



SAVING CEOs (AND THEIR COMPANIES) FROM THEMSELVES

How to avoid the ego-traps in big moves

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Over-confidence is a common trait in successful ambitious leaders. Success breeds confidence. But does confidence breed success? Some companies have paid a high price for the self-esteem of their top people.

The major disasters in the recent and ongoing credit meltdown, at banks like Citigroup, UBS, Merrill Lynch and Lehman Brothers, can be traced back to the firm controlled by a dominant personality, a docile top team and boards with a glaring lack of financial expertise. Obviously, the blame can be shared: with regulators and rating agencies that didn't do their job properly, risk managers who didn't raise the red flag high enough, the Federal Reserve that threw money at the party, and the yes-men that made up a majority of those boards.

But this is hardly the first time that the banking industry has had a melt down. As recently as July 2002, the Economic Letter the Federal Reserve Bank of San Francisco said: "The recent wave of financial crises in emerging markets—Mexico in 1994-1995, Asia in 1997-1998, Russia in 1998, and Argentina in 2001—has exacted a considerable toll in terms of lost output and welfare and at times even posed a threat to the stability of world financial markets. As a result, many policymakers and economists have focused on the lessons to be learned from these experiences - lessons both in how better to prevent crises in the first place and in how to manage crises once they occur."

Yet, five years later it all went wrong again.

Over-Confidence and Success

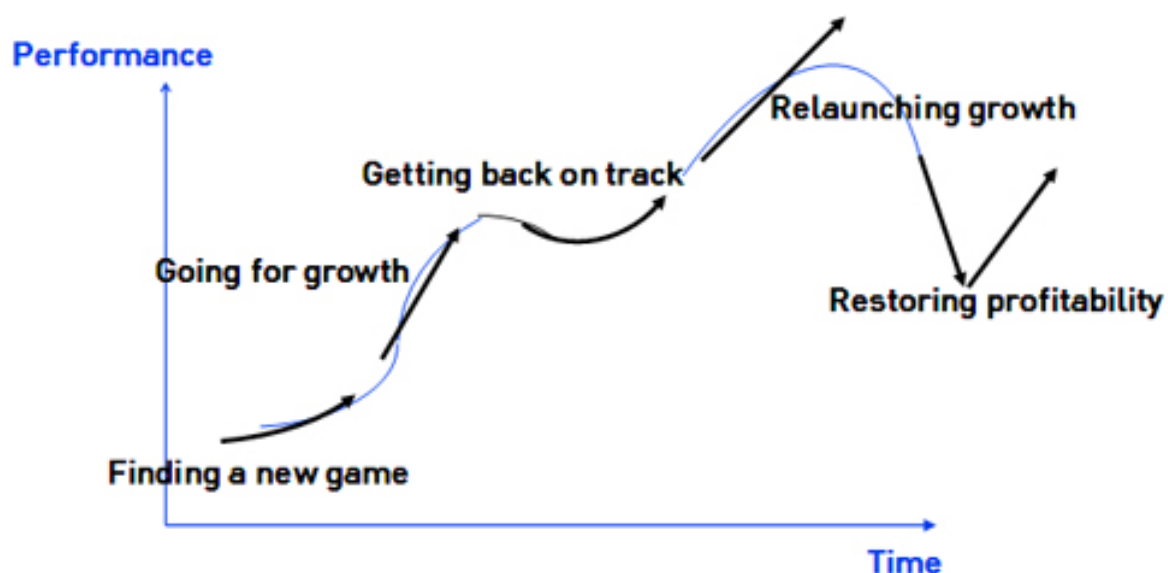
Jack Welch once said: "Oh hell, everyone in this game has ego. You have to have self-confidence to seize the opportunities." A few years later, he was to confide, "My hubris clearly got in the way in the Kidder Peabody deal. I got wise advice from Walter Wriston and other directors, who said, 'Jack, don't do this.' But I was bully enough and on a run to do it. And I got whacked right in the head."

Successful, ambitious people achieve positions in which they encounter many temptations and enjoy the power to indulge their urges. They can construct masterful rationalizations to persuade others – and themselves – that what they're doing is right. They are clever enough to talk others into acceding to their wishes, even when what they are saying is disconnected from reality. Indeed, research shows that successful, ambitious people have higher opinions of themselves than do observers of them. All of this makes them prone to hubris – that is, underestimating the challenges and overestimating their abilities.

What we have found in our observation of the smart and stupid moves made by companies over 15 years, is that leadership egos are most likely to get out of control when companies make big moves, the ones that will make or break them. Making big moves requires concentrated doses of leadership ambition and self-confidence, which open up ego-traps created by hubris.

Five Big Moves and Ego-traps

There are five classic types of big move - strategic shifts involving a large commitment of resources to a new goal. These are depicted below, each corresponding to a different position on the corporate performance curve. The sequence of moves shown is arbitrary. Big moves can be advantageous in any order depending on conditions inside and outside the company. However, for each of the big moves, a related ego-trap often gets in the way of rational decision-making.



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Finding a new game is about creating an entirely new business model to replace an existing business that is dying, or taking advantage of a new technological or market opportunity. Those trying to find a new game often think they can run any business – all they need to find is a great opportunity. They fall into the trap of opportunistic hubris – we can seize any opportunity, run any business.

Going for growth is about rolling out a business model that works, developing the resources needed to adapt the value proposition to new markets and riding the growth wave. Those going for growth often overestimate their understanding of the market and believe they know what the market wants. They fall into the trap of inside-out projection – we know what customers need.

Getting back into shape is about reducing costs by increasing the efficiency of the value chain of activities and enhancing the value proposition through the way it is produced and delivered. Those trying to get back into shape often believe they are doing better than they are, in a state of denial that anything is seriously wrong. They fall into the trap of narcissistic denial – we're the best, there's nothing wrong with the business.

Re-launching growth is about increasing revenues by re-designing the value proposition and/or adding new lines of business to serve well-defined growing markets. Those trying to re-design the value proposition to re-launch growth, often believe they can emulate and beat successful competitors at their own game. They fall into the trap of me-too imitation – we can beat the competition no matter what they do.

Restoring profitability is about turning around loss-making activities by re-focusing the business model on the core money-making parts of the business. Those trying to restore profitability often believe they can avoid the pain of restructuring by growing their way out of the problem. They fall into the trap of **raising the stakes – we never admit defeat, we always move forward.**

Avoiding the ego-traps

Calling for greater self-discipline, exhorting executives to be open to facts that don't fit their preconceptions, or opening up time in their agendas to see, hear and understand what's going on, is futile. The adrenalin and energy needed to drive big moves make it almost impossible to calmly weigh the risks involved. More pointed checks and balances are required.

The school of hard knocks

The most effective source of self-discipline is the painful memory of a previous failure. In Silicon Valley, venture capitalists like to say that the safest managerial bet is an entrepreneur with two previous failures. When he came back to Apple, Steve Jobs had been chastened by his experience outside and was much more realistic, not trying to create new markets, but addressing those that already existed. By contrast, in the banking industry, careers are so short that each new generation of managers seems to have to learn that you can't lend money to people who can't pay it back. One of the reasons Credit Suisse did much better than UBS in avoiding the sub-prime disaster was that those at the top had more recent memories of previous investment and lending excesses.

Powerful sparring partners with red flags

The most effective antidote to the ego-traps is sparring partners with sufficient personal and institutional power to block big moves that don't add up in terms of their strategic logic. The banks that did best in avoiding the sub-prime crisis had boards of directors with clout and significant experience in financial services. To complement powerful boards with expertise, each of the big moves calls for different types of sparring partners:

- **For entrepreneurship, venture capital-type opinion** can be useful to ensure that you have a compelling new business model and you don't assume that managerial expertise trumps industry-specific capabilities.
- **For roll-out, the customers' views** are essential to ensure that you create value for them. Put yourself in the shoes of your new customers to see what your value proposition looks like from their point of view.

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- **For re-positioning, the competitors' perspective** is essential, to ensure that you don't try to beat them at their own game. Step into the shoes of your top competitors to see how they will respond to your new value proposition.
- **For re-alignment, frontline employees' opinions** are essential because they know what needs to be fixed and their commitment will be necessary to make it happen. See whether or not their critique reflects where the business is on its trajectory.
- **For restructuring, independent auditor and financial analyst opinions** are useful because their valuations depend on understanding the core elements of distinctiveness. To avoid raising the stakes, ask whether or not you could defend betting the whole company on an unproven growth move.

Peter Brabeck, the former CEO of Nestlé put it this way: “If I have a yes-man on my team, I have one too many. I will fire him.” But, it's not only about being checked by sparring partners; it's also about having to listen to the right people at the right time. Listening to your engineers when you roll out a new product is a good thing, listening to them when you need to restructure, may not be as helpful.

In summary, powerful sparring partners that can raise the red flag and challenge the top team on their big moves are essential. As the current credit meltdown has highlighted this once again: for the bank CEOs, powerful board members with financial services expertise were the essential sparring partners.

Detailed examples and analysis of the five types of big move and the strategic antidotes to the ego-traps can be found in the authors' new book “Smart Big Moves: The story behind strategic breakthroughs” published in June 2008.

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