

GOOD PROFIT

How Creating Value for Others Built One of the World's Most Successful Companies

CHARLES G. KOCH

CHARLES KOCH has been chairman of the board and CEO of Koch Industries, Inc. since 1967. In that time, Koch Industries has grown from being a \$21 million company to one which is now worth more than \$100 billion. Mr. Koch is well known and well regarded for his support of institutions like the Cato Institute and the Institute for Human Studies as well as for his various non-profits like the Charles Koch Foundation and Youth Entrepreneurs. Charles Koch is a graduate of The Massachusetts Institute of Technology (MIT).

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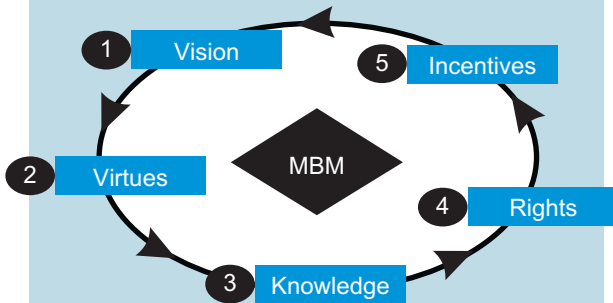
MAIN IDEA

Koch Industries, Inc. (founded in 1940) is today the second-largest privately held company in the United States, with annual revenues exceeding \$115 billion. If Koch were listed, the company would rank at 17 in the Fortune 500. And impressively, an investment of \$1,000 in Koch in 1960 would today have a book value of \$5 million – a return which is 27 times higher than the S&P 500.

"What is Koch's secret? I believe it is Market-Based Management, our unique business management framework, which has allowed us to keep pace through half a century of dramatic change."

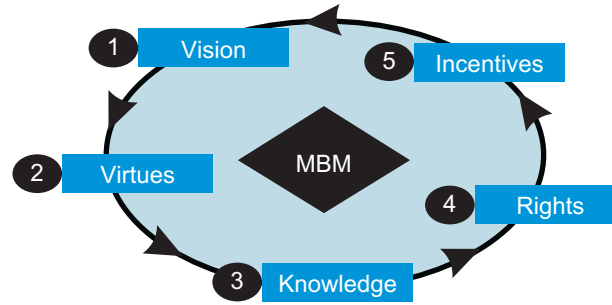
– Charles Koch, CEO

Koch's Market-Based Management (MBM) framework has five dimensions:



- 1. Vision** – strive for good profits which benefit customers and society as a whole.
- 2. Virtues** – hire based on values first and talent second, not the other way around.
- 3. Knowledge** – create a culture where the best ideas win regardless of who puts them forward.
- 4. Rights** – let employees take complete ownership of their work roles and responsibility for outcomes.
- 5. Incentives** – make it possible for anyone in the company to earn more than their boss if he or she creates more value for the customer.

The underlying goal of MBM is to enable a business to create more value and drive creative destruction faster and better than existing or potential competitors. It works.



Vision Pages 2 - 3

Koch works on the assumption the role of any business is to provide products and services which customers will value more than all other alternatives whilst using resources more efficiently than others. The company exists to earn "good profits" – to profit by providing offerings which benefit customers and society at large.

Virtues Pages 3 - 4

Hiring for skills and talent is great but if employees don't have the right day-to-day values, it won't help you get ahead. Koch's approach is therefore to hire for values first and then to hire for talent.

Knowledge Pages 4 - 5

Knowledge in and of itself has value but Koch focuses on how best to use information to produce results. You need good knowledge processes to be in place which will enable everyone to be innovative and to share their discoveries so others can build on what they find. Innovative organizations share knowledge wide and far.

Rights Pages 6 - 7

It's a well-known fact owners take better care of their property than renters ever do. Similarly, when an employee "owns" a process or a responsibility, they take greater pride and responsibility for outcomes. Koch works hard to grant decision rights to whichever employee has the greatest comparative advantage to make the best decision.

Incentives Pages 7 - 8

The fifth dimension of market-based management is to align incentives in a beneficial way. When Koch employees create superior value for the company, they get rewarded proportionately. MBM completely avoids any limits on what employees can earn – the more value they create, the more they earn.

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