

The Five Leadership Lessons of Lehman Brothers' Demise

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"Dick Fuld ran Lehman Brothers as if he were at war. He drove the bank hard and ignored the signs of collapse... He was the textbook example of the 'command-and-control' CEO." Andrew Gowers, former editor Financial Times, who worked at the heart of Lehman's Corporate Communication area during its last 2-3 years (as reported in London Times, December 2008).

Much has been written about Lehman Brothers' ultimate demise at the hands of the US government's refusal to bail it out. Perhaps others knew the real inside story – a pack of cards waiting to collapse. As Gowers went on to write: "Here was a corporate governance pre-programmed to fail: an over-mighty CEO, a top lieutenant eager to please and hungry for risk, an executive team not noted for healthy debate... a power struggle between the key players ... a board of directors packed with non-executives of a certain age and woefully lacking in banking expertise." Let's examine these point-by-point.

- **An Over-Mighty CEO** – Dick Fuld apparently defined himself as somewhat at war. His apparent ability to inspire tremendous loyalty in some but great fear in others increasingly insulated him from trouble: people were reluctant to share anything that he might not want to hear. We heard about this exact same issue with another failed CEO, Bernie Ebbers of WorldCom-MCI. Such insulation by Fuld was further reinforced by the personality of his No. 2 (or COO), Joe Gregory, a long-standing associate (see next item).

55 quarters of unbroken profit, during some testing times, apparently encouraged a fatal complacency among Fuld's top team. He among others was apt to brag about being better positioned than Merrill Lynch, which had been recently swallowed up by Bank of America (something B of A now regrets). Fuld's visits to his trading floor (one of the firm's key business engines) were rare, consequently shutting him off from independent sources of information. Such behavior enticed him to be lost in his own bubble of self-importance.

Note: It is recommended that senior executives have regular lunches with randomly selected, small groups of "front-line" staff to keep them in touch with daily business realities, as well as

signal their interest in connecting with such grass-roots people. Initially such lunches are likely to be a little stiff and strained, owing to historical barriers between such levels, but, over time, staff members will begin to loosen up and make it a highly worthwhile experience for both parties.

- **A Top Lieutenant Eager to Please and Hungry for Risk.** Joe Gregory commanded day-to-day operations (COO) and operated, according to Gowers, as "If Dick was the king; Joe was Cardinal Richelieu." In other words, Joe was a ruthless enforcer for Dick: consequently smothering any debate or honest inquiry about the investment house's direction among its senior team. Joe was regarded as Darth Vader within this team owing to his "towering rages" when anything went wrong: executives felt they had been through a horrible wringer when he was on their case.

At key moments, when Dick Fuld was advocating his worries to the outside world, about Lehman being sufficiently risk averse and detail oriented, Joe would be pressing division managers to be even more aggressive in their bets as its markets surged: especially home mortgages and commercial real estate. Division managers would be in no doubt that it would be "fatal to their careers" not to push the risk envelop. There appeared to be a revolving door in risk management areas to make the point. Toward the end, Lehman led a consortium bid for America's largest apartment company (a deal of \$15 billion). Some Lehman executives apparently regarded it as "the worst investment decision ever made by the company."

Note: Although a seemingly natural thing to do, CEOs should be wary of appointing COOs to run their daily operations. Too often there are as many downsides as upsides to such a move, not least the likelihood of insulating CEOs from daily realities and also from their customer base, too (hence lose their feel for their market and their organization). A strong team of executives should be able to take care of daily requirements without having to add another layer (and all its associated expense and cultural challenges).

- **An Executive Team Not Noted for Healthy Debate** – Lehman became overloaded with dodgy assets that could not be sold and were under-capitalized to support such a large balance sheet.

The business was like “a rickety house built on a thin foundation.” Even so, there was little known debate among the executive team about these issues, due to Fuld’s “no bad news personality” combined with Gregory’s iron hand.

Note: Command-and-control behavior at this level will swamp any intelligent discussion and, by its very nature, probably at any other level within an organization. Since CEOs are not humanly able to have all the answers, such closed-debate environments make companies most vulnerable.

- **A Power Struggle Between Two Key Players** – The top team was apparently riven with a number of nasty rivalries. And sentiment was that Joe Gregory liked to keep it that way – dog eat dog. There was particular animosity between the most senior US divisional head (Bart McDade) and his counterpart in London (Jeremy Isaacs). When the London division started contributing more than 50% of Lehman’s revenues, the power struggle to determine who would ultimately replace Dick Fuld just intensified. People within the company were anticipating a “blood-bath” when the moment would eventually come. Both men were to have a significant impact on Lehman’s eventual demise.

*Note: Such power struggles can become particularly vicious when CEOs (although in this case it was more the COO) operate on a divide-and-rule basis. Equally, when senior executives are not familiar with the differences between **Visionists** (CEO types) and **Strategists** (executive types), they cannot be mentored to discover whether they are best suited to one or the other. By clarifying early on an executive’s propensity for one or the other role, he/she is likely to become more realistic about their chances for promotion. Where there is a real top-team spirit, there is an even better chance people will come to terms with their eventual role – for the good of the firm.*

- **Board of Directors Woefully Lacking in Banking Expertise** – Clearly Lehman’s board of directors did not do sufficiently well to prevent the bank’s demise. It would clearly have helped to have had a portion of directors with investment banking expertise, who could then ask appropriately insightful questions. Although, all the indications are that Fuld’s style was not particularly open to such questioning. He probably preferred to have a compliant board.

Note: Board-CEO relations are critical in any company. There are plenty of businesses where the relationship is quite dysfunctional. Directors can either be too hands-off owing to the CEO’s disposition or too hands-on where they try to micro-manage the CEO’s company. More often than not, directors do not ask the coaching/mentoring type questions that encourage a constructive and healthy relationship between the two parties. Moreover, board members do not always reflect the types of insightful input CEOs could benefit from: that is, expertise in envisioning, executive development, resource acquisition, executive team building, corporate governance, building momentum, critical decision making and so forth ... notwithstanding the need for specific industry expertise.

Lehman’s demise in a matter of months, where it went from a company worth \$42 billion in February, with \$639 billion in total assets and 26,000 employees, to nothing by September 2008 shows how fragile it was. Fuld’s mixture of apparent defiance and paranoia – “us against the world” – could only work so long. He never tired of telling people that Lehman was “built to triumph in adversity.” He used this hostile mantra as a means of motivating his sizeable workforce. We have seen other historical collapses over the centuries where similar “hostile” motivation was used – rather than focus people on genuine opportunities. The five management/leadership forces described undoubtedly fueled Lehman’s ultimate death spiral.

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