures. The point, as Khosla and his co-author, Mohanbir Sawhney, a professor at Northwestern's Kellogg School of Management, described in an [article](#) in 2012 for *strategy+business* magazine, is to inspire teams to achieve unprecedented results and create a virtuous cycle of growth. They argue that local teams who take responsibility for forecasting and using financial resources wisely have better track records than senior executives in corporate headquarters far

When he was a young marketing manager for Unilever detergents in India, Khosla recommended creation of an innovative business model and a new brand at one-third the price of the high-end Unilever detergent to compete in the fast-growing low end of the market. To do that, he gladly applied the best of Unilever's global expertise — in R&D, procurement and process technology. But he couldn't afford Unilever's standard

solution for detergent manufacturing: building a large, capital-intensive plant. Instead, his team settled on an inexpensive yet mobile solution, adapting cement-mixers to make the detergent. For packaging, they devised small plastic pouches. For advertising, they mounted Bollywood style scenes for TV campaigns featuring Indian singers and dancers. The business model and marketing campaign were roundly rejected initially by his bosses in London as too controversial, "too raw," but Khosla persevered. "We delighted consumers with something that was locally unique," he says, "and we got the balance right between global and local." In three years, Hindustan-Unilever sold more than 100,000 tons of the



## HARNESSING CUSTOMER INSIGHTS: *The Cadbury Visi-Cooler*

After Kraft's \$19 billion acquisition of Cadbury early in 2010, a similar story of stoking rapid growth soon unfolded in India. Sales of the Cadbury business in India had reached around \$400 million after 50 years. Yet Cadbury, which operates in 50 countries, believed it knew the Indian consumer and local distribution practices extremely well after more than a half century of peddling chocolates across the subcontinent.

When its business leaders met with Khosla for the first time in February 2010, a month after the acquisition was completed, they expected he would be excited to hear they were committing to a sales-growth target for the year of 15 percent, a total of \$460 million. Other consumer-goods companies are happy with 12 percent; they pledged 15 percent. But Khosla was not excited. Instead, smiling a few days later from the stage where he stood before a crowded employee town hall meeting, Khosla held up his right hand: an open palm and all five fingers pointing skyward. What do you see? he asked. Five fingers. Five fingers for what? No one could say, so he answered: It was their new sales goal... \$500 million. "I'll be here in December, and you'll do \$500 million," he said, confidently.

After their initial panic subsided by March, the Cadbury leaders realized that they must focus quickly on three or four things. Once again, as he did in Brazil and many other markets, Khosla promised a blank check: He would provide whatever resources they needed to execute and deliver sales of \$500 million. The breakthrough idea this time was dramatically expanding the distribution of small coolers bearing the Cadbury brand that were a fixture already in thousands of small sweets shops in India. Data showed that sales were higher wherever these Visi-Coolers were used. Why

not go for more? Well, yes, it's in our plan, another 10,000. Khosla's response: Yes, but if they can drive more sales, why not 50,000 Visi-Coolers?

Indeed. Cadbury's revised orders for Visi-Coolers soared to 50,000 units, clogging the full capacity of Visi-Cooler manufacturers by mid-year. Every available Visi-Cooler in India was put into action displaying Cadbury chocolates as quickly as they rolled off the assembly floors. At the same time, Cadbury put a halt to nearly a dozen initiatives underway to introduce and build different brands – a gamble requiring at least three years for a profitable payoff. Instead they aggressively pursued their core chocolates, escalating promotions and sales incentives around the Cadbury brand.

Results: the Cadbury India team exceeded Khosla's "high-five" challenge by a staggering margin. Sales soared to \$520 million. To be sure, expenses soared as well, denting profits to deliver and position the waves of new Visi-Coolers in sweets shops and mount the marketing campaigns. Gross margins, however, did not waver. Sales grew again by more than 25 percent in 2011.

"The focus for Cadbury India was on three things: Visi-Cooler, Cadbury brand and investing in distribution," Khosla says. "In January 2011, the team returned part of the blank-check money. They hadn't needed it all! Their virtuous circle was now working. But I said, 'No, take it and do more.' I was backing the business."

Indeed, with the blank check approach, experience has shown that the teams tend to get more accountable and focused. All the initiatives are not successful. It is important to course correct if things are not going well and to learn from failure and move on.



new low-cost detergent, Wheel. Today, Wheel is one of Unilever's success stories, with sales exceeding a million tons a year in India.

Khosla and Sawhney's blank-check concept is anathema to many executives who mastered the old traditions. What about budgeting discipline? Maximizing scarce resources? What about accountability and responsibility? How can headquarters loosen the reins on these processes?

Khosla says blank-check funding schemes were essential for driving clear, highly focused campaigns calibrated specifically for consumer preferences in local markets. These programs enabled leadership teams at Unilever, Fonterra

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## **Make the core exciting and activate it for consumers. Reframing is the most important thing to do.**

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and Kraft repeatedly to deliver on ambitious growth plans in priority regions and markets around the world. To create a virtuous cycle of growth, Khosla says, business leaders should identify markets with above-average growth potential, focus on products or services with gross margin potential that is intrinsically healthy, and then invest in brands, distribution and talent to execute the plans.

"Unfortunately, resource constraints limit more than plans," Khosla and Sawhney wrote. "They also limit the creative potential of people." The commitment to unlimited funding, "is a tremendous motivator to people who have never experienced it," Khosla says. Blank checks came to be seen as an important part of the tool kit that enabled Khosla to meet or exceed his sales and profit targets at Kraft for more

than 20 consecutive quarters. More important, it energized the culture. Teams throughout his global organization were eager to share their successes with blank-check projects, projects that often were followed with rapid promotions to bigger jobs.

"People get excited about this," Khosla says. "They want to work in this kind of environment."

Local team leaders typically react to his stunningly aggressive sales-goal pronouncements by ratcheting up their fear of failure and other anxieties. How can we possibly do this? Khosla expects this. "Everyone thinks you're nuts," Khosla says. "You just keep repeating the targets and the timeline at every lunch and dinner, and then they come to realize you are serious. I've done this many times. I basically say, 'Focus on where you can win quickly and on just a few things. We must move faster than the competition and make money. The big thing for focus is just stopping things that aren't working well. The question always should be: how do we win now with the customer and intersect with markets?'"

Incremental steps can never generate quantum jumps in sales in the short run, Khosla says. In fact, he believes the enthusiasm for innovation for its own sake has deteriorated in many companies into a wasteful management fad over the years. "People tend to get bored with what they have," he says. "It is a big mistake to become 'innovation junkies' where activity is confused with output. What the teams should include instead is reframe what is already working. Make the core exciting and activate it for consumers. Reframing is the most important thing to do."

Reframing was the path a Khosla team in Brazil took out of near-desperation to meet a sales target of 25 percent growth during his first year at Kraft. The team threw intense marketing support behind Tang's basic, old-fashioned yet best-selling flavor — orange. They had little choice but to go for the core and amplify what was working here and now. One breakthrough idea was creating a pre-teens' recycling contest

with Tang's existing packaging, first in São Paulo and then across Brazil. Enjoy more Tang. Help the environment. It touched off a national recycling campaign led by Brazil's youth.

Results? The team exceeded Khosla's first-year goal and then played a big part elevating Tang's global sales by \$1 billion from \$500 million in five years.

### **Energizing The Family**

Within a few weeks after Lehman Brothers collapsed in late summer of 2008, the global economy was entering what seemed like a free fall. Khosla's 10-member executive team had just finished two days of rigorous meetings, building plans and budgets for the 2009 calendar year and getting a strong endorsement from Irene Rosenfeld and other senior corporate executives at Kraft's headquarters in suburban Northfield.

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## **...we gave them freedom to do what they want locally, within a framework for the brand and the business that works globally.**

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The team dinner scheduled at a restaurant in downtown Chicago that night had all the makings of a celebration. Sales and profits were trending well, 2008 looked like it would go into the books soon as another winner and their fresh-laid, CEO-affirmed plans for 2009 had been optimistic as well.

But, during the dinner, speculation about the plunging global economy dominated the discussion. China and India were slowing down. Europe... Germany? Not good. These budgets for 2009 could work only if life is good. What

happens if even the slightest thing goes awry?

Khosla offered no answers. Instead, he facilitated the process even though this night was taking a rapid turn from the usual. An initial focus on the positive – what's working, sharing best practices – was cut short by the team's concerns and challenges for the businesses across the unraveling global economy, particularly in China. In his native Hindi, after listening for hours, Khosla interjected what for this group was a now-familiar question: KKH (Karna Kya Hai); So, what do we do?

It also was a totemic question. Khosla was demonstrating his "family dinner" approach to leadership. Under these Khosla Rules, the boss does not know the answers. The boss identifies, assigns and develops leaders, sets aggressive performance metrics and commits the resources for the teams to achieve or exceed those metrics. The boss devolves decision-making closest to the front lines with the consumer and helps local teams frame problems, debate solutions, reach consensus, commit to and accomplish their plans.

Before the last bottle of wine was consumed late that night, the developing-markets team had answers to Khosla's question. They would find ways to cut these just-agreed 2009 expenses by more than 7 percent. And this could not, and would not, be an across-the-board retreat. The team would

keep fidelity with their 5-10-10 framework for building the long-term business.

Among other imperatives, this required *adding* resources and people in China, not cutting. As it turned out, staffing in China for 2009 increased by more than 30 percent, even as the total percentage cut in the group's global expenses widened by the end of 2009 to double digits. On the back of their quick action that night in Chicago, the group again exceeded their sales, profits and margin goals for the 2009 calendar year.

“Let’s be clear, it doesn’t always work,” Khosla says. “We were lucky. But the point here is that the family came together. Project teams quickly formed after the meeting to sort out what had to be done. All regions contributed to the cuts without compromising the virtuous cycle or our long-term strategies, such as in China. We blew out our numbers and the family was energized.”

The Kraft China business, in fact, was gathering momentum then towards what Khosla considers the essentials for any truly successful business: healthy gross margins, a lean organization and increasing investment in innovation and advertising. It is what he means by “the virtuous cycle.” Within five years, China’s revenues would soar to about \$1 billion from less than \$200 million. Oreo

was a big contributor. Less than two years after Khosla’s first meetings with his brand managers in Beijing, Oreo found its footing in the Middle Kingdom. Revenues doubled by the end of 2008. Growth has continued since at an impressive pace, helping to build Oreo’s total international revenues to around \$1 billion in 2012, from approximately \$200 million in 2007.

More important, Khosla says, is “the capability, feeling and spirit of winning in China today. It is just unbelievable. It’s partly because the numbers are great. At the end of it, numbers do talk. And it’s also partly because we gave them freedom to do what they want locally, within a framework for the brand and the business that works globally.”

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**Gregory S. Carpenter** is the James Farley/Booz Allen Hamilton Professor of Marketing Strategy at the Kellogg School of Management and Faculty Director of the Kellogg Markets and Customer Initiative. He also serves as Academic Director of the Kellogg CMO program. **Thomas C. Hayes** is a Senior Vice President at RLM Finsbury, a global advisory firm in strategic communications and a member company of WPP.

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### ***First in a Series***

This article is the first in a new series being developed by the Kellogg School of Management Markets and Customer Initiative to examine the rise of the Customer-Focused Enterprise in the digital age. The series is designed to illustrate through real-world narratives how business executives are infusing the consumer perspective into their approach to leadership, strategy development and tactics to gain competitive advantage. This article details the leadership of Sanjay Khosla, Senior Fellow at Kellogg School of Management and former senior executive at Kraft Foods and Unilever.



Kellogg School of Management  
Northwestern University  
2001 Sheridan Road  
Evanston, IL 60208

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