Leadership succession critical to sustainability

By Kurt Lieberman, CEO of Magni Global Asset Management. He can be contacted at klieberman@magniglobal.com.

Last month, I discussed how Jack Welch and General Electric (GE) exemplified the era of shareholder value, while his successor Jeffrey Immelt is considered to have been unsuccessful in his role as CEO. Perhaps Welch chose the wrong person. His other alternatives included two of the best and most high-potential executives inside a company with a reputation for developing great leaders.

What can we learn from the post-GE experiences of the two who lost the succession race? If one of them had tremendous success, then the wrong person probably was chosen. However, if neither were successful, then perhaps the shareholder value model is not sustainable.

Alternative 1: Robert Nardelli

Robert Nardelli had the nickname 'Little Jack' while at GE. Soon after Immelt's selection, Nardelli left to become Home Depot's new CEO, despite having no retail experience.

He attempted a dramatic overhaul of the company using methods from GE. Relentless cost-cutting replaced the entrepreneurial culture of innovation.

While sales and profits rose, turnover of experienced store staff increased, and the quality of customer service deteriorated, thus enabling Home Depot's primary competitor to increase its market share.

Applying the shareholder model to Home Depot provided a tactical boost in financial performance, but it was not sustainable. Nardelli and the board reached mutual agreement for him to resign at the beginning of 2007.

Later in 2007, Nardelli was recruited by Cerberus Capital Management to run Chrysler, which it had just purchased. Soon after that, the global financial crisis started. Chrysler filed for bankruptcy on the 30th April 2009.

During 2010, Nardelli became the head of Freedom Group, a gun manufacturer. Within 18 months, Nardelli stepped down as CEO.

Alternative 2: James McNerny

James NcNerny has a blue-chip pedigree: degrees from both Yale and Harvard, brand management experience at Procter & Gamble and consulting experience at McKinsey & Co. During 19 years at GE, he rose through the ranks of the company.

Soon after losing the succession race, 3M hired him as CEO. His four-year stint was more successful than Nardelli's time at Home Depot.

The board hired him to reinvigorate growth in the company.

He made significant changes and was popular with the workforce. Like Nardelli, he too applied the GE playbook. While earnings improved, capital spending dropped 65% and the research and development budget dropped 25%. Growth was not reinvigorated. In 2005, George Buckley assumed the role of CEO at 3M.

McNerny was hired by Boeing as CEO that same year. For the next 10 years he ran the company.

In 2015, he retired with an internal candidate, Dennis Mullenburg, succeeding him. During McNerny's tenure, the company achieved record profits, though it was during the longest aviation boom in history. There was significant discontent among workers, especially union workers.

> ***"As those in Islamic finance already know, the era of shareholder value is not sustainable"***

Lessons learned

Immelt, Nardelli, and McNerny rose through the GE management program. All three learned the GE playbook. In one way or another, all three used the playbook throughout their careers.

All three made significant changes and delivered near-term profits. None of the three achieved the primary change required by the companies they led. The companies were in a similar or worse situation by the end of their respective tenures as CEO.

Of the three, McNerny appears to have done the best job. At 3M, he delivered profits and was popular, though growth was not reinvigorated. At Boeing, he delivered profits and was unpopular, though he did not fix the deteriorating governance and did not demonstrate the ability to move the company in a better direction.

Even if Welch had chosen McNerny, GE likely would not have continued its success. As those in Islamic finance already know, the era of shareholder value is not sustainable.