IN CONVERSATION *with* KATIE TAYLOR

By: Lisa Ritchie & Anne Maggisano

A key theme of our Women of Burgundy studies has been capital allocation, the process by which management allocates the financial resources within a company. Some examples are paying down debt, investing in research and development, returning capital to shareholders in the form of dividends, and making acquisitions. Capital allocation is an important topic because an investor should be confident that the management of investee companies are allocating capital in ways that are in the best interest of its stakeholders.

In May of 2018, we were honoured to host an evening with Katie Taylor. As former CEO of Four Seasons Hotels & Resorts, Katie was directly responsible for making capital allocation decisions. Today, she evaluates management's decision-making in her roles as Chair of the Royal Bank of Canada, Altas Partners and Sick Kids Foundation. She is also Vice-Chair of the Adecco Group, and a director of Air Canada and the Canada Pension Plan Investment Board. We recently sat down with Katie to catch up on her current thinking. The highlights of our discussions follow.

Lisa Ritchie: In your experience at Four Seasons, what were the key drivers of capital allocation decisions?

Katie Taylor: A little background: In 1989, I was a securities

Katie Taylor speaks with Lisa Ritchie and Micha Choi.

lawyer at Goodmans and a former colleague called seeking a number two at Four Seasons. I joined and became the number two in the two-person law group, so, very glamourous beginnings. At that time, we were not what you now know Four Seasons to be. We operated 23 hotels in Canada and the U.S., and one hotel in London. In those days, we were about half-management and half-ownership of hotels.

The great real estate collapse of the early 1990s taught us some formidable lessons about scarcity of capital. As you can imagine, the ownership of hotels is incredibly capital intense, whether that relates to servicing them, refurbishing them, or building them in the first place. The cost of a brand-new Four Seasons Hotel is significant, and then there is the additional cost of funding the ongoing upkeep and improvements.

During the 1992 real estate crisis, two things really came to the fore. First, there was a general downturn in arrivals at hotels. So, loss of some revenue and, in some cases, serious financial pressure. At the same time, the market experienced a collapse in real estate values, which had a significant impact on a lender's ability to sit tight waiting for interest payments. All of this caused us to sit back and rethink our business model.

We were a relatively small company, maybe by then about 35 hotels; so, a small enterprise trying to do many things with scarce capital. It was at that point that we made the decision to concentrate all of our energy on the sweet spot of the business, which was hotel management. The skill of the Four Seasons leadership team was not in the owning of the bricks and mortar, but in the creation of the experience inside the walls. The process involved transforming from a real estate company to a brand-management, customer-experience and talent-creation business. This required a deliberate shift in how capital was invested within the business. Third-party owners were actively sought and secured for the hotels we owned, thereby freeing up capital to invest in elevating the hotel management part of the business.

LR: So, this strategic business shift led to a reallocation of capital, thus increasing the probability of success.

KT: Absolutely. When we entered the U.S. in the 1970s, for example, Four Seasons was not the brand it is today. We had the Four Seasons name on some hotels, but many of the hotels had another primary brand, like The Clift in San Francisco and the Ritz Carlton in Chicago.

We came to realize that our strategy around investing in people, systems, talent development, customer experience and innovation would set us apart from all of the big brands—the Hiltons, the Marriotts and the Sheratons, who were leading the field in the global hospitality market at that time.

So, in the late 1990s, the decision was made to double down on the Four Seasons name. This resulted in a significant capital spend to rebrand a number of hotels across the globe. We invested significantly to acquire the rights to the Four Seasons name in New York City, which enabled us to brand the flagship Four Seasons Hotel in midtown Manhattan. It was an investment that helped change the way people thought about Four Seasons and a step toward building critical mass under one brand name.

LR: What factors did you consider in deciding where to invest time and money to develop new properties?

KT: In the hotel development business, you can run around the world looking for a needle in a haystack or you can be well positioned when a key opportunity comes up. An ideal hotel development partner needs access to significant capital and they need to control the land in a desirable location in a city or a destination that can support the long-term operation of a Four Seasons hotel.

Sometimes we competed with Ritz Carlton and with Park Hyatt and other big brands, and in those cases, it was about selling our proposition over theirs. Did we win every time? No. Did we win most of the time? Yes. That was a testament to the investments we had made in people, in distribution systems, and in client and travel agent care, all over many years.

> “What our people and our leaders did next was extraordinary. The local management teams rose to the occasion, designing new ways of thinking about running their properties. Revenue was under pressure, so there was only one way to get through it and that was to manage costs effectively. No idea was a bad idea, but there was a simple test: is the customer experience the same or better?”

LR: We can't talk about capital allocation decisions in an economically sensitive business such as hospitality without asking about the 2007–2009 financial crisis. How did you lead Four Seasons through that time?

KT: I never want to live that again. In fact, I never want anyone to live that again. At the time, all the focus was on the crisis in financial services, but the impact on the hospitality industry was very significant. Many millions of people working in hospitality in America and elsewhere lost their jobs. In our business, it was the confluence of two things: a huge economic crisis combined with the political stigma of being seen doing something that was enjoyable and relatively expensive.

You've heard about women who hid their luxury purchases in brown unmarked bags. The same thing was true with companies. Some of our hotels saw over 25% drops in revenue in a matter of weeks. So, you can see how unbelievably devastating that would have been. Within the first year or two of that crisis, a number of hotels had gone into the hands of special servicers* because the loans for those hotels were part of big, commercial, mortgage-backed securities portfolios. All of a sudden, the industry went from relationships with long-term capital partners, people we'd all known for decades, to talking to representatives of the lead lenders on properties that were in distress.

Then it became a question of righting the ship. Back to capital allocation and being smart. Really scarce resources, depressed top lines, very high fixed costs. The industry had never seen a crisis this deep, this broad. We all had experience with recessions, but we didn't have a roadmap for this one. Which brings us right back to investing in leadership and making sure you have the best people in the world doing smart things.

What our people and our leaders did next was extraordinary. The local management teams rose to the occasion, designing new ways of thinking about running their properties. Revenue was under pressure, so there was only one way to get through it and that was to manage costs effectively. No idea was a bad idea, but there was a simple test: is the customer experience the same or better after the recommended change? Our standard was that it couldn't be worse.

I remember visiting one of our hotels in California where the General Manager made a point of introducing me to a young woman who had seven uniforms. Why seven? Because they wanted to keep as many people employed as possible, so this young woman worked one day a week in the spa, one day in landscaping and another day in the Kids for All Seasons. It was a local solution to a very big problem.

LR: Speaking of that time, you were also on the Board of the Royal Bank of Canada. Take us through what was happening around the boardroom table.

KT: As we all know now, early signs of the liquidity crisis first emerged in the summer of 2007, but it was not until the fall of 2008 that the U.S. had the first

*Special servicers: specialists in managing troubled commercial real estate loans failure in Lehman Brothers. That triggered a series of questions in board rooms around the world: Can this happen here? What if this happened here? Boards and management were running through all the stress analysis, assessing the level of interconnectedness and determining counterparty risks.

Canada didn't have as much exposure as the rest of the world to the subprime marketplace and that wasn't by happenstance. When you look at the way the Canadian financial system is set up to operate and the way management at all institutions responded to the crisis, you see that all the Canadian banks came through it extremely well. Everybody had pockets of distress, a little bit of tail risk here and there that wasn't expected. In the end, we all learned so much as a result of that process. There isn't a boardroom in the industry that wasn't fundamentally changed by the experience.

LR: Let's switch gears a little. How would you advise an individual to look at their capital allocation?

KT: For most people, capital is a scarce resource and not something we have in endless supply. Like anything else in life, it's about setting priorities and continuing to re-evaluate those priorities, not only against the things you're interested in investing in or supporting philanthropically, but also against ongoing performance. How well have those investments done? How well has that charity been performing?

Performance in the world of investing is usually pretty easy to assess because there are absolute numbers and benchmarks. It's a bit harder to assess the impact of your philanthropic investments, particularly if they are directed to things like research. We have scientists at Sick Kids Hospital that are doing all kinds of research that will only be commercialized beyond my lifetime, but someday a life-changing cure will come from that basic research. Think of the people who first started to work on the Genome Project. The scientific discoveries that are built on the back of that decoding are transformative, resulting in both an economic as well as a social return.

Setting priorities and evaluating performance should be something that families talk about. My husband and I are transparent with our children about the fact that they lead a privileged life. It was important to us to ground our children in the basics. So, while we had the opportunity to stay in really nice hotels as part of my role at the Four Seasons, we talked about how that wasn't the norm.

> **“My experience has been that once one woman does something, others can see it and then do it too. A lot of women say to me, “They are only calling me because they need a woman.” Of course, I say! Virtually all of the boards I serve on sought me out, for my global business experience, yes, but also because I am a woman.”**

That led us to relatively early conversations about how to think about the world. Our children are very involved in philanthropy in their own way. They've made a couple of large gifts from the family foundation, which involved making decisions on capital allocation and execution. So, they actually had to understand how the money was going to be used. They are also involved in the monitoring of performance. And then it's back to priority setting and scarce resource allocation because there is never an infinite amount of cash.

LR: You're a strong advocate for women in business and women on boards. How are we doing?

KT: There is no way to sugar-coat this: we've been talking about parity for women in the workforce since before I started working, which is really a long time ago. If you look at just the top of companies, whether it's the boards, whether it's the senior management teams, has there been progress? Yes. Has it been at a glacial pace? Yes.

This is a big deal everywhere, but it's a bigger deal for places like Canada, where we have such a small population and such an underrepresentation of women in the economy.

LR: And so many highly educated women…

KT: Yes. We spend all this money on the health, welfare and education of 50% of the population, and somehow, they're not liking the options that are available to them in the world of work. I think we need to do some serious soul searching around what the fixes are. There are very good policies in most well-managed companies. And very good oversight of HR in diversity and inclusion. And most have done the right things when it comes to family leave. But are we doing enough? Probably not.

I always ask people, “What's going on at your office that women don't want to stay and become the CEO? What's happening in your business that 55% of your hires are

Four Seasons Hotel, Toronto.

female—that's about the graduation rate out of university—but they represent just 2% of your executives? You have the policies, you're talking the talk, probably walking the walk, but something's still not working."

Maybe the problem is not process, maybe it's structural. Sometimes one little thing can make a very big difference. Early morning meetings are really hard for women with children. I didn't generally schedule a meeting before 8:30 a.m. when I was running Four Seasons, because I had to drive one of our kids to school. It was the same thing at night. I would arrange to leave a business dinner before dessert so I could get home and tuck the kids in. Easy to do when you are a senior-level woman, so let's think about things like that.

Here's another small but bold idea: ask every 30-year-old woman in your office what two things you could change to ensure that they stay forever. Sure, you'll get hundreds of ideas, but what's wrong with that? You also might find out that some of the things they suggest are pretty straightforward and not difficult to do. And then you will find that the women will double down and triple down on the business, and then do what I did and stay!

In March of this year, I co-authored an op-ed for the *Globe and Mail* in which I talked about how candidates typically must have experience managing profit and loss in a line of business before they will even be considered for the CEO role. This is a challenge because we see that many women are disproportionately concentrated in human resources, marketing, communications, finance and legal— even at the executive level—and from this position it is often a monumental task to be considered for CEO. Women need to be proactive in seeking out operational roles all throughout their career so that the path to the C-suite remains open.

LR: Can you share final thoughts on getting more women on corporate boards?

KT: Change is finally in the air. Recently, proxy advisors have put out guidelines around promoting diversity. The big investment managers, whether it's CPPIB (Canada Pension Plan Investment Board) or others, now have guidelines around diversity on boards. I think the intervention of the institutional investors into this dialogue around best practices and board diversity will be a turning point.

I also think we understand perfectly the social good of diverse teams, women in the mix and non-gender diversity as a driver of innovation and more. But we also need to focus on the fact that there is a soft "economic" issue here, where, historically, boardroom representation has been like a trading card. Think of it like an invisible currency traded on an invisible block chain. Fostering change with people that have been part of that network for over a generation is sometimes difficult to achieve. Term limits are something people advocate for and lots of people have age limits. But, it's always going to be more than that.

I was the first woman who did a lot of things—not just Chair of RBC—and my experience has been that once one woman does something, others can see it and then do it too. A lot of women say to me, "They are only calling me because they need a woman." Of course, I say! Virtually all of the boards I serve on sought me out, for my global business experience, yes, but also because I am a woman. And in all cases, the number of women on these boards has either been maintained or it continues to increase. Women can push this agenda forward. We just need to get to the table. **M**