Investment Leadership

Building a Winning Culture for Long-Term Success

JIM WARE
WITH BETH MICHAELS
AND DALE PRIMER

WILEY

John Wiley & Sons, Inc.

More Praise for
INVESTMENT LEADERSHIP

"After 30 years as an active participant/observer of the investment management profession, I've seen every conceivable organizational structure, personality type, and management style. Or so I thought! *Investment Leadership* marshals a prodigious quantity of theoretical and empirical insights into the investment industry—how it works and who makes it work. Portraits of the characters who lead the firms made me envious, amused, and generally charged up to do a better job at my own firm. Ware, Michaels, and Primer observe people in top positions doing the *right* thing well."

—Theodore Aronson, Chair of the AIMR Board of Governors

"Investment managers tend to be a lot better at investing than at managing. This is unfortunate because investment success flows from quality leadership, culture, and creativity. *Investment Leadership* provides money managers with the necessary tools, diagnostics, and examples to improve their organizations—and their alphas."

—Michael J. Mauboussin, Chief U.S. Investment Strategist,
Credit Suisse First Boston

"Given that ours is a business of nurturing and managing human capital, this book provides a systematic framework with pragmatic exercises that will generate a meaningful impact on performance. A 'must read' for anyone seeking to create a culture that will survive market cycles and deliver value to clients."

—Keith F. Karlawish, CFA, President and CIO, BB&T,
Asset Management, Inc.

"According to the SEC there are 7,468 Registered Investment Advisors in the United States managing almost $1 trillion. How is it that when America's leading firms are cited not one of this very sizable group generally makes the list? *Investment Leadership* documents how and why the leadership vacuum that exists in the investment management industry has left the industry in a particularly precarious position. But, not content to simply document the leadership gap, Ware has identified the critical qualities and best practices of investment management leaders who have set the standard. This book should be required reading for all of us in the investment management industry."

—Margaret M. Eisen, CFA and Chair, The Institute for Financial Markets

"*Investment Leadership* is a nice, easy-to-read compendium of thoughts, ideas, and insights into the cultural aspects of investment organizations. The authors provide a broad landscape for the interested reader to traverse while seeking their own vantage point."

—Gary P. Brinson, CFA, GP Brinson Investments

"There are a lot of books written about investment people and their investment processes, but finally here is a book studying the environment and culture that these investment professionals work within on a daily basis. The environment alone provides for a portion of the excellence that these individuals achieve, and this book is an excellent read on that fascinating part of the business."

—Stephen Kneeley, President, Turner Investment Partners

"It's not managers, but leaders who are in short supply in the investment management industry. This book provides food for thought and a roadmap for defining leadership and building a values-based organization."

—Susan B. Fowler, Managing Director, Russell Reynolds Associates, Inc.

"*Investment Leadership* is an entertaining, easy-to-read, and practical guide to the critical factors for successfully leading investment organizations. It is a 'must read' for anyone responsible for managing investment professionals."

—Richard S. Lannamann, Vice Chairman, Spencer Stuart

"Finally, a book that focuses on what really matters: people and relationships. To lead a truly successful organization, you can't just focus on the numbers. You must nurture and create a culture that will help your firm thrive in any market condition. This book offers practical and actionable items to get you started."

—James C. Tyree, Chairman and CEO, Mesirow Financial

"As the investment management industry transitions from a craft to a business, developing the right culture and leadership will be key factors of sustainable success. *Investment Leadership* provides a comprehensive roadmap for those management teams seeking to tackle the challenge of building a best-of-class investment organization and understanding the links between leadership, culture, and organizational purpose."

—Paul Schaeffer, Managing Director, SEI Investments

"*Investment Leadership* gets to the heart of what creates a winning investment organization over the long term: a strong focus on the culture. The authors have done an exhaustive job of chronicling how successful organizations have turned that into their competitive advantage. This is a timely and informative book for managers in today's challenging environment."

—John Ballen, CEO, MFS Investment Management

"*Investment Leadership* demonstrates effectively how cultures instilled by gifted leaders create successful investment management firms. This book is quite accessible—replete with numerous specific examples culled from multiple interviews of and articles by current industry practitioners. The insight derived from reading it should help elevate the activity of managing these firms from a pastime to a profession."

—Stephen B. Timbers, President, Northern Trust Global Investments

Investment Leadership

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Preface

We missed the gravy, but we stayed out of the soup.

—Edgar D. "Ned" Jannotta, Chairman,
William Blair & Company,
describing the company's
performance 1999–2001

Ned Jannotta's comment, from our interview in 2002, captures the essence of this book. William Blair & Company came under intense pressure during the tech bubble and bear markets at the turn of the century. They lost a few good people and asked some hard questions of themselves, but in the end, they survived and have prospered. Others, like Janus, did not fare as well. Bill McKenna, a 72-year-old retired commercial-laundry manager, removed all his money from Janus, explaining, "I've lost faith in the Janus culture. They've lost their direction."[1] Our research examines this issue: How do the best-run investment firms survive the highs and lows that inevitably come in the markets?

There are many good books on leadership and culture. If you do a search for "leadership" on Amazon.com, you'll find more than 12,000 titles. However, if you add the word "investment" to the search, it comes up empty. There simply are no books addressing leadership and culture specifically for investment professionals.

This book fills that gap. It is written for the busy and talented investment leader who knows that people are the firm's most important asset but isn't sure how to fully leverage that talent to get sustainable financial results. Throughout this book, we link the people factor with superior financial results.

It is also written for the investment leader who may never have intended to become a leader! While writing this introduction, I got a call from an investment professional who had just received a significant promotion.[2] During our conversation, he admitted that he wished he were still an analyst. He does not like or want the role of leader. Stephen Timbers, president of Global Investments, Northern Trust, stated it boldly: "Ninety-five percent of investment managers have no interest in managing people." (*Note:* All quotations, unless footnoted, are from interviews we conducted during the period January 2000 through April 2003.) In perhaps no other industry is the attitude "this is a great job except for the people" more prevalent. Most investment professionals are "idea" people, not "people" people.

So, what is the state of leadership in the investment industry? The truth is that there is a huge range of skill: from extraordinary (like Jack Brennan at Vanguard, who has written a book on the topic) to staggeringly poor (one CEO of a sizeable firm responded to our request for an interview on leadership by saying, "Leadership? What is there to talk about? People show up each day and do their work").

THE AUDIENCE FOR THIS BOOK

While writing this book, we had specific investment leaders in mind. Some of them were outstanding, like Brennan or Timbers. For these people, this book is an opportunity to fine-tune their already superior skills. We believe they will find useful ideas and tools for creating a winning culture and for measuring that culture. Ironically, almost every leader whom we consider excellent has expressed a strong interest in reading this book. They don't really need this information—they are already successful—but they are naturally drawn to the topic. Each one has a passion for the organization and its mission and are attracted to anything that will help.

"Bruce" is another person we're writing for. He has an MBA from Wharton and has earned the CFA designation. After serving as an analyst and portfolio manager, he has risen to the post of department head of a major investment operation. The chief investment officer (CIO) recently issued Bruce a tall order: double the amount of investments that the firm did last year. Bruce knows he needs the full talent and effort of the department's 13-person staff to pull this off, but he has no clue how to do it. To Bruce's credit, though, he has the good sense to call in help. He hires a firm to facilitate a series of meetings so that he can get his whole team on the same page. Bruce has expressed interest in this book and would probably read it. (He did read our first recommendation: John Kotter's *Leading Change*.)

Another person we had in mind as we wrote is the job candidate. Say you have just received your degree and are looking to work in investments. Which firm should you choose? Why, the one that pays the most money! We're joking, of course, but many people, especially in the investment field, would make that choice. (It's good to remember that Warren Buffett himself, arguably the world's greatest investor, chose his first investment job solely on the basis of the experience he would get, *not* for the money. He chose to work with his hero, Benjamin Graham [of Graham and Dodd fame], for nothing, just so he could learn from a master.) Along those lines, we believe that a person who is just starting in the investment field would benefit from joining a firm with excellent leadership and a strong culture. People blossom and do their best work in these environments. The key is knowing how to identify such a place. What questions would you ask in the interviews? What answers should you be looking for?

"Jane" is the plan sponsor head at a major organization. She hires a consulting firm to do searches on and monitoring of the investment managers that she retains. All major consulting firms recognize the qualitative side of evaluating investment managers, but the information in this book will help Jane ask the right questions when meeting with her consultants. She may even be persuaded to choose different consultants, based on their ability to analyze the qualitative aspects of a manager.

We also wrote this book for the stock picker. Though our focus is on how to run an investment firm, the lessons we've learned about the so-called qualitative side of the business also yield insights for stock selection. We provide a scorecard for identifying which nonfinancial firms will be outstanding performers. Want to avoid the next Enron, WorldCom, or Tyco? Read on.

The consultants themselves will benefit from reading this book. Many still rely on a gut-feeling approach to leadership and culture. The metrics and tools provided in this book should help them to formally assess investment managers and compare them to one another.

The book is intended for both U.S. and non-U.S. investment professionals. Originally we planned to have a chapter devoted to non-U.S. professionals so that we could address cultural differences and subtleties, making the material more relevant to Canadians, Europeans, and Asians. After speaking to non-U.S. audiences and asking colleagues from other countries to read drafts of the book, we decided the extra chapter was unnecessary. As our friend and colleague Fernand Schoppig—a Swiss-born consultant working in America—told us, "People are people. The material in the book is universal. The major difference is just the size of non-U.S. firms. European money management firms are huge. They have very few of the small entrepreneurial shops like the U.S." Several European audience members amplified this point by saying, "European audiences need it even more than U.S. audiences; we need to catch up on some of this material."[3] This gentleman's comment was reinforced by a woman working at a well-known European asset manager, who told me after the presentation, "Our firm could really use this." When I smiled in reaction to her candor, she gave me a look that said, "I'm not kidding." In the end, we decided not to include an additional chapter for non-U.S. investment professionals—but we invite comments and feedback from all readers: www.focusCgroup.com.

Finally, we believe that this book has valuable insights for any leader who is trying to build a sustainable organization, from a multinational company to a condo board or a Girl Scout troop. The principles are the same . . . though the Girl Scouts are probably a little easier to work with than most of the investment professionals we know.

LEADERSHIP AND CULTURE: TIMELESS FACTORS

In 2003, the world is dealing with the aftermath of Enron, WorldCom, Tyco, Andersen, Vivendi, and worldwide investment firm misbehavior. These events make it painfully clear how important and timely the discussion of leadership and culture is. Just half the respondents to a fall 2002 Gallup poll said that people in most companies are honest and ethical. And there may be worse to come. A majority of corporate businesses responding to a Conference Board ethics study predicted that at least a dozen more major scandals would be revealed during the next 12 months.[4] The premise of this book—that leadership and culture are the critical factors for sustainable success—couldn't be more relevant. Wall Street already knows this is true. In one study, Harvard professors Kotter and Heskett asked 75 analysts to divide the companies they follow into 2 groups: the best and the second tier. The analysts were then asked to identify the factors that separated the groups. All but one of the 75 analysts named "culture" as a differentiating factor. (*Culture* is defined as the values, beliefs, and behaviors that distinguish the members of one organization from another.) During our interviews with senior leaders in the investment world, time and again they acknowledged that culture is critical:

> *"Culture is the key to real future growth" (Bill Nutt, Chairman, Affiliated Managers Group).*[5]

> *"The key to attracting, motivating, and retaining employees lies with a firm's investment culture" (Thomas Dillman, while Director of U.S. Research, Scudder Investments).*[6]

> *"Culture and a set of shared values are absolutely critical and every bit as important as money management style to a firm's success" (Alison Winter, Executive Vice President, Northern Trust Company).*[7]

In this sense, many of the leaders we know see their primary role as being creators and caretakers of the corporate culture.

Because of current events, interest in the topic of investment leadership has never been higher. In 1999, during the dotcom explosion, I was asked by an industry trade group to make a conference presentation called "Leading the Investment Firm into the Future." In a beautiful ballroom that could easily have held 200 people, we gathered: 15 presenters and about 10 attendees. The room was so quiet you could hear the waiters pouring orange juice by the exit doors.

In contrast, that same conference presentation is fully subscribed in 2003. What's more, I've been asked to speak on the topic of "Leadership, Culture, and Investment Success" by more than 50 financial analyst societies, from Vancouver and Des Moines to Rome and Budapest. A survey on "hot investment topics" distributed to professionals by the Association for Investment Management and Research revealed that the overwhelming choice in 2003 is culture.

FOCUS CONSULTING GROUP

Since 1987, Focus Consulting Group (FCG) has been helping leaders build foundations for sustainable success using our expertise in leadership, culture, and change management. Our ideas and tools have been written up in *Consulting Magazine* and other trade publications. Beth, Dale, Jim Dethmer, Fran Skinner, and I work with organizations in many fields, although the focus of this book is on the investment industry. My background on the buy side, as a research analyst, portfolio manager, and director of planning and strategy, plus my experience as a Chartered Financial Analyst and an instructor of finance and investments at the graduate level, provided unique insights into the investment world. This book thus combines in-depth knowledge of the investment industry with our cutting-edge, solidly based ideas and tools in the areas of leadership and culture.

OVERVIEW OF THE BOOK

The book is divided into five parts. The first, called "Foundation Pieces," gives behavioral descriptions of leadership and culture and discusses our general mindset concerning them. It also describes the process of identifying, clarifying, and implementing your firm's values, vision, and culture.

The second part, "Assessment Tools," explains how you can quantify the people side of the business. By giving your firm a checkup, you can tell where to focus your improvement efforts.

The third part, "Getting Practical," uses the information garnered with the assessment tools to improve your firm's goal setting and implementation, innovation, compensation, and succession planning.

The fourth part, "Putting It All Together," provides a case study and complete analysis of an exemplary firm. Chapter 14 wraps up with concrete guidelines for continuous improvement.

The final part, "Other Audiences," addresses the special interests of consultants, those who perform manager searches, and analysts/portfolio managers who pick stocks for exceptional performance.

Throughout the book, we connect financial results with leadership and culture—the hard with the soft. We know that investment professionals in particular want quantitative evidence that time and attention to the "soft side" will pay off. It's here in spades.

THE RESEARCH PROJECT

In designing our approach to this project, we were heavily influenced by Jim Collins, coauthor (with Jerry Porras) of *Built to Last*[8] and author of *Good to Great*.[9] We knew that investment professionals would be a tough audience when it comes to the qualitative side of the business. Investment professionals have grown up in a culture that worships at the altar of formulas, statistics, and hard data. Jim Collins has done as much as anyone we know to quantify and legitimize the people side of business. Each of his books represents more than five years of research and endless hours of debate over cause and effect, and the validity of the findings. Rather than propose various hypotheses to be proven or disproven, Collins employed an empirical approach. Namely, he and his research team read about and studied the best organizations and their average counterparts to determine the differentiating factors. They looked for recurring themes and patterns that were present in the exemplary companies and absent in the mediocre ones. The result was a set of 21 factors that characterize the *Built to Last* companies.

In our research, we stood on the shoulders of Collins and asked, "Are these same 21 factors valid for investment companies? Or is there something unique about the investment industry (Collins did not examine any pure investment companies) that renders the Collins analysis irrelevant or inapplicable?" To discover answers to these questions, we researched and visited hundreds of investment firms. To our satisfaction, we found that the *Built to Last* principles were alive and well in the investment industry and went a long way toward explaining why certain firms had enjoyed remarkable long-term success.

The proof is always in the pudding. We eat our own cooking, which is to say that we practice these principles in our firm and with our clients. We know that they work. In taking on the challenge of this book project, our intention has been to clearly identify the elements of leadership that contribute significantly to a firm's sustainable success. We present them in a practical way so that you can use them in your firm as well.

JIM WARE
BETH MICHAELS
DALE PRIMER

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We especially want to thank the "contact" people at the investment organizations who set up interviews, sent material, answered questions, filled in details, read and proofread draft versions, and so on. Most of these people are not named in the book and deserve to be named here: Jerry Bartlett, John Cole, Dennis Cook, Barry Gillman, Mark Gilstrap, Jane Hobson, Lisa Jones, Merrillyn Kosier, Isidora Lagos, Mark Toledo, Margaret Welch, John Woerth, and Jamie Ziegler.

We want to thank Lauren Topel for all the work that she did in arranging interviews, travel plans, speaking tours, and so forth. And speaking of speaking, thanks to the Financial Forum Speaking Bureau for their good efforts to help us get the word out to audiences around the world. In the same vein, thanks to Julie Hammond, Lisa Medders, Craig Ruff, and Katy Sherrerd at the Association for Investment Management and Research for their kind invitations to present this material at their conferences and to their member societies around the world. Truly, the feedback from these presentations has shaped and improved the material in this book. We have had running dialogues with people like Alida Carcano, Peggy Eisen, Jane Farris, Dave Fowler, Michael Frazin, Mike Gasior, K. C. Howell, Leandra Knes, Michael Mauboussin, Jeff Pantages, Jonathan Smith, Jay Taparia, Malcolm Trevillian, Steven Waite, and many other CFAs around the world.

We would be remiss in not mentioning our friend and colleague, Ted Aronson, who graciously consulted with us and provided insights and support throughout.

As always, special thanks go to our editor at John Wiley & Sons, Pamela van Giessen, who follows many of the *Built to Last* principles; most notably, she does not micromanage the process! She provides high-level input and lets us research and write as we see fit. The writers out there understand what a blessing this is.

On the production side, we work with a great team: Brooke Graves of Graves Editorial Service, who cleans up the editorial mess we've created; and Jamie Temple of Pageworks, who transforms it into a beautiful hardcover book.

Jim Ware

Jim wishes to thank his wife, Jane, who did more than her share of baby duties with Alexandra (two years) and Nicole (six months) while he sneaked off to read and write. Jim and Jane both want to thank family members Marilyn, Pat, Allene, Wendy, Marta, Mary, and Donna for their help in this regard. We don't know if it takes a village to raise a child, but it certainly takes more than just two sleep-deprived parents! He also wishes to thank his writing partners, Beth and Dale, for their invaluable assistance in collecting the data, designing the structure, writing the material, proofing it, debating and dialoguing, and finally proving that collaboration—while not necessarily the simplest path—is the most rewarding.

Beth Michaels

Helping people achieve their goals is my lifelong passion. This book represents many years of experience with people of all ages working diligently to create their preferred futures. I feel blessed and grateful to have been a part of your successes.

Teamwork and collaboration are at the heart of our work. In that spirit, I wish to thank the people who helped steer my professional growth: Shirley Lewis, Dan Stamp, and in fond memory of Pete Stursberg. To my partners, Dale Primer and Jim Ware, thank you for challenging me, for nurturing me, and for what we have built together.

I wish to thank my clients through the years, from whom I have learned so much and whose partnership I treasure. Learning and growing with you is a joy.

A big thank-you to all the investment firms who opened their doors to us, allowing us access to their inner operations and personal motivations. Your commitment to creating wonderful career experiences and results for clients is inspirational.

Lastly, to my husband and my children, thank you for your patience with me when I blurred the line between work and family time to complete this project. I love you dearly.

Dale Primer

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Betty and Seymour Primer, my parents, for inspiring me through your example of youthful vigor.

My wife and best friend, for being with me and behind me, all the time.

My children, Lisa and David, for bringing heartfelt love, pride, and loyalty continually into my life.

Contents

PART

One

Foundation Pieces: Cornerstones of Long-Term Success

CHAPTER 1

Leadership and Culture in the Investment Industry

The most important lesson I have learned is never to forget that investment management is a people business.

—David Fisher, Chairman, Capital Group Companies[1]

Proactive attention to leadership and culture will help create sustainable success for your organization. To begin, leaders of investment firms must tackle the realities of this industry. This chapter covers:

- The traits of investment professionals and why they create distinct challenges for firm leaders.
- The myths of the financial industry and how they affect success and sustainability.
- The quantifiable difference in business results between firms that attend to leadership and culture practices and those that do not.
- The differences between leading and managing your firm.
- The definition of effective leadership activities.
- The questions that must be answered to distinguish your firm's culture.
- The financial impact of having a flexible culture.

In 1999, "Allstar Capital" was enjoying the fruits of a 17-year bull market. Since 1996, the firm's equity assets had grown from $13 billion to just under $40 billion. The firm's senior leader had become a minor celebrity in the investment field, having been asked to speak at many conferences and having been the subject of several press and trade articles and interviews. He was proud of the firm's success: During the past 20 years, only one investment professional had left for reasons other than retirement. In the past 10 years, no clients had left because of disappointment with his firm's performance. The firm was very profitable and at least 20 of the investment professionals were shareholders of this private firm. The credentials of the staff—MBAs from Harvard, Stanford, and the University of Chicago, plus CFA and CPA designations—were proudly displayed in a booklet in the reception area. The firm's exceptional track record and reputation attracted chunks of money from huge mutual funds, which Allstar Capital managed as a subadvisor. The managing director believed that teamwork accounted for much of the success. He explained in one speech that investment decisions at his firm were made as a team. Leaders at the firm wanted the professional staff to enjoy a "long-term and mutually satisfying relationship."

The Allstar story is a thread that runs through this entire book. (*Note:* Allstar represents a compilation of true stories from different firms with which the authors have had experience.) But why begin a book about investment leadership with a fabulous success story? After all, good news is boring. Everyone knows that there are lots of successful investment firms, making lots of money and keeping their clients happy. What is unique about Allstar Capital?

Its dramatic and complete failure. In 2002, Allstar collapsed. In just three short years, it went bankrupt. The $40 billion had shrunk to $2 billion. Allstar survived only because of an infusion of cash from a merger. Half the staff quit or was fired. Worse yet, one 43-year-old portfolio manager, with a wife and small children, was dead from what seemed to be a stress-induced heart attack. A wonderful success story that had taken more than 20 years to build was gone in what appeared to be the blink of an eye.

That's the point, and that's why we begin the book this way. This book is about *sustainable* success. We've isolated and detailed the critical success factors necessary for investment firms to thrive in the face of difficult market conditions. Bull markets and tech bubbles can hide lots of flaws. Perhaps no other industry is as vulnerable to the sin of hubris as the investment industry. While the Allstar Capitals were sailing, were they good or just lucky? When they failed, were they bad or just unlucky? Did these bright MBAs suddenly get stupid?

To make it crystal clear, Allstar's collapse was *not* caused by criminal acts. It was not an Enron or WorldCom or Andersen. No Allstar employees broke the law or created a scandal. So . . . what factors accounted for its success and then its collapse? How do you build a sustainable organization? What can be learned from Allstar's experience? That's the subject of this book. Our charge is to equip investment leaders, especially the "Bruces" and "Janes" discussed in the preface, with the mental models and tools that will help them create sustainable success.

UNIQUE ATTRIBUTES

Within the topic of strategies for building successful organizations, is there something unusual about the investment industry? In a word, yes. Investment professionals share a unique set of personality traits and personal values. To generalize, professional investors tend to be:

- Independent thinkers (nonconformists).
- Tough-minded (not sentimental).
- Naturally skeptical ("prove it" attitude).
- Anti-authoritarian (don't like to follow rules or sing company songs).
- Creative (question the status quo).
- Conceptual and task-oriented (rather than people-oriented).

When you add these characteristics up, you've got one hell of a management challenge! The television commercial that shows the ranchers herding cats isn't far from the truth.

Patrick O'Donnell, formerly a managing partner with Putnam, described the typical investment professional in similar terms, and noted that anyone charged with managing these folks "certainly needs a management structure that accommodates these individuals—a structure that develops and challenges analysts and one that provides for appropriate evaluation and compensation."[2] With this recognition and these characteristics in mind, we've written this book specifically for this audience. Later in the book we address the personality traits of investment professionals from a more objective, quasi-scientific perspective, using the Myers-Briggs Personality Type Indicator as a psychological measure. For now, let us just say that we know each investment firm will have its own set of challenges based on the people who are attracted to it.

INDUSTRY MYTHS

Before we discuss our findings from extensive research and experience, we begin with several myths—peculiar to the investment industry—that we discovered and shattered during our research of successful firms.

Myth 1: Money is everything

Reality To be sure, investment professionals are fascinated by money, and the industry is clearly one of the most results-driven. Nevertheless, our research shows that the most successful firms do not focus on their own profit. Yes, they are fabulously profitable, but mostly because they focus on their clients and how to serve those clients (namely, through excellent service and performance). In this regard, the best firms reflected Warren Buffett's view: "I love the process more than the proceeds, though I've learned to live with them, too."[3]

When it comes to employee satisfaction and loyalty, again, money is not everything. Yes, compensation is important, but survey results from Capital Resource Advisors show that the two most important factors are leadership credibility and organizational culture and purpose. Other studies, by reputable firms such as Russell Reynolds and Associates, confirm these findings: Money is not the top motivator. Paul Schaeffer, formerly of CRA and now with SEI Investments, summed it up well: "The investment management business is about a lot more than just making money."[4] Compensation becomes a major issue when employees feel that they are not being treated fairly. In this sense, "fairness is everything" does generally hold true in the industry.

Myth 2: Brains are everything

Reality As with Myth 1, many investment firms fail because they believe that sheer intelligence wins out over everything else. These firms recruit the top brains from business schools, pay them top salaries, and then turn them loose on the markets. In our Allstar example, this was the firm's strategy. It worked beautifully right up until the company fell apart.

The best firms realize that brains are enormously important, but also recognize that there is a second, equally important factor: cultural fit. Individuals need to share a sense of common purpose and guiding principles. The best firms hire for skills and fit. Gary Brinson, a legend in the investment business, addressed this myth head-on:

> *Given a choice between a highly talented but introverted, self-serving, and unenthusiastic person and another person who is not as smart but*

> *very enthusiastic, I will choose the enthusiastic person every time. The enthusiastic people may not have the highest test scores or may not have gone to prestigious colleges or universities, but they will fit much better within the culture of our firm.*[5]

Myth 3: We can fix it ourselves

Reality This one is related to Myth 2, as many investment professionals believe that their high IQs will allow them to solve any problem. They don't believe that they need new mental models or advice from outside experts; they just need to turn their powerful brains to the problem at hand, and they will see the solution.

Einstein had a wonderful saying in this regard: "A problem cannot be solved by the same consciousness that created it."[6] Anyone in the investment industry will tell you that there is no shortage of ego among the professionals. Brains and arrogance combine to make it very difficult for investment leaders to ask for help. David Maister, Harvard professor and consultant to professional service firms, has some apt comments about investment professionals:

> *In many professions, especially the advisory professions, clients need trust and reassurance, and, to be successful, professionals must project an air of omnipotence and omniscience. Naturally enough, this manner carries over into other areas of the professional's life and breeds a sense of self-confidence, of mastery, that can handle anything.*[7]

Myth 4: Good performance equals strong culture; bad performance equals weak culture

Reality We have met no one in the investment industry who likes to lose. By definition, this is a competitive group. When we show our culture research to investment professionals, they often react with, "Sure, the culture results look great for those firms; they have terrific performance records!" In other words, culture is seen as a proxy for investment success. Winners are happy people with a strong corporate culture; losers are unhappy people who complain bitterly.

This viewpoint may sound reasonable, and it may align with human nature—but it is not supported by our research. Many firms that we surveyed were in the middle of a very bad stretch of performance, but nonetheless showed remarkably healthy and strong cultures. The adversity had not caused the organization to break down. Alison Winter, executive vice president at Northern Trust, told us, "Of all the things I'm proud of about this team, I'm most proud of the fact that we've stuck together during these tough markets." There's an old saying: Weave your parachute before you have to jump! Alison and her team had created a strong culture before the hard times hit.

Myth 5: Bigger is better

Reality Sandy Weill and others appear to be living out this myth. Their thinking is that strategic acquisitions, huge capital pools, and economies of scale will win the day. Possibly, but our research shows that small and medium-sized firms can establish excellent track records for long-term success, without making any acquisitions. Charles Burkhardt was right when he said, "Investment management is not inherently a scale-oriented profession."[8] Research from Capital Research Advisors bears out this statement, showing that profit margins do not increase with firm size.[9]

Myth 6: Honest guys finish last in the investment business

Reality With Drexel Burnham Lambert, Salomon, and Enron grabbing headlines for their misbehavior, there is a sense that playing it straight is a sure way to miss the glory in the investment business. An old joke in the investment business involves the ethics portion of the Chartered Financial Analyst exam: "What is the correct response to the ethics question?" Answer: "The one that makes the least amount of money." (Tom Bowman is *not* laughing. . . .) In sharp contrast to the jokes, stereotypes, and general perceptions, we found that the best firms are fanatical about ethical behavior. Each of them had stories about turning away a profitable deal because it would have compromised their values.

Myth 7: Investment firms are unique and need different rules

Reality The suggestion inherent in this myth is that the nature of the industry, and the nature of its professionals, are sufficiently different from any other industry to warrant a different set of rules. We were open to this possibility as we performed our research. What we found, though, is that the same principles that drive other successful organizations hold true for investment firms as well. Human nature is, after all, human nature. Rather than say that investment firms require different rules, we believe that the same rules apply—but in some cases face unique obstacles. One of the reasons we wrote this book was to address these obstacles: How do you apply the time-tested principles of leadership and culture to the investment industry?