

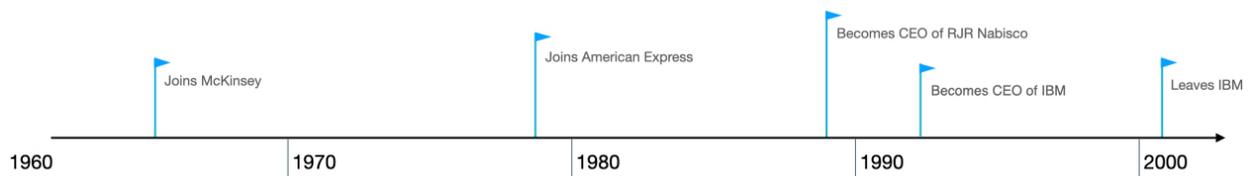
Lou Gerstner – Active Coper!

By Leslie Pratch

Some CEOs cope with whatever life presents; more than that, they grab opportunities. They learn from experience, face problems rather than avoid them, overcome obstacles rather than giving up or blaming others. They consider others' interests and the interests of society, as well as their own. They seize opportunities that others miss. They seek out multiple perspectives, in order to avoid own blind spots. These are active coping behaviors. Lou Gerstner is a model of active coping. CEOs for your portfolio companies should be too.

Lou Gerstner began his career at McKinsey in 1965, where he became one of the youngest partners in the history of the firm. In 1973, he went to American Express. During his 10 years at American Express, he grew its business from 8.6 million to 30.7 million cardholders and produced 18% annual profit growth. In 1989, he became CEO of RJR Nabisco. There, he unified two separate cultures that had been brought together through the merger of RJR Tobacco and Nabisco Brands. KKR had purchased RJR Nabisco in 1988 in a leverage buyout that left the company with \$25 billion debt. In four years, Gerstner reduced the debt to \$14 billion, sold off \$6 billion of non-core assets, and cut general expenses. In 1993, he was hired by IBM as the once world-class company was approaching failure. Most people believed that only smaller firms could nimbly adapt in the rapidly changing technology industry, and IBM's board expected Gerstner to break IBM up. Instead, Gerstner kept the company together and revitalized it. In nine years under Gerstner's leadership, IBM's market capitalization rose from \$29 billion to \$168 billion.

Lou Gerstner's Career



When you pick people to run your companies, you'd like to find someone like Gerstner who can lead an organization through tumultuous times. A person might have a good track record but not yet the sustained success under trying circumstances that marks the active coper. How can you tell if a candidate's previous success is luck or circumstance or if it actually reflects how they are as a person and leader? We'll talk about how you can identify these characteristics in advance, before a candidate has the track record after we delve into the example from Gerstner's life and learn more about what active coping is.

Active coping is necessary but insufficient. Great leaders also need intelligence and motivation. Many executives are smart and motivated to lead but lack the coping to carry out their ambitions. They may do well in stable situations they're familiar with, but they won't necessarily respond well to significant new challenges and opportunities. But let's first talk about active coping with stories of someone you might have heard something about.

Active copers have characteristic behaviors that reflect their underlying psychological makeup. They:

- face problems rather than avoiding them,
- overcome obstacles rather than giving up or blaming others,
- take into account the interests of others and of society, as well as their own,
- take advantage of opportunities that others might fail to capitalize on,
- seek to understand multiple perspectives, so as to avoid own blind spots, and
- learn from experience.

As we talk about each of the dimensions, we'll use examples from Gerstner's life.

Face problems rather than avoid them

Gerstner was recruited to lead IBM when it was about to fold. In 1992, *The Economist* wrote, "In an industry driven by rapid technological change and swarming with smaller, nimbler firms, can a company of IBM's size, however organized, react quickly enough to compete? And can IBM earn enough from expanding market segments ... to offset the horrifying decline in mainframe sales from which it has always made its money? The answer to both questions may be no." Gerstner, then the CEO of RJR Nabisco, knew that KKR was planning to sell its stake in that company, and Gerstner was open to leaving too. He called Vernon Jordan, a friend and a director of RJR Nabisco, for his advice. Jordan said, "IBM is the job you have been training for since you left Harvard Business School. Go for it." Gerstner also realized, "I had always drawn to a challenge. The IBM challenge was daunting, almost frightening. But it was also intriguing."

Overcome obstacles rather than giving up or blaming others

When Gerstner arrived at RJR Nabisco in 1989, he discovered most of the senior executives had departed. "I'd thought there was going to be some management here. But practically no senior people were left. We had to decide, how do you run a \$15 billion business?" Gerstner recruited new leaders. His team cut costs except when spending directly benefits the brands. Gerstner also raised close to \$6 billion by selling low-margin commodity lines and low market share brands. He increased spending on R&D, marketing, and sales to strengthen the brands he kept.

KKR expected to keep the company private for five years, and Gerstner's plan was designed position RJR to go public then. Unfortunately, the junk-bond market collapsed, and to save the company RJR was forced to sell 50% of the company to the public. Now Gerstner had to satisfy public stockholders and KKR. Meanwhile, the sale of cigarettes (RJR Nabisco's most profitable products) was declining. The stock price dropped when the EPA said secondhand smoke caused lung cancer. And there was a recession. Gerstner and KKR both decided it was time to abandon the rejuvenation plan. Gerstner exited just before KKR.

Gerstner decided to keep IBM intact rather than divide it into separate business units. He faced IBM's core problem of declining mainframe revenues by pushing his team to develop a cheaper mainframe that ultimately became more powerful and cost-effective for consumers. This reversal restored customers' trust in IBM.

As the Gerstner/RJR story illustrates, not giving up is not an absolute rule. Rather, it is an orientation that an active copier has – to keep looking for a way forward, or an alternate path. But it is possible for an active copier to run into circumstances that are impossible (for them and the resources they can gather) to overcome.

Take into account the interests of others and of society as well as their own

Gerstner took the IBM job for himself, for the company's employees and shareholders, and for the U.S. – all these interests aligned. The head of the company's search committee told Gerstner, "You owe it to America to take the job." A second search committee member argued that Gerstner's track record as a change agent – first at American Express, then at RJR Nabisco – was precisely what IBM needed – "a leader who could grab hold of it and shake it into action." Gerstner felt, "IBM is such a national treasure that it was my obligation to fix it."

Shortly after becoming CEO, Gerstner listened to the concerns of a large group of CIOs, an important part of IBM's customer base. Based on their complaints, Gerstner promised to them that IBM's priorities would start with the customer, that it would provide the performance the customer wanted, and that it would deliver open, distributed, user-based solutions. He asked all senior managers to meet with customers to discover and solve their problems. Based on their interviews he identified shifts in customer attitudes and context. The high price of the mainframe and IBM's promotion of centralized computing alienated business customers at a time they were increasingly shifting to distributed computing, delivering computing power to individual employees.

He made good his promise to the CIOs by reducing the price of mainframes and boosting their performance, delivering consistent customer service no matter where the customer was based, and pushing to make services a driving force inside IBM. The services business shifted to recommending the products of all major IBM competitors if that was the best solution for the customer (rather than only recommending IBM). IBM serviced those products too. Services' revenues in 1996 were \$5.9 billion. By 2001, the business had grown to \$32 billion.

Take advantage of opportunities that others might fail to capitalize on

When Gerstner joined IBM, its board of directors expected him to break up the company. But Gerstner viewed IBM's size, geographic reach, broad expertise, and research capabilities as a competitive advantage that could be exploited. He positioned the company to deliver integrated solutions and services to customers that the competition could not and created a global services business that rapidly became a leading technology integrator.

Gerstner also saw that the emerging network model of computing would require large scale computing infrastructure products, which IBM was uniquely capable of making. IBM's network business addressed all the opportunities and challenges of creating and operating a customer's network infrastructure.

Mainframes were IBM's legacy business, but they had become less profitable to make. To cut costs and prices, Gerstner shifted to a new technology architecture, a shift his predecessor had resisted making. IBM was able to reduce the price of mainframes while making them more powerful which spurred huge sales growth. By 2000, IBM was virtually the only manufacturer of mainframes, as its aggressive technological changes left competitors behind.

Seek to understand multiple perspectives, so as to avoid own blind spots

Before accepting the job at IBM, Gerstner gathered information about IBM and its problems by listening to industry pundits, the media, IBM's competition, and IBM's recruiters. He asked for permission to talk with one of the Board's advisors so he could better understand the financials and budget.

Before becoming IBM's CEO, Gerstner also met Dennie Welsh, the head of an IBM subsidiary that provided customized information technology services to U.S. customers. Welsh envisioned a services company "that would

literally take over and act on behalf of the customers in all aspects of information technology – from building systems to defining architectures to actually managing the computers and running them for the customers.” Gerstner embraced Welsh’s vision.

Once he got to IBM, he talked to his brother who had been an IBM executive, and listened to his brother’s insights. Gerstner met with all the senior managers and observed them with their direct reports. He met with a large group of CIOs, who were part of IBM’s customer base. He had each of the 50 members of the senior management team visit at least five of IBM’s biggest customers to listen, to show them that IBM cared, and to solve their problems as quickly as possible. Each of the executives’ direct reports was to do the same. Gerstner asked the executives to write a report on each customer visit for him and for anyone else who could solve that customer’s problems. He read all the reports.

Learn from Experience

Gerstner learned from holding multiple large company jobs. He learned while at American Express that IBM made life difficult for the customer whereas American Express had consistent service no matter where the customer was located. He learned from leading RJR Nabisco that companies facing multiple challenges can run out of cash quickly. He learned not to ignore customer demands.

When he became CEO of RJR Nabisco, he was aware of some of the company’s problems – the 2% to 3% annual decline in the U.S. cigarette market and the fact that R.J. Reynolds, formerly No. 1, "was being hammered by Philip Morris." But he did not see soon enough that the fundamentals of the tobacco business were changing. Even as consumers switched to cheaper brands, RJR was focused on higher-quality more expensive brands. Gerstner later said: “We were fools. We were naïve. As the guys playing the volume game were rolling out their discount cigarettes, guess who lost? Us.” Too late, RJR joined the cut-rate fray. Gerstner learned not to ignore consumer demand. “The world is changing so much and so fast that if you don't modify, shape, adjust the tactics you use to implement your strategy, the strategy becomes useless.”

At IBM, he applied what American Express did to provide consistent customer service by reorganizing the company around global industry teams. A customer would receive the same service in all of his locations and support systems would be easily replicated. He applied what he learned to his successive environments/ challenges.

Finding the right leaders

So, how do you identify among seemingly equally qualified candidates, who has the personality to be a great leader for your company?

You can use assessment techniques that give you a glimpse of what is going on under the surface of someone. To be an active copier, a person needs a particular alignment between their conscious and unconscious attitudes. The assessment techniques let you understand both their conscious and unconscious perspectives and draw conclusions about their active coping capabilities (or lack thereof). They also examine the stability of the executive’s motivation to lead and interpersonal skills to lead.

If you own a company and want to make sure the right leader is in place to implement your plan, please get in touch.

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