CHAPTER 1

Investment Leadership

Building a Winning Culture for Long-Term Success

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Over the long term, culture dominates.

—Charles Ellis, Greenwich Associates

Our previous book, *Investment Leadership: Building a Winning Culture for Long-Term Success*,[1] examined the elements of leadership that significantly contribute to the sustainable success of an investment firm. The concepts and research presented in that book set a context for this present book, which delves more deeply into the specific behaviors of top-performing teams. *Investment Leadership* was written in the aftermath of a 17-year bull market. During that time, it was relatively easy for an investment firm—any investment firm—to prosper. In fact, during a recent presentation to a group of Chartered Financial Analysts (CFAs) in New York, I flippantly remarked, "During the '90s, Forrest Gump could have managed a successful investment firm." One audience member, without missing a beat, responded, "He did!"

The prevailing attitude at that time seemed to be, "Give us some individuals with solid investment talent and we can win." (Or, to paraphrase the line from *Blazing Saddles*, "We don't need no stinking culture!") *Investment Leadership* chronicled the fortunes of a semifictitious firm called Allstar, which had grown to $40 billion in assets by the turn of the twenty-first century, only to fail completely three years later (and not, by the way, because of legal or talent problems). In our view, Allstar failed because of leadership and culture issues. To support this contention, it was important that we provide lots of data on leadership and culture—so we did.

In sharp contrast to the overconfident and somewhat naïve view of leadership during the 1990s ("Anyone can manage an investment firm"), we are finding now that leadership, culture, and teamwork are top priorities for investment firms. We no longer get quizzical looks and furrowed brows from CEOs asking, "Why would we worry about those soft issues?" Even the thickest-skinned, toughest-minded investment leader understands that the so-called soft skills are critical in attracting, retaining, and motivating talent. These leaders also know that optimal use of talent is the key to success in investment firms. (One Canadian CEO whose firm suffered from high turnover committed the ultimate Freudian slip when he said, "We do attack and retrain the best talent!")

The following is a quick review of the key concepts from *Investment Leadership*. If you have read our first book and do not want a review, skip this chapter and go directly to Chapter 2.

THE CULTURE THING

To begin with, what is *culture*? We use the following working definition:

> The beliefs, values, and behaviors that differentiate one organization from another.

Because leaders have the most influence over beliefs, values, and behaviors in a firm, they have the most influence over culture. Anyone who has recently changed investment firms can appreciate this difference. From the physical layout of the firm's offices, to the way decisions are made, to the beliefs about how markets work, firms differ. Gary Brinson used to compare investment cultures to world religions: Each may be valid in its own way or sphere, but they are very different from one another.[2] We agree that there are many ways to skin the investment-culture cat, but we have found some guiding principles that are common to the best firms.

First, though, let's examine some evidence that highlights the importance of leadership and culture in the industry. The following list shows the factors that contribute most to investment employee satisfaction and commitment. In the war for talent, this information is critical. The best firms attract, retain, and motivate top talent. How do they do it? Here are the key factors:[3]

1.	Leadership credibility and trust	84.8%
2.	Organizational culture and purpose	69.6
3.	Opportunity for growth and development	50.0
4.	Challenging, meaningful work	50.0
5.	Total compensation	50.0
6.	Relationships with co-workers, customers	39.1
7.	Work recognition	39.1
8.	Quality of life/work balance	28.3
9.	Ownership	24.4

Notice that leadership and culture are the top two factors. Our view of this data is based on three important connections that top investment firms establish and foster:

1. A connection of trust among leaders, professionals, and clients. When trust and respect exist in a culture, individuals make deeper connections with one another because fear is largely absent.
2. A connection with the firm's purpose. Top firms make it clear that they are driven by a purpose beyond making money. This higher purpose allows employees to connect with a mission that feels meaningful, such as "providing financial security for people" or "helping people realize their financial dreams." (Notice that in the preceding list, monetary compensation is important but not the top factor in creating employee satisfaction and commitment.)
3. A connection between the employee and his or her unique talents.

> Factors 3 and 4 in the preceding list relate to this connection. People feel and perform best when they exercise and develop their own special gifts.

In short, these three connections can be thought of as "above" (mission and higher purpose), "around" (with trusting relationships), and "inside" (with their own unique talents). Good leaders create cultures in which all three connections are developed and strengthened.

These basic concepts are necessary, but how does one think about culture in a practical way? What model is helpful in understanding how to measure and shape culture? We use the causative model shown in Figure 1.1 to understand the key elements.

In consulting work, we at the Focus Consulting Group start with results. This word is carefully chosen: not *vision* or *mission*, but *results*. Why? Because some firms may quibble over whether they even have a vision or mission or goal statement—but all firms, every day, produce results. The word *results* eliminates any hiding place. The question thus becomes, "Are you producing the results you want?" Therefore, we start by investigating what success looks like and how we would know if we achieved it. In short, what results are we aiming for?

In this process, we encourage leaders to be as inclusive as possible in creating a document that describes the firm's successful future state. The

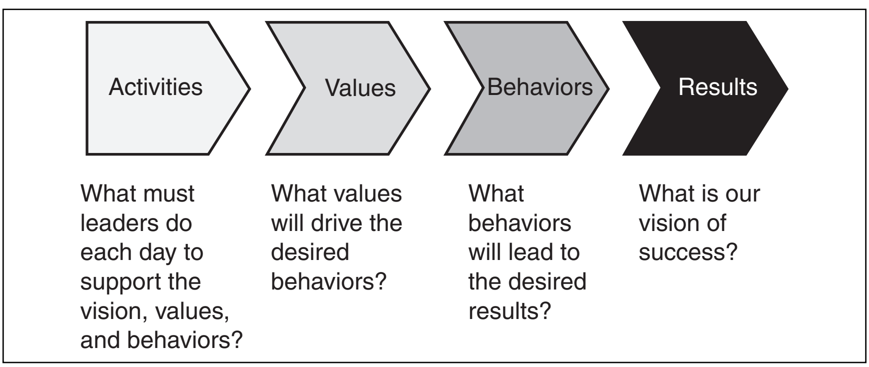

FIGURE 1.1 Causative model.

range of possible inclusion levels goes from the CEO crafting the document personally and telling everyone what it contains, to the leadership team starting with a blank sheet of paper and creating the document with the help and input of the entire staff. (Obviously, this is harder to do for UBS than for Analytic Investors.)

Backing up a step from results, we then discuss which behaviors will lead to the desired results, and which values will drive those behaviors. We provide a process by which investment firms can identify, define, and implement (*behavioralize*) values. For example, a company can create a list of measurable behaviors that are then used as a scorecard to track progress.

To summarize, the causal chain is that *beliefs* underlie *values*, which drive *behaviors*, which in turn create *results*.

In this context, what does the term *activity* mean? Underlying values, behaviors, and results is the need for leaders—and employees—to constantly reinforce key activities so that employees clearly see that "walking the talk" matters. When discussing these cultural issues with investment leaders, I always ask for an example of a top performer being dismissed because he or she didn't fit with the culture. From the top firms, I invariably get concrete examples of just that, usually along with an admission that those decisions are some of the toughest they ever have to make. Leaders at top firms are clear about vision, values, and behaviors and are relentless about reinforcing them by creating experiences that recognize and reward them. For example, American Century in Kansas City devotes an entire day to celebrating the five employees who best exemplify the company's five values.

With all this emphasis on vision and values, what other evidence exists (aside from the fact that employees like good leaders and strong cultures) proving that values and vision contribute to superior results? How do we link culture work to the bottom line? We offer the work of Collins and Porras in *Built to Last*[4] as strong evidence that firms that pay careful attention to culture outperform their competition over the long term. In fact, the 18 firms that Collins and Porras identified as superior companies outperformed the 18 comparison companies by a wide margin. For example, $1 invested in the superior companies during the period 1926–1990 grew to $6,356, versus $415 for the comparison companies. (For the record, the superior companies were not chosen based on stock appreciation, but rather on factors such as reputation and quality of products and services.)

With this huge difference in stock performance, though, it makes excellent sense to ask if there were consistent differences between the two groups of companies. Collins and Porras found 21 factors that explained the difference between "great" and "good." Six of the most telling factors involved leadership and culture. We have extended Collins's and Porras's work into the investment community and measured these same factors.

In what follows, we describe the six key factors and present the data for the original *Built to Last* superior (BTL) and comparison companies. We also include our own data from 35 well-known investment firms. The range of scores is from +1 to –1, with zero being a middle rating. In each case, BTL companies scored higher than the comparison companies. Investment firms (average of 35 well-known firms as self-rated by members of their leadership teams) tended to score in between these two groups. This makes intuitive sense, as the investment firm sample combined top companies, such as Capital Group, Goldman Sachs, and William Blair, with firms that fit the description of comparison companies (that is, average performers). In our experience, top investment firms score well on the following six factors.

CULTURE SUCCESS FACTOR 1: CLARITY OF VALUES AND VISION

> *The company has identified and articulated core values and a vision and uses them as a source of guidance* (see Table 1.1).

Top-performing companies worship at the altar of clarity. They have carefully identified and defined the results they want and the values, beliefs, and behaviors that will help them achieve those results. The very best firms make this process as inclusive as possible. They invite in all the key stakeholders so that each person's voice will be recognized. In this way, they build a high degree of ownership in the firm's vision and values. Investment professionals want to work with organizations that have strong cultures and purpose. A necessary ingredient in such a culture is

TABLE 1.1 Scores for "Clarity of Values and Vision"

BTL Companies	Comparison Companies	35 Investment Firms
.78	–.11	.42

conscious focus on and precision in the firm's values and vision. In the case of investment firms, part of that precision extends to the description of the investment process. The best firms have great clarity about the investment process itself and where each employee adds value.

The data in Table 1.1 shows that the average investment firm rated itself significantly behind the BTL companies. Note that the sample of 35 investment firms included stellar performers such as Capital Group, as well as companies that were, by their own admission, struggling. The message to take away is clear: There is great opportunity for most investment firms to improve their scores in this area.

There is good news here. Our experience in talking with leaders from around the globe reveals that the prevailing viewpoint as to culture is shifting. Increasingly, investment leaders are acknowledging the role of culture in performance. Leaders are beginning to understand the difference between working "in" the business (blocking and tackling on the field) and working "on" the business (going up to the skybox and observing). A relatively small investment of time (typically two days) at a carefully facilitated offsite meeting can translate into enormous competitive advantages. (We have yet to hear from a team after an offsite, "Sorry, but that just wasn't worth the time invested." Invariably, it's just the opposite: "We should have done this years ago!")

CULTURE SUCCESS FACTOR 2: CONSISTENCY OF VALUES AND VISION

> *The values and vision described have undergone little change since inception* (see Table 1.2).

So your firm has established values and a vision—good! The question then becomes: Have the vision and values been in place for a while, or do they change like the latest fashion fad? Consider two extreme cases.

TABLE 1.2 Scores for "Consistency of Values and Vision"

BTL Companies	Comparison Companies	35 Investment Firms
.67	–.89	.34

First is the building of the Sears Financial Network. Remember the so-called socks-and-stocks experiment? The leaders of Sears put forth a vision to build a financial network that would allow consumers to take care of all their financial needs under one roof; a financial supermarket, if you will. Almost a decade in the making during the 1980s, the whole enterprise had been dismantled by the early 1990s. Hence, a poor score for consistency of values and vision.

Consider the opposite example, just down the street from the Sears Tower. John Rogers started Ariel Capital Management in the mid-1980s with a laser-like focus on becoming the premier name in small and mid-cap value investing. Over the next 20 years, Rogers grew the company from a few hundred million under management to the $20-billion, top-rated firm that it is today. The firm's mascot is the tortoise and its motto is "Slow and steady wins the race." Everything in the firm proclaims "Focus!" Ariel is vivid testimony to the power of consistency and focus.

Our recommendation concerning the consistency factor is simple: Do it right the first time. Most visions and values shift because the process originally used to develop them was not thorough. If you take the process seriously and dig deep, you won't need to revisit the vision and values a year later to redo the process. The old carpenter's rule of "measure twice, cut once" applies here.

CULTURE SUCCESS FACTOR 3: ALIGNMENT WITH VALUES AND VISION

The vision and values are "alive" in the company (see Table 1.3).

Factor 3 could be called the "walk-the-talk" factor. Do the leaders and staff really embody the values and embrace the vision? We worked with a $60-billion, buy-side organization that had completed work on Factors 1 and 2. Values and vision were identified and printed on wall hangings and paperweights, and they had been in place for at least six years. The prob-

TABLE 1.3 Scores for "Alignment with Values and Vision"

BTL Companies	Comparison Companies	35 Investment Firms
.72	–.20	.22

lem came in walking the talk. We made it a practice, every day while we were on site, to ask several employees: "What are the guiding vision and core values of this firm?" Of the 280 employees, exactly one could answer the question with conviction and accuracy. She was the director of human resources, whom I later found out had crafted the statements.

Built to Last companies score very high on this factor. Employees know the core values and vision and reflect them in their actions. The average score for investment firms (.22) suggests that there are great opportunities for them to strengthen their cultures. There are several effective ways to do this. Leaders' reclarification of and recommitment to the vision and values can have a quick and powerful impact on the staff. Employees watch leaders like Fed watchers eye Alan Greenspan. Every single word and gesture is analyzed and critiqued. Smart leaders understand this human tendency and make sure that signals from the senior team are clear and aligned.

A second technique involves recognizing and rewarding staff who walk the talk. American Century's recognition day celebrates staff members who have shown exemplary behavior involving values. For example, each year one employee is nominated by colleagues for being the most innovative. He or she receives money and public recognition for this contribution.

Firms that have clearly identified their values and vision and are successfully walking the talk are well on their way to Success Factor 4, a strong culture.

CULTURE SUCCESS FACTOR 4: STRONG CULTURE

> *The firm's culture is well defined and "binary"; that is, some people love it and others hate it* (see Table 1.4).

Even the best of the best, the *Built to Last* companies, only muster a score of .44 on this factor. It's not easy to build a strong culture. Firms that

TABLE 1.4 Scores for "Strong Culture"

BTL Companies	Comparison Companies	35 Investment Firms
.44	–.33	.21

rate highly here are characterized by great pride in their products and services, elitism ("we're the best"), and a binary nature. *Binary* means that some people would love it and some would hate it. In the investment world, Vanguard is an excellent example. Founded by Jack Bogle, Vanguard has a strong nautical theme running through its culture. (The firm's name itself comes from the winning ship in a naval battle between Lord Nelson and Napoleon's forces; the French surrendered to the *HMS Vanguard* in 1798.) The buildings at the headquarters are named after sailing vessels. There are paintings of ships on the walls. The employees are called the "crew." The cafeteria is called the "galley." The bathrooms are the "head." If a crew member is missing, one almost expects to hear, "Man overboard!" The director of corporate communications once told me that his neighbors tease him about working for the "cult company." The comments neither surprise nor upset him. He acknowledges the cult-like nature of Vanguard, that is, its strong culture. He is proud of the firm.

What does one do to achieve strong culture? Factors 1 through 3 are critical and cannot be skipped over; no shortcuts there. Assuming that leaders are serious about establishing a strong culture, the critical step for Factor 4 is aligning hiring practices, incentives, and performance management processes with values and vision. Staff members must see evidence that employees are hired, promoted, recognized, and rewarded based on their conformity with the firm's cultural norms. ATB Financial in Calgary is so serious about hiring good "fits" that they actually have a page of recruiting material listing the characteristics of people who should *not* work for the company! Sheldon Dyck, ATB's investment leader, takes culture seriously and can offer up stories in which a top performer was dismissed from the firm because she or he wasn't a cultural fit. Nothing sends a clearer message to the troops that culture matters than the dismissal of a top producer. Firing a star player sends the message that leaders care not only about results, but also about how they are achieved.

CULTURE SUCCESS FACTOR 5: CULTURAL INDOCTRINATION

New hires are informed and educated about the culture of the company (see Table 1.5).

Built to Last firms far outscore comparison companies and the average investment firm in the area of indoctrination. Obviously, indoctrination can happen only in firms with fairly strong cultures. After all, how would you indoctrinate someone into an amorphous culture? There would be no clear guidelines or norms in such an environment. Hence, Factors 1 through 4 must be tended to before a firm can tackle this fifth step. Firms commonly make the error of ignoring this area, despite having done the hard work of creating a strong culture. Rather than carefully managing the process of training new hires, leaders often incorrectly assume that rookies will learn by osmosis.

Top investment firms do not take this chance. They establish formal and effective training programs that quickly get the new hires acculturated. A key consideration for any new hire is, "How do I succeed in this organization?" The orientation program should address this issue. What is expected from employees? What factors translate into promotions, pay increases, and bonuses? The same is true with new leaders. Top firms have a careful assimilation program for new leaders, which allows these individuals to get up and running quickly.

Ariel Capital takes the indoctrination process extremely seriously. Its "Ambassador" program concentrates on the new recruits' first 100 days. In that time, the new hires learn the firm's values, vision, product offerings, performance results, strategies, investment philosophies, and so on. At the end of 100 days, each new hire knows enough to be considered an "ambassador of the company." Capital Group also provides clear cultural guidelines. Its TAP program for new recruits is one such vehicle. David

TABLE 1.5 Scores for "Cultural Indoctrination"

BTL Companies	Comparison Companies	35 Investment Firms
.61	–.39	.17

Fisher at Capital Group believes that "culture is our only competitive advantage" and plans accordingly.

CULTURE SUCCESS FACTOR 6: SUCCESSION OF LEADERSHIP

> *The company has a history of careful succession planning and formal leadership grooming* (see Table 1.6).

Leadership drives culture, so the development of leaders is critical to building a winning culture. Even with a carefully planned and skillfully facilitated new-leader assimilation process, the sharpest, most willing learners still require months to get the feel of a new culture. Worse yet, many new leaders don't even try to understand what they've inherited. Rather, they resort to bringing in people from their old firms in an effort to reproduce that old culture. This move can work if the firms' cultures happen to be very similar, but most are not. The evidence is clear: Outside leaders are disastrous when they ignore the existing culture. Looking more broadly, research and statistics indicate that many mergers, acquisitions, and new regimes fail when inadequate attention is given to the viability of combining cultures.

Several years ago I watched as a buy-side investment firm brought in a new outside chief investment officer (CIO). For the next several years, the firm suffered relatively high turnover. Significant time and money were lost as people tried to figure out the new way of doing things. Key players eventually became frustrated and left. After a few years, the firm finally stabilized at a mediocre level of performance. Then, amazingly enough, the whole cycle recurred when the CIO was tapped for another

TABLE 1.6 Scores for "Succession of Leadership"

BTL Companies	Comparison Companies	35 Investment Firms
.33	–.39	–.06

assignment in the parent company! Although he had had six years to find his successor, the CIO had not groomed a replacement, so, once again, the firm brought in yet another new CIO from the outside. The same turmoil ensued, but to an even greater extent. The most notable example of the talent drain occurred when a derivatives trader left two weeks before the end of the year. All his colleagues reminded him that if he could just "gut it out" until December 31, he would be entitled to a sizeable bonus. His response? "It's not worth it." And he left, with his bonus still on the table. Basically, he walked away from a Mercedes because the environment was so bad that he couldn't take it one more day.

Most investment firms traditionally have followed the tribal method of leadership. Each tribe—fixed income, equities, real estate, privates, etc.—establishes its own rituals and ways of doing things. Then, as if at a secret midnight ceremony, these rituals are passed down to the next generation, along with secret handshakes. Today's top-performing firms, however, are beginning to look at a more formal approach to succession. With culture in mind, we recommend designing leadership development programs based on the unique vision, values, strategies, and investment philosophy of the particular company. We have helped firms develop leadership programs that include "soft" skills such as:

- Managing difficult employees (i.e., "stars").
- Interviewing and hiring for both skills and culture fit.
- Handling performance management, especially delivering tough reviews effectively.
- Resolving conflicts, including techniques for clearing the air on a regular basis.
- Giving and receiving feedback, on a regular basis, skillfully, with both candor and tact.
- Embodying accountability and integrity (defining and operationalizing these key concepts).
- Coaching and mentoring (developing and assessing the rising talent in a firm).
- Building trust (recognizing that success rests on the "three legs of trust: congruence, competence, and caring"[5]).

- Fostering teamwork (defining roles, responsibilities, and critical guidelines).
- Demonstrating emotional intelligence (developing self-awareness and relationship skills).

The last skill, emotional intelligence, was made famous by Daniel Goleman in his book of the same title.[6] This skill has been identified by reputable organizations (including the Center for Creative Leadership) as the key leadership skill yielding success, even ahead of IQ or experience. Obviously it's critically important . . . but what is it? Emotional intelligence has four basic elements:

1. The ability to identify one's feelings and behaviors (self-awareness).
2. The ability to manage one's internal state (self-control).
3. The ability to recognize and understand others' emotional states (empathy).
4. The ability to manage skillfully one's relationships with others (rapport).

CULTURE FOR COMPETITIVE ADVANTAGE

To recap, the six culture factors discussed in this chapter are powerful and effective steps that the best investment firms have taken to secure a competitive advantage. As David Fisher noted, and other leaders of top firms agree, "Culture is our only competitive advantage."[7]

The formula is simple, but not easy to implement. For one thing, success requires a deep commitment at all levels of an organization. For this reason, Focus Consulting Group uses a "Readiness Survey" with firms that are considering a culture change. Typically we discuss leadership and culture with the key opinion leaders and then distribute a survey that asks questions such as:

- Does the process make sense to you?
- Do the facilitators seem capable?
- Is the level of urgency in your organization high enough?
- Are trust levels sufficient to make real progress?

- Is senior leadership committed to the change process?
- Is senior leadership capable of leading us through the change?

If the responses to these questions are lukewarm, typically the level of commitment from participants will also be lukewarm. In these cases, we recommend postponing the process and dealing with the obstacles.

PRACTICAL APPLICATIONS

For the more “hands-on”-oriented readers, let me give a few illustrations of how the Focus Consulting Group has applied these concepts with clients.

A large, East Coast money manager with a very strong performance record is planning to double the assets it has under management in the next three years. The senior management team’s concern is keeping the company’s successful culture *pure*. They obviously don’t want to wreck their winning formula. They asked us to analyze their current organization and design training on how to hire an excellent fit for their culture. This work involved clarifying the outstanding features of the firm’s current culture and developing an interview process that specifically incorporated these features into questions for candidates. The outcome of this customized, tighter interview process is objective rankings as to how well each candidate will fit with the existing culture.

Another practical application of leadership and culture work is designing a customized leadership development program. Recognizing that they were heavily dependent on the tribal approach to leadership development, one firm that Focus Consulting Group works with asked us to design a more formal program that would fit with its current environment. The process again started with analyzing the company’s culture, defining it, and leveraging the talents and strengths of leaders who were currently excelling in that environment. The practical outcome of this assignment was a definition of what it means to be an effective leader at that particular firm. Formal training and executive coaching (including 360-degree feedback) were used to drive home the desired attitudes and behaviors.

The result was a good fit between leadership and culture. Leaders reinforce the appropriate beliefs, values, and behaviors. When done skillfully, this process also addresses the succession issue, as internal leaders are prepared to take over when senior people leave. Both the evidence and our experience clearly support the case for home-grown leadership.

A third application addresses mergers and acquisitions. A large global investment firm asked us to help define and integrate the cultures of four different firms that it had acquired. This process involved facilitating a discussion between key opinion leaders of the newly formed entity and gaining agreement on the new vision and values. The acquirer's strategy and desire was to capture the best practices of each separate firm and leverage them for use by the new entity. A different strategy, employed by parent companies such as AMG, Old Mutual, and Convergent Capital, is to acquire asset management firms and leave the existing cultures intact. A blend of the two strategies is employed by NatCan in Montreal, where three distinct asset management groups have defined their own separate cultures but collectively agree on "meta-values" at the parent-company level.

CONCLUSION

Leadership drives culture, which in turn drives investment performance. Building a strong culture requires leaders to work "on" the business, as opposed to their normal task of working "in" the business. Leaders must step away long enough to deeply consider and identify a clear vision and strong values. They must then walk the talk and reward staff members who do the same.

Our research shows that a huge opportunity exists for investment firms to differentiate themselves from the pack by strengthening their cultures. Specific areas on which to focus are:

- Clearly define vision and values.
- Communicate the vision and values and reward behaviors that reflect and promote them.
- Hire for cultural fit.
- Indoctrinate new hires and new leaders carefully and thoroughly.

- Promote and compensate using a cultural-factors approach.
- Develop strong leaders from within the firm via formal training and coaching.

The aim of *High Performing Investment Teams* is to describe and teach the seven key behaviors that we find in top firms. These behaviors are woven into the fabric of a top firm's culture and day-to-day activities. From the newly hired receptionist to the CEO of 10 years' standing, each professional at the firm understands and lives these behaviors, because each employee understands why these behaviors are important to the long-term success of the firm.