CHAPTER 1

Developing Good Leadership

Long before I was a psychiatrist, I was a basketball fan, and throughout my adult years I have followed the careers of great players and great coaches. One person I have admired from afar is John Wooden, the legendary coach known as "The Wizard of Westwood," who earned his nickname by accumulating an extraordinary track record: 10 NCAA titles in 12 seasons before he retired in 1975.

While it is true that Wooden recruited and coached remarkable players, his modest demeanor and his ability to manage such outsized personalities as Kareem Abdul Jabaar and Bill Walton contributed much to his legendary status. Today, his famed Pyramid of Leadership, which includes 15 building blocks to success, is posted not just in locker rooms, but in offices and boardrooms as well.[1]

At the foundation of Wooden's pyramid are personal character traits—industriousness, friendship, loyalty, cooperation, and enthusiasm. At the top sits "competitive greatness" which Wooden defined as being "at your best when your best is needed."[2] In between, he constructed layers of personal qualities such as self-control, skill, "intentness," poise, confidence, and team spirit.

Coach Wooden's vision of success and the steps he outlined in his Pyramid to achieve it are as valid for the workplace as for the basketball court. A great coach, like any great leader, teaches those who join him how to play to their strengths, how to stay on target, and how to tune out the distractions and the emotionality of the game. In this sense, what is called *executive coaching* is similar to what a good sports coach does. Wooden's example, as well as my personal experiences with Olympians and top hedge fund masters, has demonstrated that it is possible to help people to tap their hidden leadership potential and thereby maximize their own performance and the performance of others. This interest in helping people become leaders in their own lives and achieve greater personal freedom and self-expression by overcoming their self-doubts, inhibitions, and fears, is a very intense paradigm for leadership that has led me to write this book.

A UNIQUE PERSPECTIVE

In my previous books on the psychology of trading, I emphasized the importance of going beyond self-limiting notions about yourself and public commitment to goals, risk taking, centering, and turning breakdowns into breakthroughs.

In this book, I focus more on the empowerment of others. How do you lead a team? How do you get to your objectives with the help of others? How do you get collaboration from other people? How do you get the best out of them? How do you do it in a way that engages them without dominating them? In this book, I want to focus on how you can not only empower yourself but also empower others with these principles—in essence, how you can become a successful leader.

THE VALUE OF EMPOWERMENT

Leadership in the hedge fund world is not all about numbers anymore. It's about people. But, of course, that presumption alone leads to numerous questions. How do you get people to go to bat for you? How do you get people to make that extra bit of effort? How do you empower your team to get the job done?

Successful leaders have found that empowerment results from finding a leverage point from which they can encourage others to see the necessity of trying something new. Good leaders help others to develop a willingness to change behavior and take risks. They develop the skill to reach the emotional wellsprings of belief, motivation, courage, and perseverance, which help contribute to trading success for themselves and others.

Peter represents a new breed of hedge fund managers who have begun to understand these concepts. With 10 years of experience under his belt, he recognizes the importance of leadership skills in preparing for the next phase in the evolution of hedge funds.

Peter also recognizes the importance of defining a vision or goal for the team, but then looking for the cutting edge and asking what more can be done to help reach the goal. He considers what incentives will motivate change, how he can reframe the team's objectives so as to overcome inertia, and considers longstanding patterns of complacency and caution.

Case Study on Leadership Issues in Hedge Funds

A successful leader doesn't shun resistance. In fact, he anticipates it and prepares to challenge the resistant team members in a compassionate way. He helps them to keep focusing on the goal, while creating a safe space that allows them to experience failure. He understands struggles and listens to what others are saying—directly and indirectly.

These and a number of other insightful issues are more fully elaborated upon in the following verbatim dialogue with Peter, the principal at one of the more successful funds on Wall Street. His 10 years in the business provide him with a number of comparative experiences and insights into the nature of leadership issues in hedge funds.

Kiev: What does it take to succeed as leader of a hedge fund? What are the tasks and what are the skills you need?

Peter: It starts out as portfolio management, but at least from our perspective it's much more about people management and HR. The people who are building good hedge fund businesses are doing a better job of paying attention to people, HR recruiting, and screening people. They try to set a direction and vision for the firm so that when somebody joins such a firm, they know exactly what the next three to five years look like. If you look at the model from the late nineties, it was the sole proprietor. From the perspective of an employee joining them, they were only trying to figure out how much capital they could deploy and how much they could get paid for it, and that was really about it. The process of business building wasn't collaborative.

Kiev: How is it different now?

Peter: People who I think are being successful today are looking to not only financial risk, but also business risk. They are interested in protecting, preserving, and growing their franchise. They are choosing multiple products. They care about the brand name and they care about retaining talent. You may not make as much money as the old-time CEOs in any one year, but over five years or ten years you are going to make a lot more. I think people are reinvesting rather than just taking the money out of the business and stuffing it under a mattress. Today, people are making real reinvestments in hiring and training a bunch of junior people, opening offices in London or in Asia, and expanding the business that way. They bring in professional business managers, professional HR people, and leadership consultants. So people are making discretionary investments that you normally find in other businesses. I think the difference between a good leader in a hedge fund business and a bad one is that they are thinking about it as a business in much the same way that we expect our portfolios to think about it. We have free cash flow. Do we reinvest that in the business? What's the return that we can get from there? Do we give it out to ourselves or do we do a share repurchase?

Kiev: This sounds like a real paradigm shift.

Peter: In the past, CEOs could just keep the money, or they would pay it out to people who kept the money for themselves. The best funds today have invested phenomenal amounts of money, people, systems, marketing, and product design in advance of launching new products. If you have the right team in place today, you are doing things that are small and reasonable, and making normal returns when it comes time, so that you have excess returns and still have the capabilities in place.

Kiev: What happened that led to this paradigm shift or awareness of looking at hedge funds as businesses? Is it that they existed long enough for people to realize they had some longevity and that some of these other considerations weren't what they thought?

Peter: I think that is part of it, along with the fact that the industry has grown so large and that there are so many multibillion dollar hedge fund managers. If you are a professional CEO, COO, or HR person, you tend to look at what their growing industry is. I think the business is growing so much that it attracts professional management.

The second thing is that it's attracted interest in capital among third-party investors. So we have seen insurance companies take stakes in hedge funds. We actually have seen hedge funds sold. We have seen a lot of third-party interest in the investment at multiples of earnings. There are leaders and there are fast followers. Portfolio-wise, hedge funds are very good fast followers, and also in the business sense. They saw somebody not only maximize the short-term profit, but make seven to ten times that amount by selling a stake in their business. And putting a seven to ten multiple on it, that really changes things. Where you had businesses, which were sole proprietorships, there are some people who manage money, and they have all been into institutional business over time.

Kiev: Can you discuss other keys to success in hedge fund leadership?

Peter: To a certain extent, it's the growth and popularity of attracting a professional management. Since you have a larger population of people that are of critical mass, there are just the odds of you getting good business models out of fifty to a hundred companies. Those odds are better than the odds of getting them out of four. If you look at good hedge fund managers today, you know there is something about a thirty- or forty-year-old CEO that thinks with a twenty-year time frame investment future versus people who are at the twilight of their careers. A smart younger guy is thinking about not only that year's profit, but how can he build something for the next ten, fifteen, or twenty years? He has a lot more gas left in the tank than many of the earlier guys.

Kiev: Did you see some transitional leaders that were learning to be CEOs without necessarily bringing in outside managers? There is a learning curve, if you are aware of it.

Peter: Yes. You can either bring in a swing coach to teach you how to get the golf club or you can try it yourself or some combination therein. The fact is, that the best are built around portfolio managers who trust their own decision-making power better than they trust others. You are getting much more on-the-job-training. There is more bringing in of coaches than handing over the reins of the business to a professional manager with the idea of, "You run the register and I will just be the chef." Because of the wealth of the CEOs of hedge funds, they can afford to do it. They are used to making decisions and they trust their own analytical abilities. I am thinking of one guy who went from working at a top investment bank, to block trading, to being a portfolio manager, and then to being a business builder. He didn't bring anybody to help him do that. I think he just learned on the job. Another leader surrounded himself with bright business people, good legal advice, good operations, and counsel to provide input and alternatives to him. When he finally makes the decision as to which direction to go, he trusts his own instincts.

Kiev: How self-aware does a great leader need to be?

Peter: Some people have the ability to look in the mirror and see their own weakness and compensate for them, while other people look in the fun house mirror and see themselves differently. I think that

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> is true both in the portfolio sense and business sense. The ones who will succeed—and hopefully, we will be one of those—will have a good idea of what we are lacking and hopefully go out and get help.

Peter represents the new breed of hedge fund manager who recognizes the importance of leadership skills in preparing his fund for the next phase in the evolution of hedge funds. He has formulated both a short-term and long-term vision and has the desire and willingness to impart it to his people, while recognizing that the learning curve is steeper for some than for others. He also recognizes the unique features of hedge funds when compared to other business organizations. Many of the most successful funds are run like small family businesses, even though they are managing billions of dollars and generating hundreds of millions of dollars of profits. In fact, the hedge fund manager is often a unique combination of both player and coach and in many instances the principal owner, trader, and moneymaker in the organization, which makes for certain special psychological challenges in managing such organizations.

CASE STUDY ON THE PLAYER-COACH CONCEPT

Because of the importance of this distinction, I explored the theme of the player-coach with Dean, a portfolio manager whose work experience included time as a consultant for a major management consulting firm. His remarks help clarify the critical variables differentiating hedge funds from other business organizations.

Kiev: What's unique about the leadership of hedge funds?

Dean: Hedge funds are unique in that the leader is often still a player. It's not like professional baseball where the coach is more often than not someone who played baseball twenty-five or thirty years ago. Joe Torre is not batting in the lineup. He can't get in that box to take swings. His credibility is based on his track record as a coach, not his record as a player.

Kiev: What's the significance of this?

Dean: Hedge fund managers can lose credibility as managers if their stats aren't the best. This may be why some managers have decided to stop running money so that they could concentrate on managing the firm. Others have brought in new people to manage the firm.

Kiev: How do these models differ?

Dean: Hard to say. A guy like Torre in baseball or Pat Riley in basketball has years of being a coach that he can draw upon. His playing stats are a long time ago. The issue is different if you are a player-coach, which is how it is in the vast majority of hedge funds and what creates the most difficulty. There are a lot of hedge fund managers who are trying to coach people while they are still trading alongside them.

Kiev: Can you go into more detail about those who have trouble as a coach when their stats aren't great?

Dean: Your stats have to be great for you to continue to be a player-coach. Otherwise you risk rejection. Take basketball. It's hard to be a player because if you are sitting and telling the young guys to do this and do that, they are likely to say, "Wait a minute, old man. You can't even get up and down the court anymore." Your answer is credible if you are able to say, "Yeah, but I am a coach. I am not playing anymore. I am not doing what you're doing." I read about one successful fund manager who basically said, "I am just surrounding myself with really smart guys. I am not doing this anymore." It's clear who the leader is.

Kiev: Do you think a guy whose numbers aren't that good would be wise to do what this manager is doing?

Dean: I think so. You are starting to see guys who are mediocre step back and say, "I am going to get other guys to run this and just leverage my brand name." Then they try to build the organization and try to do those other things.

Kiev: What are the leadership tasks involved in running a hedge fund?

Dean: You need to be very clear on what you are looking for. You say, "Okay, this is the amount of money we're looking for. This is the kind of volatility that we are looking for." You need to be explicit about your expectations and the minimum requirements for keeping a position so as to reduce the degrees of uncertainty, which exists in so many firms. One of the strengths of our shop is that basically everyone knows how much he or she is getting paid, based on a formula. In this way, you don't have a big conversation at the end of the year. More and more organizations are moving in this direction, although there are still many where you don't know where you stand until the end of the year. A lot of places they don't until the end of the year.

Kiev: Have you observed hedge fund leaders who understand the psychological issues, the sensitivity of others? Do they see how they might get in their own way in reaching their objectives? Does a leader need to improve his ability to listen to his people to communicate more clearly with them? To provide feedback to them on how they are doing?

Dean: Difficult to say. It's such a dollar-and-cents business. If you look at typical corporations, many of them do that kind of three-sixty evaluation, where everyone evaluates everyone else and there is an effort to improve communication around these softer issues. Most hedge funds don't do that sort of thing, but I would say that some of the more forward-looking firms are starting to pay more attention to these kinds of issues.

Kiev: Is it a good idea to think about doing such things, at least paying attention to the quality of communication, and whether or not you are tapping into the hidden potential of the people in your organization?

Dean: Absolutely, but it will take time because ultimately it's about the dollars and the cents, and if this adds value, it will be incorporated.

Kiev: Is this starting to happen?

Dean: Yes. I can see it. It involves a real difficult cultural change in this business. What you are talking about is the process of institutionalization, where it's not just about your whole net worth, or your whole experience isn't based on how much you get paid.

Kiev: Even if your net worth is based on how many dollars you make, are you going to make more dollars if you are nurtured a bit more?

Dean: What you are saying makes sense. You need a real commitment. When old-line hedge fund managers are running a book, I don't think they view themselves as mentors. They don't view themselves as a coach per se because they are worried the guy is going to leave them. But the new breed of hedge fund managers is definitely thinking this way. They recognize that if the environment is right, people aren't likely to leave, and while it may be too much of a burden for a lot of fund managers to take on, they are finding ways to institute these processes.

Kiev: It's not all about numbers; it's about people. How do you get people to go to bat for you? How do you get people to make that extra bit of effort? You need to relinquish some of the control. You can't look at all the companies. You've got to teach somebody how to do it. Maybe if a guy learns how to do it, he is going to leave you, but at least while he is with you, he will have done it in the most effective way possible. I am suggesting that there is value in bringing this soft side out in the open and trying to figure out how to empower people in the best way possible in order to get to the top of Everest.

Dean: The challenge in doing this is an issue of time and resource allocation from the leader's perspective.

Kiev: OK. So how do the best funds handle this? How do they maintain a consistent level of performance year in and year out? How do they boost the level of ordinary performance? What do they do about recruiting top talent? What do you think of such key principles for maximizing performance as focusing on a larger vision, looking for the cutting edge, challenging resistance in a compassionate way and creating a safe space in which the greatest mistake is not making an effort?

Dean: These principles sound fine in theory, but in actual practice at the best hedge funds, the focus is generally on performance and not so much on creating a safe space. It is results oriented and most big funds are only recently beginning to embrace the supportive approach you are talking about.

Kiev: So you agree with my viewpoint, but only insofar as the focus is on goals and helping people to reach them.

Dean: I like to compare the best funds to the New York Yankees.

Kiev: How so?

Dean: The New York Yankees have done very well with home-grown guys that came through the Yankee organization—Pettitte, Rivera, Posada, for example. They won a lot of championships with those guys. Not that they were the best players. Jeter is not the best player at shortstop. But it's ingrained in them what the environment is like. You then get a guy who is a very talented guy outside the organization to come into the Yankees, let's say. They just don't do as well. I think it's the makeup. They don't understand the culture. They don't understand the expectations coming in. You can make the argument about some of our guys who came through our hedge fund organization and know what it's like.

Kiev: Do you think the organization articulates what the culture is?

Dean: The culture doesn't know and sometimes it's a negative. When Steinbrenner is bringing a new guy in, he is not going to tell him what to expect. When you're losing, he may go in the public arena and say you stink. If you read the paper, you kind of figure out that's the way the guy is. Now I came in to this fund and I had known some of the guys for a fairly long time. I clearly knew what it was like to come in to the situation. It's basically been what I expected. So that's why I think I have survived. I think you do better when you know what to expect.

Kiev: You weren't disappointed?

Dean: My expectation was based on what this organization's leaders told me.

Kiev: Would newcomers do better if they understood the environment? If everyone owned up to what it's really like, if you could really see it? You know this place isn't for everyone. This is for guys who have thick skins. These are the guys who want to go for the gold and [are] willing to go through hardship and starvation and loss of limbs. You are signing up for the Marines.

Dean: I think most people know that it's a tough environment. I think most people know the reality.

Kiev: I think that's good. You want the expectations to match the reality.

Dean: If you want to play for George, what's the big deal? I have come in with that mindset since Day One. This is the Yankees. I might be a superstar to someone else but when I come in here, I have got to play a superstar game if I am to be considered one. If I go to other places, guys might think I might walk on water. Here I have to face the reality of my performance if I am not up every day.

Kiev: Is that maturity?

Dean: I think it's somewhat maturity.

Kiev: Are you saying that with a Yankee-type hedge fund, you don't need approval and are willing to be judged by your performance?

Dean: I know what the deal is. I know the expectations.

Kiev: Jack Welch talks about the value of candor and being willing to speak the truth and being willing to follow things straight.

Dean: My thing is, we should embrace the Yankee image if this is the way it works.

Kiev: Does that mean this firm is not made for everybody?

Dean: I think we say that, but we are always trying to grow the firm and recruit people who eventually won't make it or who will have trouble doing so. I came here because I wanted to be like the portfolio manager who started at zero and now he is worth a hundred million bucks. It would take me twenty years on the Street. If I can do that in two or three years, that's why I'm here. That's the difference. I still can go somewhere else. It's always in your mind. You always want to make sure you are not cheating yourself, making excuses for the people around you, just to justify being here. That's not the case. This is like the Yankees. The Boss gets impatient every now and then, but that's fine.

Kiev: Because you want to play for the best teacher, the best leader, right?

Dean: In baseball, there is one standard and it's the Yankees. Right now our fund manager and this firm are the standards. You almost have to embrace it unless they want to change it.

Dean: Look at the Yankee turnover. The Yankees turn over and we had like four or five guys that are the same. The idea here is you become one of my core guys. Jeter is a core guy. Posada is a core guy. Four guys on this team won the championship game, like seven years ago. Just like at this firm.

Kiev: What happens when a core guy leaves? Can his performance standard remain so high?

Dean: Most guys would do as you would expect. It's pretty good and it's not taking a ton of risk.

Kiev: Do you think they have learned enough?

Dean: I think they have learned enough.

Kiev: Do you think they have learned what this firm is doing or they have discovered the confidence in themselves?

Kiev: So, they do well, knowing that they know it's doable.

Dean: I think it's the confidence.

Kiev: I always thought the place was entrepreneurial.

Dean: In fact, it could help get rid of people. Say look, they couldn't cut it with the Yankees. There is no shame in not being able to play with the Yankees. There are lots of other teams you can play for. The more we run away from that, the less genuine we are, I think. We pay top dollar for talent. That should be the standard. If you run a hundred and you are down in a few months we're not going to be happy. I think we should embrace that.

The discussion with Dean underscores the need for the leader to balance his own objectives with his need to manage the team. The more he learns how to manage other people and to leverage his knowledge through them, the bigger the organization can be. If he thinks he is the only one who can do it, then he is never going to build a team. So the challenge of leadership is to build a team and then leverage it by setting larger targets and motivating people to get past their own fears. To do this, the leader has to get past his own fears and anxieties about helping other people, which is not always as easy as it may seem. Those are the kinds of things that are inherent in leadership.

IT BEGINS WITH YOU

To activate authentic leadership, you must put yourself on the line to resolve personal issues and take the first steps toward personal mastery. When you are more present-centered and psychologically at risk, you will be an ideal medium for growth.

The key to developing mastery *and* leadership is a willingness to be open and to share your experiences, both good and bad. Of course, this requires that you first overcome a variety of limiting beliefs and stopping points that serve as obstacles to becoming an autonomous, emotionally connected decision-maker. This begins with a considerable amount of self-examination. Ultimately, self-examination becomes the paradigm for transformative leadership in which you can become even more powerful and effective in your own trading life and in your impact on supporting others in the process as well.

As you learn how to act independently of your own blocks and fears, you can begin to see how you can lead your teams toward greater performance. To the extent that you can reveal your own vulnerability and sense of uncertainty, you will develop greater mastery and become an invaluable leader to your team.

In effect, the willingness to talk openly about your personal trading issues will enable you and your team members to get past the need to appear stronger and more confident than you really feel inside. As you expose your weaknesses and frailties, ambitions and dreams, and get past the need to maintain a facade of competence, you will become amazingly alive and empowered by the process and discover a tremendous amount of support that exists for you and others in this shared experience.

This type of communication doesn't happen by accident, especially in the harried world of trading. A good leader will have to make communication a priority and work to establish opportunities for the team to develop communicative skills. Whether it be a regular weekly consultation or an intensive several-hour consultative seminar, I encourage you to set aside a specific time to examine a variety of issues with your trading team. As you and your team openly discuss them, you will rapidly get at the heart of some of the issues that keep people from being as effective as they can be as traders and leaders. Begin by addressing the following items:

- The most common psychological problems: lack of specific goals, an inability to cut losses, panic, fear of success, fear of losing, euphoria, gambling impulses, perfectionism, and so on
- Problematic trading patterns: not trading big enough, not holding long enough, holding too long, excessive caution, inflexibility, paralysis by analysis, excessive risk-taking
- Examples of trading strategy in regard to sizing, conviction level, price targets, and P and L goals
- Examples of investment ideas vis-à-vis specific companies in regard to bullish and bearish case, catalysts, risk and reward parameters, and

variant perception (what was known at the time of the investment that no one else knew, which gave them a trading edge)
- Examples of best and worst trades
- Summary sheets of trading statistics, if available, in regard to P and L, amount of capital being used, percentage of winning days, ratio of average amounts of money made on winning days to average amounts of money lost on losing days, and any other statistics that might be illustrative of trading patterns
- Thoughts about trading objectives
- Examples of experiences in dealing with analysts, risk management, and management—including communication issues, command and control issues in the organization and the like so as to empower the team by initiating openness and the sharing of vulnerabilities
- Receptivity to coaching—how much the team can admit to vulnerability and the need for support
- Spreadsheets illustrating the sizing of positions, hedging strategies, and level of conviction of ideas

The more you bring to the table, the bigger the impact the meeting will have on you and your team and the more you will accomplish during the session. If you really put yourself out there, by exposing some of your own performances as well as the performances of the people on your team, and if you are willing to explore the good and the bad, what works, and what doesn't work, for yourself as well as your team members, then you will walk away with a huge win by your understanding of behavioral and attitudinal changes in yourself and others.

This open dialogue will translate into profit potential in your own trading and that of your team. Perhaps most important, such a dialogue invites the opportunity to break through and develop team connections. There is suddenly an opportunity for everyone to see that leadership is not about demanding something from people, but about providing a setting in which everyone can voice concerns, fears, self-doubts, differences, and even disagreements without fear of retribution.

Group discussions encourage people to see the nature of sharing, help overcome the natural reluctance of others to speak out, and challenge the status quo. As team members learn to share their dreams and identify everyday obstacles in the life of the organization, what often emerges is an amazing interaction that was not previously present because of fear, or lack of time, or opportunity. Such discussions will help foster a sense of teamwork, loyalty, and motivation as well as motivate better performances and a more competitive edge.

ENJOYING THE PROCESS, SOLVING THE PROBLEMS

Of course, the point of good leadership is not just to get the team engaged in a dialogue, it is to move the team toward the resolution of problematic issues—especially those issues that prevent the production of out-sized results. By talking about such specifics as trading targets, goals, sizing positions commensurate with the targets, and so on, you can translate the lessons of the dialogue immediately and directly into trading profits and thus quickly see how to accomplish breakthroughs that reinforce goal-oriented achievements.

As you work with your diverse group of team members and recognize their diverse responses, often to the very same or very similar experiences, you will begin to understand that each person will get something very powerful and unique from the communicative exchange with others and from the opportunity to reveal certain truths and recollections about his own experiences. This kind of experiential learning is not formulaic but rather stimulatory, creating a context in which people can take as much or as little as they are willing to absorb at a particular time. Still, the results can be very powerful.

For example, after one group dialogue in which a variety of concerns were addressed, one trader zoned in on the discussion about sizing his high-conviction ideas bigger. After hearing that only 3 percent of his trades accounted for much of his profitability, he spent several weeks reviewing his 250 positions and seeing where his sizing needed to be bumped up consistent with his level of conviction and profit targets. This trader also saw the benefit of reviewing his data from a statistical perspective to unearth various trading patterns that pointed to strengths and weaknesses—including the time frame in which he made the most money and where he needed to get out of positions when the trade had matured to its maximum point (rather than holding on and seeing his profits dwindle).

Another trader found that the same dialogue had confirmed some of his perspectives. He recognized that he was not trading to win as much as he was trading not to lose so as not to disappoint his demanding investors. He began to understand that he had been adjusting his position sizes to reflect his level of conviction. While he had been thinking about some of these things before, the discussion offered confirmation that led to a boost of confidence about his methodology.

Another group of traders found an appropriate and forgiving atmosphere in which to launch a variety of concerns about risk management—such as when to cut losses, the importance of having real and unemotional reasons for putting trades on, how to develop an algorithm for getting bigger as they developed higher conviction, and how to leverage ideas from the analysts so as to build their investment thesis, understand catalysts, and create a variant perception. So, the interaction helped everyone feel freer to reveal their problems without embarrassment and to discuss issues that are often ignored in "polite" company.

The more you learn about your team, the more you, as a leader, will be able to help your team to improve their processes, to maximize their creative input and to give them a greater sense of ownership. When an open dialogue is created, there will be an increased awareness of millisecond responses associated with hesitation about pursuing objectives. Leaders and team members will become more adept at discerning quick, subtle, nonverbal emotional communication and other clues that can help traders push themselves even further than they imagined. Along the way, you will gain a glimpse of a new future—a future in which team members can make more decisions on their own and have a greater role in their own destiny.

Understand that communication in and of itself is not necessarily the answer to all of your leadership dilemmas. It is the process of communication, inviting traders to join an interactive dialogue, that helps everyone face the often unpleasant task of owning and overcoming anxiety. One particular meeting won't necessarily solve all the problems that you are facing. But such meetings will help construct a methodology of inquiry about what is needed to develop leadership and to empower the people on your team.

Of course, the type of communication I am describing involves participation as opposed to top-down edicts from the leader. The best leaders are able to help others call on their strengths and move the organization along, not by fiat, but by engaging everyone's interest and enthusiasm.

BREEDING GOOD LEADERSHIP

Warren Bennis, one of the most respected writers on business leadership wrote, "Around the globe, we currently face three extraordinary threats: the threat of annihilation as a result of nuclear accident or war, the threat of a worldwide plague or ecological catastrophe, and a deepening leadership crisis in organizations."[3]

Does it surprise you to hear such a respected author lump a "leadership crisis" right among the threat of nuclear war or some sort of endemic plague? Most of us would not consider the three to be equally intimidating. Yet, on a broader scope they probably should be. Our world seems to be groveling for good leaders. Men and women in leadership seem unsure of themselves at best and totally incompetent at worst. The hedge fund world is no exception.

But it doesn't have to be this way. There is no shortage of talent, and leadership is a skill that can be learned. In fact, leadership will thrive if the environment is suitable, and thankfully, many hedge funds are beginning to understand what conditions are necessary to breed successful leaders.

Bennis and his co-author, Burt Nanus, note in their book *Leaders* that the best leaders "are able to concentrate on what matters most to the organization and to use the organization as a learning environment."[4]

They develop skills, says Bennis, that allow them to acknowledge and share uncertainty with colleagues in task force settings. They use their mistakes as "learning experiences . . . they engage in goal-setting exercises to force reexamination of current assumptions and priorities; they use their interpersonal skills to encourage others to join in the search for new ideas . . . they constantly enhance their understanding of their own limits and biases by testing their views against those of knowledgeable colleagues and outside experts."

Hedge funds that embrace this type of management become more adaptable and exemplify the best features of what MIT professor and author Senge has called the learning organization. This type of open meritocracy is far superior to the traditional command-and-control hierarchical style of leadership that has always been prevalent in the financial field and breeds better leadership as well as greater stability and the opportunity for more sustained success.

Case Study: The Distinctive Organization of Hedge Funds

To better understand some of these distinctions I talked with the head of the quant division at one of the premier hedge funds on Wall Street about his views of leadership and how they differed from his prior experience at one of the larger investment banks. I think Todd's views are useful in defining some of the ideal characteristics of the best hedge fund leaders and in emphasizing the importance of trust and autonomy and the creation of a safe space where creative people can innovate without fear of retaliation for making mistakes.

Kiev: Based on your experience working in a number of different kinds of financial organizations, what would you say is the key to your leadership success in a hedge fund?

Todd: I put a special emphasis on hiring extremely talented and motivated individuals. The key element is one of trust. A good leader has to hire people that he trusts and then give them a tremendous amount of freedom within the constraints of the requirements about the way they are going to perform. You say, "Here is your sandbox. I am going to trust you to do what you know how to do, and I am basically going to leave you alone. I am only going to look over what you do to make sure you are staying in the sandbox and playing fair."

Kiev: What else can they expect from you?

Todd: I need to be sure that I can live up to my commitment to those who trust in me. During the good times, it's easy. They are making money every month, and there is no problem. But in bad times, I need to stick by them and stick by that commitment to give them freedom to function within the constraints of the requirements.

Secondly, I have to have a great deal of discipline in executing the strategy. I need to look ahead when I hire someone and say, "What are all the things that could go wrong?" If they have drawn down quite a bit, but they say their strategy is not fundamentally broken, that it hasn't violated the sandbox parameters, then I stick with them, even though I say, "This is killing me." I am staying by it because we agreed ahead of time this is correct.

Kiev: What are other elements of this mutual arrangement?

Todd: As a good leader, I need to understand what they are doing so that I can support them in bad times. In order to make these promises, I have to know what I am talking about because otherwise I am going to find myself changing my mind a lot. At the same time, I need to be disciplined so that when people violate the sandbox, I can say, "You are outside the parameters. You haven't lived up to your end of the bargain, and we have to reestablish or end this relationship."

Kiev: How would you characterize this type of relationship?

Todd: I think giving people the intellectual freedom to do what they want is incredibly empowering.

Kiev: It seems that these principles would apply to a lot of different organizations where leaders are dependent on the knowledge base of the people on their teams.

Todd: I would think so.

Kiev: Have you seen situations where these principles haven't been applied?

Todd: Yes, when I was at one of the largest investment banks, a general partnership, my bosses were incredibly micromanaging. They would come by twelve hours before we launched a new strategy and say, "Well, we would like you to run these tasks before you launch." Their only explanation was: "We are in charge." I was living and breathing this for a long time: "I know better than you do right now about this strategy. You may have broader knowledge. You may be wiser than me in general. In this little corner of the world, I am the pro. You should listen to me." So whether it was ego, fear, or both, they were forcing me to make changes that complied with their current wishes. Oftentimes there would be a blow-up—something would go wrong. I could point to the exact moment where they needed to make a change. But then they thought I was making excuses, and the relationship would unravel.

Kiev: Where do you think management goes bad? Can you give me an analogy of how it happens?

Todd: Imagine Bobby Fischer or some world champion is playing chess, and I am managing it. He is about to do a move, and I say, "Before you do the move, explain it to me. Go down that road; let's see how it goes five moves in." This kind of bad micromanaging happens far too often. The manager is pulling his hair out. "This is a disaster. You are fired. Leave—I am going to take over." Of course, he takes over and loses because he doesn't understand it fully. Not only does he lose, but also he completely blames the fired person (who now hates the manager because he feels he is being blamed for the result, even though the manager didn't know what he was doing). In this kind of damaged relationship, both sides think they are right, but fundamentally, it was the boss's lack of understanding.

Kiev: Do you think that pattern happens more often in traditional organizations than in the more empowering model that you follow?

Todd: Absolutely! I think that pattern is *de rigueur* in America.

Kiev: Command and control?

Todd: Command and control by egocentric individuals who are ruled by their own narcissism. I don't think that's right. I think the really strong person understands what their role is. For example, my role here is to hire people who are smarter than I am at what they do, then trust them. I know this guy is great. I don't fully understand what he does, but I believe he understands it. I know enough to know that this scenario is very possible.

Kiev: To create good work you have to allow your team creative space within the parameters you have set. To make money in finance requires a certain amount of ability to deal with the unknown, to deal with a lot of changing variables. What if the leader doesn't do that? What is the effect of bad leadership?

Todd: Depending on the degree, it can be everything from frustration, to lack of trust, to a lack of willingness to do work, to a lack of loyalty. If my boss is constantly telling me that I am not so good, that he is better than me, he is saying, "You are just an extension of my brilliant mind." That frustrates me. When I am frustrated, I shut down. I start to second-guess myself. I start to worry more about what my boss is thinking than what I think is right. People leave because they are frustrated, or they shut down, or they simply under-perform.

It takes a certain amount of strength to empower others, to tolerate their risk when you recognize that you are responsible for it. But the only way for a leader to truly empower his team is to allow them the freedom to take the risk and sometimes to even fail.

This kind of psychological awareness on the part of leaders is necessary for team members to function as creatively as possible within the parameters of the firm's objectives and is a good jumping point for consideration of what is known as the flat organization.

INTRODUCING THE FLAT ORGANIZATION

A flat organization is different from the way in which many of us have experienced the business world, but it can offer opportunities that we may have never considered possible before. The flat organization is a structure designed to tap into the creative talents of the people in the organization in the best possible way by encouraging autonomy and self-directedness within the framework of a firm's larger objectives and vision.

A leader in a flat organization may find some initial discomfort in the new surroundings. After all, leadership in this type of atmosphere requires sharing (not hoarding) research and information. It requires leaders to be emotionally sensitive, open, and yes, even vulnerable. If leaders can master these strange waters, they will soon learn that these characteristics are consistent with the psychological openness and tolerance of uncertainty, ambiguity, and change, which enable the best traders to navigate the marketplace. By surrendering their ego and maximizing their trading performance, the best hedge fund leaders will be able to empower their colleagues and teammates and discover that managing a flat organization enables the leader to tap the hidden potential of every team member.

Most creative hedge funds are basically flat organizations with a lot of contact between the leader and his teams of analysts, traders, and portfolio managers. The hierarchical structure is limited, allowing the leader to recognize the emotional needs of people to express themselves and to be acknowledged by him.

As Paul, an industrial analyst, put it: "The value of a flat organization is that you have more autonomy and flexibility and can more readily adapt to changing markets. You have more chances to take the initiative and more accountability for your results, which can be a good or bad thing, depending on how you are doing. Furthermore, you can talk more directly to various analysts or traders who are working in other sectors, exchange information, and share your best ideas in order to produce these results. There is more autonomy and greater accountability for results. You have to put your ass on the line every time. You can't hide behind the structure of the organization."

By contrast, in a more traditionally structured kind of organization, such as an investment bank or large long-only funds, there is less opportunity to monitor the work of the analysts who may be reporting to another department because of the complex way in which the organization may have been structured. In such organizations there are too many layers of people to go through, and communication is not as precise or timely.

For example, I recently had a discussion with a hedge fund manager named Micah. Micah and I discussed ways in which he could involve his team in his larger vision for the firm. I urged him to challenge the team members to find new ways for developing the investment thesis, even if that made them (and him) slightly uncomfortable. I encouraged him to use a more forceful view to help get the team members to voice their ideas instead of just standing on a soapbox and pontificating. This was going to require a movement out of his and their current comfort zones.

To be a good leader in a flat organization, I explained, a manager has to push his people as far as he can, not so much for challenging their analytic points of view but in getting them to think beyond what they would ordinarily think about as they try to size the positions. Listen to Micah's initial response:

> *It is like sitting around a table and saying, "Let's talk about the art of painting with water colors." Is everyone going to have the same look in painting when they leave the table and go back and paint something? No, they are going to have a different impression and different view, a different product of their experiences and what they are feeling. That to me is what portfolio construction is like. It is not totally formulaic. A lot of it is an art form. I have thought about it a lot, of how my painting would look. What I want to ask is, "How do I make my painting better? How do I adjust it through input*

by other people?" The reality of it is, no one else in that room has ever managed money before. I don't think that they have ever really thought about it. I think they are still learning how to paint.

Using Micah's own analogy, I argued that the issue is not to teach the team "how to paint" but to brainstorm their best thoughts in the sense of helping him (the leader) to create the picture he wants created. For example, if there is an objective in mind of how to produce a portfolio of a certain size with a certain profitability, then ask the team to consider their formulations as *that* objective rather than some vague theoretical one. If indeed you have to make $10 million in technology as part of the $100 million result for the month, how big do you have to get? By using the reverse engineering principle, leaders can challenge team members to come up with a size that is consistent with the outcome that is needed.

Of course, there is going to be tension, but the best leaders want to push people to fit into a larger frame. It is very probable that you are going to hear a little bit of "I don't know what I need to do." Then you say, "Fred, what do you think Jack can do?" You encourage them to contribute to each other's quandary. You are trying to introduce a little more vitality into the place through dialogue among the members of the team and then by holding them accountable for the goals. When a team works together in this way, their efforts will still reflect individual points of view, but they will be stretched to have met the requirements of the portfolio.

As we walked through this discussion, Micah began to get a glimpse of what I was describing.

"'They should be giving me a more realistic set of guidelines,' he said, 'not just relying on my intuitive grasp of the market. Then they will feel more connected to what I am doing because they have thought it through . . . and will be more committed and watch it more closely or think about it a little more. So you are saying, get people to express what they think the upside is versus the downside. Then they have to see what the quality of it is and relate it to how much money they want to make.'"

As he began to look at his organization in this way, Micah began to see that he is the pilot, but his team members are the navigators. The leader sets the destination. The team plots the course. Obviously, there will be times that the leader's experience dictates that his opinion takes precedence, but when team members are given the opportunity to think through the plans with the leader, they will still feel more powerful and engaged. Don't worry, at the end of the day their natural, artistic intuition won't disappear. They will still throw the ball the same way they throw it. The leader's goal is to get them to throw it harder and faster.

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Case Study on Becoming Comfortable with a Flat Organization

Not everyone welcomes the autonomy and responsibility that comes with the seemingly laissez-fare approach of the small hedge fund. Newcomers, therefore, to such a flat organization often feel as if they are not getting the support they need.

While the flat organizational structure of hedge funds fosters autonomy and greater personal responsibility, it also provides fewer guidelines and structure for those originally trained in more highly organized and hierarchical organizations such as investment banks and mutual funds. This was true for a portfolio manager named Sean who felt that this new firm was "a little bit disorganized."

Sean: I come in with a little bit of a different perspective. I didn't have a lot of the portfolio management experience. I think it would have been helpful to have a layer of structure. You've got a lot of autonomy, but it would almost have been nice if I had received more guidance and mentoring for the first three to six months. The firm is so loosely structured as a flat organization. I don't know what is expected of me, and no one seems to want to tell me.

Kiev: Have you ever considered that the firm was intentionally designed this way, to bring out the best in people and that it might be useful to learn how to take advantage of this freedom?

Sean: Not really.

Kiev: I think there is a set of expectations of how to do things but that each PM is given a lot of discretion in figuring out how to contribute to the main account. Have you figured that out yet?

Sean: I think so. You helped me realize that I have to get past my own expectations and interpretations of things.

Kiev: Do you have some notion about yourself that has changed?

Sean: The change that I have made is just being less passive. You do have a lot of autonomy here, and you do your own thing. The bad thing about it is you don't force yourself to change as much. You want to be out of your comfort zone and put yourself on the line and make a bet and then get rewarded. I have had to move from being more passive to being more aggressive.

Kiev: Were you brought up to be aggressive?

Sean: I was aggressive in certain ways. From the standpoint of getting my ideas into the portfolio, I was under the assumption that I should just work really hard and do my work. I thought that as I made money the portfolio manager would see it, and he would want to come to me and get my ideas. But if I want to have an effect on the firm's main account, I have to be in his face, you know, getting him to notice me.

Kiev: Being proactive. Were you inclined to be too passive before?

Sean: At first yes, because I didn't really know the structure of what's going on here. One of the things you helped me understand is this is the *modus operandi* here. This is how things function. Passive isn't going to work. I need to be aggressive. If I have good ideas and am making money, the way to get more capital is to go up and say, "I have great ideas; give me more capital." I can't be like "OK, whenever you are ready, I would like more capital."

Individuals who have developed a *need* to have a handle on the contextual clues of the organization often require quite a bit of coaching to learn to become more self-assertive in contributing in a flat organization, getting recognition, and leveraging it to increase their capital allocation. Of course, this is not always comfortable and may take time, but as we work through the rest of this book I hope you will begin to discover that sometimes discomfort is the first step toward mastery.

STARTING FROM THE EMOTIONAL CENTER

As you will see throughout this book, the best leaders have the skill to reach the emotional wellsprings of belief, motivation, courage, and perseverance, which help contribute to trading success. However they do it, they generally are able to do some or all of the following key steps, all of which you will no doubt learn as you read and study the leadership principles explored in this book.

1. Find a leverage point from which you can encourage someone to see the necessity for trying something new, and so be willing to change a behavior and take a risk. The ability to foster such changes works best when your colleagues can admit to problems or issues or identify something they want to change or improve.
2. Look for the cutting edge. Ask what more someone can do; what incentives will help them to change, how can they reframe their objectives so as to overcome inertia and longstanding patterns of complacency and caution.
3. Define a vision or purpose to help you and those you lead to become more engaged in the present moment before you.

4. Anticipate resistance from others and prepare to challenge them in a compassionate way.
5. Help others to keep focusing on the goal, while creating a safe space, which allows people to fail. Be open to understanding their struggle, and create a safe space for them.
6. Above all, keep listening to what others are saying directly and indirectly and pay attention to your own inner voice.
7. Most of all, listen to what others are saying, to what your associates might imply in indirect ways, to your own most trusted inner voice.

Keep these themes in mind as you read this book so you can improve your ability to lead others and get a better understanding of the psychological underpinnings of good leadership. Read it to see how to address the deeper layers of your feelings, the unspoken conflicts, the sources of tension that exist in your organization. The key, of course, is to know yourself, and to have an understanding of some of the psychological forces pulling you and others in opposite directions. You do have to recognize the need to be transparent, to tell the truth, to be as good a listener as you are a speaker, and to encourage others to buy into your strategy. You do have to learn to choose the right people for the right jobs on your staff, to uncover and unleash their strengths, and to be tough about moving out those who don't accept your ideas. You need to crank up the energy level in your organization, to build momentum, and then take what steps you must take to sustain momentum. You need to learn strategies that avoid both burnout and euphoria, which are the twin enemies of breakthrough results. You need to discover how to make sure that when you are no longer in charge, you have left a legacy that will keep your organization advancing forward. Employ these strategies, and you will begin to think like a leader.

My hope is that this book will jolt you with what I call the *ah-ha* phenomenon. I want you to think, "This makes sense! That's a good idea! I can do that. I can think about the unthinkable, I can talk about the fact that I'm not communicating, that I think some of my people are resisting me." When you reach the last page, I hope you'll say to yourself: "Communication is a two-way street. It's important to talk about the things that people don't ordinarily talk about in running a company."

I'm not going to tell you how to do your job. I'll talk about how you can do what you're doing more effectively by looking at it from a larger frame of reference, by discussing an often-buried underlying layer of understanding. With this knowledge, you can uncover some of these issues, sit your associates around in a circle, and find out who they really are. Perhaps then you and your team members can at least acknowledge unspoken issues in your organization. Maybe, having brought them out into open, you can minimize the frustrations and tensions that occur when such issues are allowed to fester under the surface. This will help you win more ballgames over the long haul.

I look forward to introducing you to these concepts. To begin, however, I would like to talk about what we mean when we use the word *leadership* as it relates to the concept of vision. Every great leader starts with a vision of the future. But leading from your vision requires a change in perspective from the old (and, I believe, outmoded) ways of taking charge.[5]