



Refining Shell's position in Europe

Ivo J. Bozon and Peter N. Child

Two senior executives of Europe's largest fuel marketer explain how it experienced a huge reorganization.

In the mid-1990s, the Royal Dutch/Shell Group had to face the fact that its giant European downstream operations—refining and fuel marketing—were making unacceptable returns. The corporation's leaders decided on a large-scale reorganization to reshape Shell Europe's 28 national operating companies by creating a pan-European structure. The goal: raising business returns significantly by gaining scale and critical mass at the European level while retaining strong local customer relations.

This was a tall order. The national operating companies, which had their own support operations, were replaced by three separate businesses—retailing, commercial (business to business) and manufacturing, and supply and distribution—each managed at the pan-European level. In the process, more than 3,000 jobs vanished.

The difficult decisions and the changes made during the past four years are now paying off. Shell Europe has turned itself around, with returns rising to

more than 15 percent in 2001 on \$6.5 billion of capital employed. Costs have been cut by more than \$500 million and capital employed by \$2 billion. Shell is Europe's largest fuel marketer and biggest fuel retailer, with 14,000 sites. The company's executives hold up the success of Shell Europe Oil Products as a model for other regions.

In many respects, retailing has led the way, and the company's fuel-and-shop offer—together with a refocused, less capital-intensive business model—has delivered significant growth in revenues, margins, and profits. Adrian Loader, the president of Shell Europe Oil Products, and Pat O'Driscoll, its vice president of retailing, discussed the transformation of the retailing business with Ivo Bozon, a director in McKinsey's Amsterdam office, and Peter Child, a director in the Paris office.

Adrian Loader



Vital statistics

- Born June 3, 1948, in Thessaloniki, Greece
- Married with 3 children

Education

- Graduated in 1969 with degree in history from University of Cambridge

Career highlights

- Royal Dutch/Shell (1970–present)
 - Member of Chief Executive Staff Group, Shell Malaysia (1975–76)
 - General manager of Shell Honduras (1979–82)
 - General manager of Shell Uruguay (1982–84)
 - Administration manager of Shell Exploration and Production (1984–87)
 - Head of central recruitment (1987–89)
 - Chief executive of Shell Philippines (1989–93)
 - Director of South Zone (Africa, Latin America) for Shell Oil Products (1996–97)
 - Director of East Zone (Far East, Middle East) for Shell Oil Products (1997–99)
 - President of Shell Europe Oil Products (1999–present)

Fast facts

- Member of board of directors for European Petroleum Industry Association (EUROPIA)
- Fellow of Chartered Institute of Personnel and Development

The Quarterly: Please describe the condition of Shell Europe's downstream operations, including retailing, in the mid-1990s.

Adrian Loader: This was a business that had been underperforming for a while. The unsatisfactory situation had not been terribly transparent, because under the previous organizational structure the results of what now is the Oil Products group were hidden in the national-operating-company accounts. As we looked more closely, it became evident that the downstream operations were far from meeting Shell's objec-

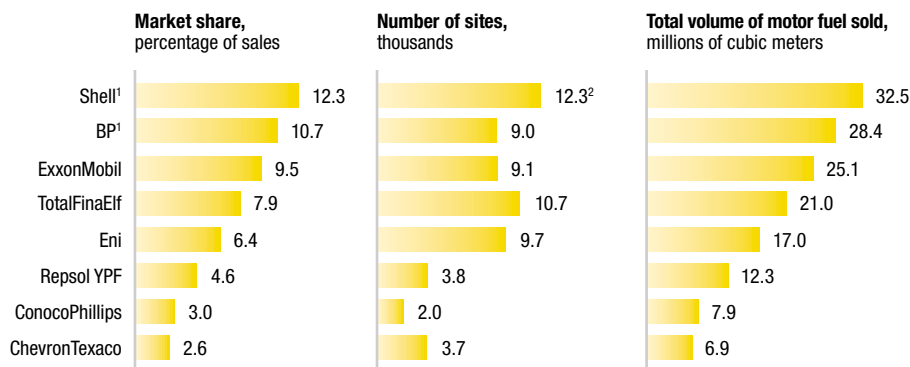
tive of a 15 percent return on average capital employed for a mature business and that a radical reorganization was called for. What was less obvious, initially, was that we were failing to satisfy customers—something we have spent a lot of time rectifying.

Pat O'Driscoll: As for the retail business, we first had to figure out exactly what it was. We had no clear understanding of the retail-customer experi-

EXHIBIT 1

Fueling Europe

Comparison of top European motor-fuel retailers, 2001

¹Figures for BP and Shell include estimates for Veba and RWE-DEA acquisitions, respectively.²14,000 sites as of 2003.

Source: PFC Energy Downstream Monitoring Service, European country profiles, 2002; McKinsey analysis

ence or offer. Once we defined what we meant by retailing, we soon understood that the level of return was unacceptable. Whether you take Shell shareholder expectations or you benchmark us against gas-and-convenience retailers around the world, we clearly needed to make improvements fast.

There were three major factors behind this. First, we didn't understand what was important to our customers; in fact, we weren't even interacting directly with customers in many respects and therefore weren't able to start satisfying their needs. Second, we had markets that were becoming more competitive as nontraditional players came in: the hypermarkets, the independent gasoline companies, and the automat formats. Third, we had 28 highly decentralized national organizations. This was costly and complex.

We had some six million customers a day, and we were getting, at the very most, 30 to 40 percent of the potential value they offered. On the positive side, Shell had a fantastic brand, asset base, and people. Shell's brand value to customers was underexploited across a high-quality asset base—both envied by our competitors—and we had many great people who recognized the urgent need for change.

The Quarterly: What were some of the most difficult change-management issues you faced?

Adrian Loader: When we started, we had 15,000 full-time employees. We had to cut 3,000. We had to establish the case for change. We had to answer some basic questions: What are we trying to do, and what are the objectives? Who is responsible for what, and how does it work?

Getting the message through to 12,000 people is a huge challenge, and more so if someone already has a long association with Shell and strong national roots. I was born in Greece, for example. If I were working there, I would have had a strong attachment to Shell Hellas. I would say, “I can see the Greek structure; I know who’s the boss of Shell Hellas, and I know what career path I can have in my own country. But in a transnational organization, what’s in it for me? In the past, I knew the retail-sales manager’s job

and its appeal, responsibility, and accountability. What do these new pan-European jobs have?”

Pat O’Driscoll



Vital statistics

- Born April 27, 1959, in Kwe Kwe, Zimbabwe
- Lives with her partner in Farnham, England

Education

- Graduated in 1981 with degree in sociology from University of Exeter

Career highlights

- Marks & Spencer
– Various roles in operations and food buying (1982–87)
- Tesco
– Buying controller, chilled convenience foods (1988–90)
- Pacific Connection
– Owner and manager of this Singapore-based food consultancy (1991–93)
- Safeway
– Buying director for drinks/tobacco and nonfoods divisions (1994–97)
- Royal Dutch/Shell (1997–present)
– President of Shell Retail International (1997–98)
– Vice president of retail marketing, Shell Europe Oil Products (1998–99)
– Vice president of retail sales, Shell Europe Oil Products (2000–02)
– Vice president of retailing, Shell Europe Oil Products (2003–present)

Fast facts

- Member of board of directors for Assa Abloy and Shell UK Pension Fund Trust
- Fellow of Royal Society of Arts

There are always some people who are not convinced of the case for change, and some of those may be in senior positions. The issue is whether they leave the organization or whether they are won over. Occasionally, there are people who just don’t fit in, even with training and development. Looking back over the past few years, in those situations I think we’ve learned it’s better to part sooner rather than later.

The Quarterly: How did you go about convincing people at Shell of the need for fundamental change in the organization?

Adrian Loader: When you want to get someone to act in a different way, you have got to start from the top, and that may well require quite dramatic and overt changes in behavior. For example, we sold some countries’ head offices and then moved the new business into more fit-for-purpose locations. In a certain number of cases, the new retail offices were actually in, above, or

below service stations. This move caused quite a bit of pain to the organization; it was not so long ago that if you came into Shell, you could tell someone’s level in the organization merely by the size of the office and the furnishings! That’s no longer the case.

There have been lots of changes at the top. Previously, there was a chief executive or a general manager of a country, and these were great jobs but outdated. I myself enjoyed one in the Philippines. The bottom-line accountability was with the general managers or the chief executives. The bottom-line accountability now is with Pat for European retailing.

Pat O'Driscoll: In the first two years, we also worked with all levels of staff to understand the customer better. That meant getting senior leadership out to retail sites and talking to customers and the staff who were serving customers day in and day out. We called these “bus rides.” The idea was to encourage people to think back from the customer’s perspective rather than from the head office—outside-in thinking to help reshape the business to be more responsive to customer needs. The bus rides were difficult for a lot of people who, in their work history, had hardly ever had to talk to a customer and find out what was good and not so good about Shell from the customer’s standpoint.

Adrian Loader: Another thing that goes with a change of behavior is giving people the tools to do their jobs properly. It’s embarrassing to admit this, but we didn’t have retail-site profit-and-loss statements. Today, however, if I’m at a site, I know how each category—such as toys or fast food—is doing. It’s enormously powerful and has meant that we have been able to adapt our offer and capture growth opportunities faster across Europe.

The Quarterly: What were your priorities at the national level?

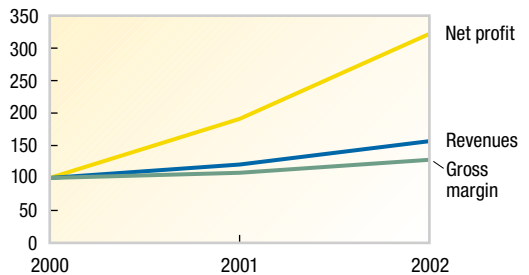
Pat O'Driscoll: To leverage the value of a European-wide retail business, we had to stop the duplication of strategic and development work across 28 countries. This meant focusing the national retail staff on running the retail operations to meet the customer’s expectations and operational standards of excellence. By doing so we saved huge amounts on development costs and started to apply consistent customer offers and formats across the European network.

In the first few years, we reduced capital spending dramatically. We cut spending to just 50 percent of our depreciation rate because we had overspent in the early '90s in retail and we weren't getting the returns. We forced

EXHIBIT 2

Shell Europe's fuel-retailing growth

Index: 2000 = 100



Source: Royal Dutch/Shell

people to optimize the return on what they already had and earn the right to grow through selective capital investment.

Adrian Loader: Rather than spending more on technical hardware and equipment or, indeed, building new service stations, we have been modifying the less-expensive elements, such as signage, visuals, and the merchandising layout in the Shell Select shops. We know from our regular research what elements are important to customers. It turns out that the best-performing sites can often be the older ones, which have lower levels of investment. This kind of microformat evolution—rather than total renovation—results in both a high return on capital and increased customer satisfaction.

Pat O'Driscoll: But besides understanding what is going on at the national level, we wanted a better understanding of what needs were common to retail customers across Europe. Fundamentally, around 70 to 80 percent of what customers want, they want in common. This is not a difficult proposition. People who come into a gasoline station want to refuel in a way that's quick, easy, convenient, and safe. They want to go into the shop and buy a few things to keep them going and to care for their vehicles. In general, the service station convenience-retailing industry has been poor at delivering the basics of customer service.

The Quarterly: Could a pan-European organization jeopardize the effort to understand the needs of your customers?

Adrian Loader: At the European level, you can get too far from our people on the ground and from the customers, as an example will show. A few years ago, “food on the move”—food that is easy to eat in the car—was seen as a good opportunity. One or two interesting ideas were developed, including a so-called driver's dog. A driver's dog is a huge hot dog with a bigger bun. The product went into trial in Norway and was a great success.

At that stage, the decision was that we're not going to reinvent the concept in 28 countries as we used to do; we'll just roll it out everywhere. Unfortunately, it didn't quite work out, as Italians don't eat hot dogs, and neither do the Greeks. In fact, I reckon that only the Scandinavians, the Brits, and the Germans like the offer!

The point about this example is that you can have a great concept—in this case, food on the move. You can do things like procurement at a transnational level and get the scale and efficiencies that go with this. But ultimately, you have to do your local tailoring, and it may not even be at the country level; it may be at the regional level, because what's appropriate for fast food in the north of Spain may be different from the south of Spain.

Our organizational structure helps. When we put together a retail-sales organization covering the 28 countries, it was clear that we couldn't have 28 sales managers reporting to the retail leadership. The solution we developed was to organize the retail business in eight geographic clusters of countries. This has been very powerful in spreading best practice across countries quickly, helping us to achieve efficiency in operations and to develop our retail staff. For example, the roll-out of differentiated fuels and loyalty programs has been achieved with much greater speed and at lower cost by combining European marketing experience with cluster sales-operational capabilities.



The Quarterly: How did the skills of the people in your organization evolve?

Pat O'Driscoll: One of the key points for us was making clear that we are a European retail business. We have seen big changes at the site, national, and cluster sales-management levels because we have demanded different skills there. We have also invested in functional marketing skills to deepen our understanding of customers, to develop offers and formats consistently, and to track customer satisfaction. For example, we've put in place satisfaction measures for both customers and our people. That's critical in helping us guide the business and shape the organization. There is a direct correlation between customer and site-staff satisfaction; in other words, happy employees, happy customers. Many retailers have been doing this for years, but we had to find a way to do it transnationally, consistently, and cost-effectively.

We have looked at great customer-service organizations, and we see one thing they do in particular: recruit for attitude. Skills can be taught through training. That's the philosophy and the mind-set we've adopted. We can see through our surveys that motivation is going up, as is the belief that Shell is a great company to work for. Also, staff rotation levels are dropping. Staff turnover is a huge hidden cost. We know how much it costs to lose people, then recruit and train new ones—plus what you lose in customer service. In key markets, we know we're now saving that money and seeing the parallel improvements in customer satisfaction and market share growth.

The Quarterly: Looking back, what might you have done differently?

Adrian Loader: I would have gone further, faster. The critical thing would have been to make some of the structural decisions earlier. Instead, we spent too long just focusing on operational excellence out in the sites, engaging with staff and customers, rather than balancing these changes with the structural ones that were needed up-front.

We got a huge surge of energy and enthusiasm around our customer initiatives, tied in with the change in leadership behavior. It was, literally and figuratively, “are you getting on the bus?” Shortly after that, it became evident that our cost base was too high and that some radical restructuring would have to occur. So having gotten 15,000 people on the bus, metaphorically speaking, we said, “There’s only room for 12,000 of you” and then had to

make the cuts quickly to minimize the loss of the positive energy we had created.

‘It’s much more difficult to replicate the leadership, the shared sense of **the direction** of the business’

Pat O’Driscoll: Looking back on the large-scale changes we embarked on, I have learned about the value of

visible leadership, consistency, and the energy that’s needed to cover a wide span of geography. As for doing things differently, I think I would have moved to the cluster structure earlier, as this shift has been a key enabler in balancing a local customer focus with leveraging our European scale.

The Quarterly: How much of what you have done would you consider applicable to other organizations?

Pat O’Driscoll: The issues that we face are generic to players in the gasoline convenience sector. We know this from mapping our competitors and understanding how they perform and operate.

The transnational dimension is critical because in retailing it’s often difficult to succeed outside your home country, and for that reason our experience may offer some learning opportunities for other retailers. What Shell had was the infrastructure, the people, and the asset base to thrive in multiple markets simultaneously. But the missing elements were the actual processes, the organizational structure, and the transparent management information needed to manage effectively at the transnational level.

If we have a distinctive competence, it is being able to determine where we can leverage scale, either at the cluster or the European level, and the way we continue to tailor locally to be meaningful to customers and to our local staff and thus capture the huge value of the Shell brand.

The Quarterly: What might be difficult for others to replicate?

Adrian Loader: It comes down to people. You can replicate the retail sites, the products, and, by and large, the retail processes. You can replicate organizational structures. It’s much more difficult to replicate the leadership, the shared sense of direction of the business, the alignment of staff around

values and priorities, the motivation of the organization, and great customer relationships.

Pat O'Driscoll: Staying ahead requires understanding your business and growing your capabilities. But as much as anything else, the important thing is the passion and intensity among your people to go out there—day in, day out—and find ways to win and stay ahead. Our success has helped us attract more high-quality people to fuel the passion to carry on successfully. It's exciting.

Adrian Loader: All our competitors focus on customers. And all our competitors strive to serve the customer better in order to make more money. Our goal—and we're not there yet—is that everyone in Shell should be absolutely clear about how they fit into the line of sight back from the customer. That goes for everyone from the European management team to the refinery operator. I don't expect refinery operators to be seeing customers daily, but they must have an understanding of what the enterprise is about and how what they do fits into the overall delivery to our customers. After all, meeting customer needs profitably is the reason we are in business. **Q**

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