

# The Wichita Eagle

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Koch's Hidden Message

## Koch has grown quickly, quietly

■ Under Charles Koch's guidance, conglomerate has kept a low profile.

By Molly Mcmillin

The Wichita Eagle

Koch Industries is a gargantuan company with a global reach.

Once a mid-sized but significant player in the oil industry, the company has grown nearly 300-fold in the past 30 years, with \$30 billion in revenue last year.

Based in Wichita, Koch Industries is the second-largest privately held company in the nation. If it were a public company, it would rank roughly the country's 21st largest – behind PepsiCo, but much bigger than Boeing Co. or Microsoft. Consider:

■ Koch operates more than 40,000 miles of pipeline – enough to circle the Earth 1½ times.

■ Its two refineries process about 540,000 barrels of crude oil a day.

■ It is the country's largest buyer and seller of asphalt.

■ It operates cattle ranches on 450,000 acres of land and ranks in the top 10 calf producers in the U.S.

■ It is the country's 34th-largest landowner, according to Worth magazine.

Koch Industries operates dozens of diverse businesses – businesses that are often overlooked but are the underpinnings of an industrial society.

But because Koch has a long history of being tight-lipped about its successes and its operations, many people may have difficulty immediately recognizing Koch's impact on Kansas, and Wichita in particular.

That's why so many eyes were popping about 10 days ago, when Koch announced it would significantly expand its Houston operations – a solid and logical business move, but a blow to hometown pride.

There are impediments to its growth in Wichita, company officials said. Among them is the ability to attract employees to

the city and the availability and cost of air service.

Those impediments may be a factor when it decides where to direct its future growth, the company said.

"It is very difficult to get metropolitan-area people to come to Wichita, Kansas – particularly if they come from the north and the east," said Bill Hanna, Koch Industries' president.

Koch is a major area employer, having nearly doubled its work force in the past 10 years. About 2,800 of its 13,000 employees worldwide work in Wichita. In 1987, it employed 7,000 worldwide, including 1,232 workers in Wichita.

And the company is a major contributor to a long list of local and statewide philanthropic endeavors, such as Big Brothers and Sisters, Rainbows United, Heartspring, Music Theatre of Wichita and Youth Entrepreneurs of Kansas.

The company recruits from area and regional universities and beyond, and from top business schools from around the country. And it recruits professionals from across the country.

Last year alone, Koch hired 600 or 700 professionals and 150 or so college students, Hanna said.

Koch Industries' interests are divided among 10 business groups. The biggest chunk of its assets and a good portion of its profitability has been in the refined products and chemical areas, said Paul Brooks, senior vice president of Koch's capital services group.

But gas liquids, crude oil services and energy service areas are also significant parts of the business, he said. Materials, chemical technology, mineral services, agriculture and capital services make up the remaining groups.

Each of the 10 groups operates under the auspices of five or more legal entities, Brooks said.

Koch is a huge player in several major industries because of the acumen of its chairman and chief executive, Charles

Koch, said Sterling Varner, a former Koch president who is now retired.

"He sees opportunities that other people don't see," Varner said. "He's always pressing on to something."

Koch was the one who pressed to enter the gas liquids business and the chemical business, he said. And he has bought and turned other companies' castoffs into successful operations.

After buying Sun Oil Co.'s refinery and petrochemical plant in the early 1980s, for example, the operation has grown about 20-fold, Varner said.

Growth has come to all phases of Koch's businesses through patience, prudence and

from a keen sense of timing.

"Koch is a formidable competitor," said Ray Ory, president of Vector Associates in Houston, a consulting firm.

"They've stuck to their knitting over the years and I believe they've reaped the benefits of investing resources in the businesses they know best," Ory said.

Koch reinvests heavily in the corporation – pumping 90 percent of its earnings back into the businesses – a reinvestment difficult to match by the standards of any publicly held company, and a particular advantage in the capital-intensive oil and petro-chemical businesses. Its private status also allows officials to seize opportunities, making decisions and following through on them quickly.

Charles Koch, now 61, took over the reins of the company from his father and founder Fred C. Koch. David Koch, Charles' younger brother, runs the firm's chemical operations from New York.

Charles followed his father's footsteps and attended the Massachusetts Institute of Technology. After a stint at Arthur D. Little & Co., a prestigious consulting company based in Cambridge, Mass, Fred C. Koch called Charles back home to help him run the company in 1961. The elder Koch died in 1967.

Under Charles Koch's leadership, revenues have skyrocketed.

**In 1967, the company had revenues of \$177 million. By 1994, that figure had swelled to \$24 billion.**

In 1967, the company had revenues of \$177 million. By 1994, that figure had swelled to \$24 billion. And last year, revenues totaled nearly \$30 billion – a 25 percent growth in two years.

The company will not reveal earnings or profits.

Charles Koch, in an interview at company headquarters last week, called the corporation a “discovery company” – one in which employees are charged to seek ways to “create value,” by finding new ways to integrate and use its diverse operations.

“Everything is open,” he said.

But that doesn’t mean there haven’t been failures along the way.

“We’re trying to find new ways to create value,” Koch said. “If we’re not getting any failures, we think we’re doing something wrong.”

One of the company’s most recent failures was its attempt to produce a product from slag generated by steel mills. The company didn’t fully understand the process before it delved into the business, an operation it quit late last year.

How big was the hit?

“It was sizable,” Koch said. But “it didn’t cripple us.”

Koch has long followed the philosophy and methodology of market-based management, which applies the principles of how free-markets bring about social progress.

His vision for the future is to expand its thinking and integrate its lines of businesses in new ways.

For example in the past, the company would buy, transport and market gas to its customers. Now it can provide risk management, financing, management and environmental services packaged to meet an individual customer’s needs, Koch said.

And rather than only delivering oil to producers, the company will lend them money to drill wells, upgrade plants or buy land.

“We’re trying to do that in all the different industries we serve,” Koch said.

In business, Koch said, there are four kinds of firms – industrial or operating, distribution or trading, finance or investment banking and service or consulting firms.

“We’re saying to do this, we have to do all four,” Koch said.

Any acquisitions will be made only if they fit logically within existing operations, Brooks said.

It is difficult to predict which of its operations will be most successful, because commodities markets are so volatile. What produces explosive growth one year may collapse the next.

## KOCH’S BUSINESS ACTIVITIES

Koch Industries is the second-largest privately held company in the country, with 1996 revenues of about \$30 billion – almost \$1,000 a second, every second of the year. Koch business encompasses 10 major areas.

■ **Refined Products Group:** Manufactures and markets refined fuel products, including gasoline, heating oil, diesel fuel and jet fuel.

■ **Chemicals Group:** Supplies feedstocks to the petrochemical industry and markets both commodity and specialty chemicals.

■ **Crude Oil Services Group:** Involved in exploration, production, purchasing, trading and transportation functions in North America.

■ **Gas Liquids Group:** Produces, purchases, processes, transports, stores and markets gas liquids.

■ **Mineral Services Group:** Markets bulk commodities such as petroleum and metallurgical coke, coal, anthracite, slag, gypsum and molten sulfur, sulfuric acid and carbon dioxide.

■ **Materials Group:** Manufactures asphalt-based products for the construction industry. With more than 100 plants, it is the largest buyer and seller of asphalt in the country.

■ **Chemical Technology Group:** Manufactures combustion and vapor recovery equipment, heat exchangers, membrane separation systems, corrosion-resistant materials and distillation, mixing and mist-elimination equipment.

■ **Agriculture Group:** Involved in beef production on ranches and feedlots; produces, trades and distributes fertilizer and other chemicals used in agriculture; financial services and risk management; and in the milling and processing of oil seed, grain and feed. Koch Beef Co. is one of the top 10 calf producers in the country.

■ **International Group:** Works to develop and expand Koch Industries business internationally. Koch has offices in Calgary, London, Mexico City and Singapore. It also operates a Canadian oil business involved in oil exploration, pipelines and crude oil and gas trading.

■ **Capital Services Group:** Funds Koch companies and their venture partners. Activates range from asset trading to advisory service for Koch and its customers.

■ **Energy Services:** Through Koch Energy Inc., this division includes Koch Gateway Pipeline Co. and Koch Energy Services. The company combines natural gas transmission, gathering, storage and processing facilities in the southern Gulf region.

The company expects growth in all areas, but especially in international business, trading and agriculture.

Koch has overseas offices in Singapore and London. Last year, it opened offices in Mexico city and Venezuela.

Its agriculture business is small when compared to Koch’s other operations, but it has the potential to be a growth leader for the company.

“We find that by integrating our milling business with our farm service centers and our fertilizer business and our grain genetics, that we should be able to double the revenue for a farm,” Koch said.

Koch work with seed genetics, for example, helps farmers grown corn with a higher oil content. The oil helps put weight on cattle. If that corn is sold especially for that use to feedlots, the corn grower can command higher prices. The feed lot ultimately receives higher prices for its cattle.

And it is working to improve the quality of beef through genetics, a move that has been successful with chickens by feeding consumers’ demand for large, high-quality chicken breasts.

Those attempts to innovate across all

business lines leave Varner, the former Koch president, optimistic for the future. When asked to predict where revenues could be in five years, Varner said they could likely double.

Koch said he does not measure success by revenues.

“Our measure is what value we are creating,” he said.

Koch has no plans to slow down anytime soon.

“I think everybody has to live and be happy,” he said. To do that, “you have to use the abilities and you have to pursue.”

Molly McMillin can be reached at 269-6708.