

**Speech by John Roth, President & CEO of Nortel Networks Inc.
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I think the field of public-private partnerships is an exciting one, and today's discussions couldn't be more timely following elections here and in the U.S. – though they're still trying to figure out the results of that one.

Now that our federal election is over, and with the year 2000 winding down, I think it's a good time to take a snapshot and see where the world is going and what it all means for Canada. I'm a great believer in taking the 50,000-foot view to understand the macro trends that will ultimately drive major change, so this afternoon I'd like to share what I'm seeing from up above, and discuss what the agenda for Canada ought to look like as we move forward given some inevitable changes I see on the horizon.

The first big change I see coming is global free trade. NAFTA, the European Union, APEC, and the World Trade Organization all represent huge trends towards the continued globalization of markets.

Globalization and the Internet

And a force called the Internet is accelerating the globalization trend. The Internet is a huge advance in telecommunications technology. Many economists talk about it as an invention that will rival the impact of plastics and gasoline. It will be another 25 years before society really learns how to take full advantage of it, but it's already opening up new global channels to market.

There was a story on TV the other day showing a fellow in Oakville running a travel agency. He sells packages of golfing vacations, and now has about 40 percent of his business coming in over the Internet – with much of that coming from outside Canada. When he first built his website, he thought he might get some extra clients from Burlington, but he ended up with customers from as far away as Australia.

A second major trend I'm seeing is a steady decline in the relative value of raw materials and natural resources. As a society, we're working very hard to be better at conserving and wasting less, so the demand for these is not like it used to be. In addition, there's much more supply than before as developing countries with a significant amount of natural resources start to tap what they have to better their economies.

At the same time, knowledge-based economies are on the rise, with the demand for high technology going up faster than supply can keep pace.

So what do these trends mean for Canada? Well, let's talk first about the implications for free trade.

I'm on the Business Council for National Issues, and in looking at its membership I find that Nortel Networks is different than the general makeup of the group. You may not realize it but 42 percent of the Canadian members of BCNI – the who's who of Canadian big business -- operate with some form of government protection. It's astounding to me that government protection of Canadian industry is still so prevalent. We have foreign ownership restrictions in all kinds of areas – including finance, telecom, transportation, and publishing – and with policies such as mineral rights, stumpage fees, and marketing boards, you can see that we have a very well developed system of market protection.

The End of Protectionist Policies

Now, as free trade continues to grow, I would maintain that all our protectionist rules will prove to be untenable, and we'll start to see them drop away one by one.

I think that's something we should all look forward to. Just because companies are protected, it doesn't mean they're not good. In fact, we have some great companies that are protected. The problem is that they've found it very comfortable to just operate within the confines of Canada. Protectionism means they've had no incentive to take their skills and go aggressively abroad. They are truly domestic corporations.

The consequence of that – in conjunction with the low Canadian dollar – is that the market capitalization of those companies is generally quite low. People were astounded that Nortel could reach over 35 percent of the TSE – and even now with our bargain-basement prices we're still well over 20 percent of the exchange. Well, a key reason we're so much larger than the other companies on the TSE is that we're one of the few companies in Canada that has tapped global markets for shareholders.

The Canadian marketplace is just too small to support the levels of capitalization we need for our battles with global competitors. And I have to say our large market capitalization is more a statement about the rest of Canadian industry than it is about Nortel. I don't think it's a case of our company being too expensive. I would argue that the rest of Canadian industry is hopelessly undervalued – with domestic protection a major reason why.

Canadian industry must understand that their protection will disappear – it's inevitable – and if they do not move outside our borders for both business and shareholders there will be serious consequences. People outside the country will discover that there are a lot of attractive domestic companies in Canada at extremely cheap prices. They'll say: "Hey, let's go buy a couple." Look at the rumour of the day today -- BCE. The speculation is that it's takeover time, and I have to say the people who'd want to buy that company are not based in Canada.

So as protectionist policies prove to be unworkable over the coming years – and one by one these policies will fall -- our businesses will be exposed for what they're really are -- nice, domestic corporations and industries in a relatively small market, attractively

priced, and probably a little below the critical mass needed to be global. Fortunately, they're not all going to get bought overnight. There's time to remedy the situation.

Look at Nortel as an example. It wasn't that long ago that we were 52 percent owned by BCE. You could say that Nortel had foreign ownership restrictions imposed on us by virtue of the fact that BCE operates in an industry with foreign ownership restrictions. That has changed, and we're proud to be a truly independent global competitor.

Now, in growing as a global corporation, we looked at the area of the Internet as an opportunity for us to play offense. Dating back to the times of Walter Light back in the early 70s when we did our IPO, Nortel has had a long history of looking at changes and discontinuities in the marketplace as tools to improve our position.

Well, the change we're witnessing today with the Internet is one of the biggest society will ever see -- certainly the biggest in my lifetime. And it doesn't represent a great opportunity just for companies like Nortel. It's an opportunity for all companies. I can't think of a company that will not be impacted by it.

Canadian Companies Need to Go Global

Creating customer value is the basic premise of business. If you do not create value for your customer, you won't be in business very long. The Internet helps you create new value for customers in countless ways. And, as I mentioned earlier, it's also the best channel to market ever devised to reach customers throughout the world. My challenge to people in other industries is the following: "What are you doing to use the Internet to tackle global markets?"

For a small country like ours, the Internet presents a particularly great opportunity to attack the rest of the world. My belief is that whenever change takes place it's a big advantage to be agile. The big guy is the sitting duck. I'd exchange 10 percent of the Canadian market for 10 percent of the U.S. market any day of the week. With the U.S. being 10 times larger than Canada that deal would double the size of Nortel.

That shows how there's everything to gain and very little to lose. So let's use the Internet to go for it. At Nortel, we have pursued customers worldwide. This year 95 percent of our revenue will come from outside Canada. And next year only 4 percent will be generated in Canada.

In fact, I believe the idea of being a regional supplier is going to become passé. If you're good at something you should supply that to a worldwide base of customers. In the future, there will be either very local companies or global companies. The idea of national companies is going to disappear.

A global approach to business has rewarded us very well at Nortel. We are going to grow this year by over 40 percent, and that's no small feat for a company that last year had

revenues of US\$21 billion, or in excess of C\$30 billion. That means we'll grow by about C\$12 billion this year – these are massive numbers.

Behind all that success is our chief strength at Nortel -- our people. If there are two rules of business we live by, number one is to create value for our customers and number two is to be valued by our people because in reality they are our only asset. And by the way, in the process of delivering value to your customers and being valued by your people you'll also end up being valued by your shareholders. And certainly Nortel's stock has proven that. In addition to reaching as high as 35 percent of the TSE, we're also the second most valuable telecom company in the world.

With that in mind, let me make a couple of points. First, on being valued by employees, it's important to understand that in today's battle for talent, people elect whether they want to work for you or not.

In Peter Drucker's most recent book, he argues that you have to treat your people as volunteers, because they can work for anyone. You have to make it more enjoyable for them to be spending time with you than they could by spending time with your competitors.

That means they need a greater sense of achievement and job satisfaction for a job well done, and they need to know that they're working on some of the most exciting projects in the world. Creating that kind of environment that will attract and retain the best people in the world is quite a challenge.

Focus on Core Activities

Secondly, in terms of delivering value to our customers, we realized there were a lot of activities we were involved in that did not add any value to our customers. These were activities that supported our operations, and in being honest with ourselves, we realized our company didn't really value those assignments. They were almost necessary evils -- operations that were needed to keep the machine running, but tasks we would never dream of having our best people do. And when we were preparing our budgets, we wouldn't put our first dollar there either. Those activities would be lucky if they got our last dollar.

The key question for those jobs out of our mainstream was: "What value are employees in these areas adding to our customers?" And in answering that question we found many jobs where we couldn't identify any value being delivered to customers. Now, that isn't to say the jobs weren't valuable, but certainly we didn't place a high value on them when it came to directly serving our customers.

In the end, we came to the conclusion that we were doing a disservice to our customers and ourselves, and the reality was that we'd be better off buying these activities as services rather than trying to run them ourselves. And I have to say it was a huge mental step for us to understand that other people could do these activities better than we could,

and that we'd be better off acting as a customer rather than a vertically integrated company that did everything itself.

We wondered how we even got into that situation in the first place and realized that originally we had no choice. As a 105-year-old company, we evolved over a long period of time where there were no companies that could offer those services. We had to do it all ourselves, got in the habit of doing things that way, and it just stuck. But today there are all kinds of companies we can turn to in a variety of areas.

The Need for Agility

Using those companies fits with our need to be agile, which is very important in a competitive environment that's changing so rapidly. It may seem to be an oxymoron for a company of 80,000 employees to be agile, but it's an attribute we simply must possess. The industry is changing too fast to ever predict with detailed clarity exactly how it's going to unfold, and if you can't predict it, you need to be agile to adjust quickly.

It's interesting that the most agile company is the company that hasn't been formed yet because it can do anything. On the other hand, a big existing company has the competitive advantage of owning assets. So there's a trade off between being agile and having the advantage of owning assets. The more assets you have the less agile you are. The fewer assets you have the less of a competitive advantage you have.

To try to get the right balance for our company, we took a critical eye to determining how many assets we needed to run our company. We decided we didn't need 24 manufacturing plants -- just six assembly houses -- so we sold what we didn't need. And we sold them to companies that do a better job of running these plants than we did. Today they're part of an organization that is typically five times as big as our manufacturing group was. Plus, manufacturing is all those companies do. They embarrass us with how good they are, and they give us better prices even though we're paying them a margin.

Most importantly, I can tell you there's no way we could have increased our revenue by 40 percent if I had to ramp up my 24 plants. Adding 40 percent capacity on top of 24 plants would have meant adding almost a dozen factories, and there's no way we could have built that many in one year. But when we turned to the people we were contracting with, the 40 percent growth looked like 10 percent to them because they're so much bigger. It was really easy for them to handle.

An example that for me really hit home the value of outsourcing involved our Training Department. In going through huge changes where all the technology in our industry is moving toward Internet Protocol -- or IP -- we need our people to have all kinds of new skills. We turned to our Training Department to meet the need but they said first they had to get educated in IP. When I asked how long that would take, they said a while because they had to find and read textbooks on the subject.

My response was why don't we just go out and hire some people who are expert at IP and have them do the training? When you have training people in-house they expect to do the job. Well, how expert will they really be? The reality is that you'll never get where you need to be if you have the experts come train your training people. You have to hire the experts to do the training directly.

The Importance of Top Talent

Now, that brings me to another key point about talent. When being agile is paramount, your only asset is your people. At Nortel, we have about 80,000 employees today. But the group we pay the closest attention to is our top talent. They're what the war for talent is all about.

We see the top talent as being roughly the top 10 percent of people – the individuals that are critically important. They have scarce skills combined with passion, vision, insight, and the determination to win – leadership qualities that the other 90 percent of the people will follow.

We have learned a tremendous amount about the leaders we have to keep in the company, who we have to attract, and who's easily replaced. It's very difficult to replace the top 25 percent and almost impossible to replace the top 10 percent. And, though it sounds cruel, frankly it's easy to replace about three quarters of our people. In fact, in many cases we're becoming pretty hard on the people who are in the bottom 25 percent because they need to leave to make room for more top-potential people to come in.

Our transition in this area has been quite dramatic. We've gone from an environment where Nortel was based on entitlement to one where twice a year we judge and reward every employee's contribution to the success of the company. What we found is that many of the top managers had made great contributions many years ago but, as one of my executives says, they are now "rested and vested." These are people who hadn't made much of a contribution for many, many years but were still pulling down big paycheques and occupying big offices. I think you could describe the situation as the business world's equivalent of tenure. Well, those people are no longer with Nortel because we could clearly see how their recent contributions were not what we needed. This is the new world.

On the other hand, top talent is in such demand in our industry that we realize we can no longer ask the star performers to come work for us on our terms. We now employ the top talent on their terms, so if they want to live in Toronto or Ottawa or Monkstown or San Jose or Boston or Dallas or Atlanta or anywhere else, it doesn't matter to us. They can work wherever they want. We just want them to work for us.

I think the days are gone when multinational companies can come in, build a facility, and then ask people to move to where the company wants them to be. I think the days are coming, especially with the power of the Internet, where more and more corporations will

do what we're doing. They'll ask the bright talent where they'd like to live and employ them wherever that is.

The Role of Government

Now, let me put all I've talked about – the trends toward globalization, the Internet, the end of domestic protection, the decreasing importance of natural resources, the importance of talented knowledge workers, and so on -- in the context of public-private partnerships

Well, to start, I would say that one of government's primary tasks is to set the economic strategy of a country. And in Canada, if my assertions are right, there is much to do. I would characterize it as the need to get Canadian businesses to be more like Nortel – which means getting them to play offense instead of providing defensive economic protection.

I view business as a sporting game, but it's one without a clock. It's like watching a Grey Cup that never ends. You can't sit back if you're ahead by a field goal and just hang in there for another 2 or 3 minutes until the clock runs out. The only way you can win is to play offense all the time.

Having that kind of approach – spurred by the end of domestic protection -- requires new mindsets and new ways of thinking. For example, we need more confidence. Good companies don't need protection. They need encouragement. That's playing offense.

I mentioned earlier that domestic companies need to go global to survive in the future. Well, with the Internet as a channel to market, I think every Canadian company should be viewing itself as a global player. That's playing offense.

We need to take full advantage of the telecom infrastructure that will be the backbone for Canadian industry's ability to reach a worldwide base of customers. Fiber optics are the information highway of the future. There was a rule in the past that you wanted to locate your company close to the highways – in fact, waterways if you think back far enough. Most recently it has been the airports, but in the future it will be proximity to fiber optics. So making Canada the most connected nation in the world is clearly the right agenda – one that a country playing offense has to have.

And with the industries of the future based on knowledge-intensive tasks, a country playing offense will also focus on having the most talented workforce in the world. As I mentioned, the work will come to the top people wherever they want to be – so why not make that Canada? When's the last time we've heard of a brain drain into Canada? That would be playing offense.

The economic strategy of Canada has to be based on building and training our people to levels of excellence that others in the world wish they could attain. We need to make sure

that the best talent choose to make Canada their permanent home -- not just a home for retirement.

For a knowledge-intensive world, we also need to improve our schools. They have been starved for funding. In the election there was a lot of talk about health care, but what has been overlooked is that the schools are in a similar situation with a lack of funds.

We've got some great institutions. I can vouch for that. But we need to keep those schools strong. Nortel is doing its part. We put all of our corporate contributions behind the educational system -- \$25 million a year in scholarships to students so they can go to the schools of their choice.

Be A Role Model

As well, and of importance to all of you here, if we're to succeed in playing offense Canadian business needs a good role model. Many Canadian industries are worried about embracing the Internet, and this is where the government itself can play a big role. If the government can become Internet-centric and truly embrace the Net as a service delivery means for its customers and constituents, that would be an inspiration to all industries. To put it more bluntly, industry will say, "My God, if the government can do this, I'm sure that we can."

So please step up to the challenge and get it done. The neat thing is you don't have to do it yourself. You can hire other people to do it -- demonstrating how well public/private partnerships can work. Rather than just giving companies funding, you can think of yourself as a customer creating suppliers.

In the process of our outsourcing at Nortel we have created a tremendous number of businesses that now serve not just us but hundreds of other companies. Our partnerships have created organizations that are expert in metal work, circuit boards, payroll systems, running real estate -- all kinds of activities that we were struggling to do ourselves. Now we have an array of expert companies to choose from.

Talent is Our Most Precious Resource

To conclude, I'd like to return to my point about the war for top talent. I kicked off a debate about 18 months ago that became characterized as the brain drain, and it's certainly an issue Canada has to pay a lot of attention to. Top talent is the natural resource of the future, and if a company like Nortel pays so much attention to it why wouldn't a government do the same?

I believe that whenever Canada loses one of its talented people there should be an exit interview. We should find out why people leave and what we can do to fix the problem so we never lose another person. If exit interviews work for industry, they could sure work for a country.

We're talking about a natural resource that we can't keep let creep away. It's like selling off our water and other natural resources we feel are so precious. Remember that companies will go to where the talent will be, so if you want to attract great job opportunities, you need to have a gold mine of really valuable people. I think the government's budget certainly moves us in the right direction, though I take every opportunity to encourage the government to go a little faster.

To summarize, I think the role of government is to be a role model – in particular for how to move on to the Internet and to demonstrate to the rest of the world that all of Canada is connected. And it isn't just having fiber optics but knowing what to do over top of it.

Please use your purchasing power to create suppliers. Give them contracts to supply you with goods and services -- and make them deliver.

And above all, I urge you to create an atmosphere of winning. It would be really nice to have Canada be the country from which it's the most fun to run a winning business.

Thank you very much.