



The Three Financial Styles of Very Successful Leaders

Strategic Approaches to Identifying the Growth Drivers of Every Company

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Introduction

Why do some CEOs succeed? And why do so many CEOs fail?

Many of the failures can't be chalked up to inexperience, since the leaders are sophisticated executives, often veterans of large, successful enterprises, and often selected by their companies for their overall competence, drive and passion. They were enormously successful in other enterprises and environments and were fully expected to be brilliantly successful in their new posts. But they weren't.

The answer lies in the leaders' personal financial traits. Leaders have widely different approaches to the way they approach the building of value. Top executives have characteristic financial traits, just as they have other traits, such as aggression, drive and execution. These financial behaviors are linked to corporate outcome and to the company's street or market value.

These personal financial traits can be referred to as a leader's financial signature. A leader leaves an indelible mark on his or her company through this financial signature. It's like a hidden personality that no one, not even the leader, is generally aware of. By understanding leaders' financial signatures and styles, we can potentially avoid many mistakes and provide them a more supportive en-

vironment. We can also hire the leaders who are most likely to succeed.

Financial Signatures

A financial signature is a behavioral imperative, an innate way of dealing with finances. The two characteristics of a financial signature are resource utilization and value adding. All leaders have an inborn calculus for evaluating risk/reward characteristics and the resource utilization requirements of situations.

Resource utilization comes down to money, essentially — how leaders spend or conserve it. Value adding deals with the extras companies try to provide their customers, from software upgrades to additional product features to service extras such as free delivery or guarantees. These two drivers lead to specific patterns of performance for the company.

Research by the Perth Leadership Institute shows that a leader's financial style has a greater effect on an organization's success or failure than other corporate or external factors. Put another way, a leader's financial style is at least as important as the company's product, marketing, pricing strategies, technology and strategic plans.

Financial signatures can be measured using just two simple metrics. For determining the health of the company, and the value a leader has added, the

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measure is the gross margin — the difference between revenues and the direct costs of gaining those revenues. In effect, it's a measure of earnings potential. The higher the gross margin, the higher the level of value the company possesses. It's possible to find out gross margins for specific companies and industries, which gives the basis for comparing leaders, not only from organizations but also among markets, on the concept of value adding.

There's also a metric, although not quite so clear-cut, to measure a leader's resource utilization: company expenses as a proportion of revenue. Although, like earnings, expenses are easy to manipulate, the term is easily understood and is an acceptable measure of resource utilization.

The Nine Financial Missions

Leaders can be grouped into nine basic categories, based on whether they're high, medium or low in their intensity level on the two key drivers: value adding (V) and resource utilization (R). Each of the signatures represents a financial preference — a financial mission. It expresses a leader's built-in calculator for achieving profitability.

- **Venture capitalist (High V/High R).** A venture capitalist does things the hard way, investing in things with high value and gross margins, understanding that it will require high expenditures and investment for several years for the company and product to mature. If the investment pays off, the venture capitalist will reap substantial financial rewards. But in the vast majority of cases he or she will fail. It's a risky approach with no easy answers because the path of increasing value requires high expenses — there are no shortcuts.

- **Profiteer (HV/MR).** The profiteer is essentially a cheap venture capitalist, aiming for high value adding but without the same high resource utilization. Instead, the profiteer shoots for a lower-risk product or service but with high gross margins. The profiteer will typically aim for a product with shorter development cycles that provide some cash in the relatively short term, even if that means some reduction in gross margins. But the aim is to make a lot of money with a high-gross-margin style coupled with medium levels of resource allocation. This leader is often a reliable money-maker.

- **Buccaneer (HV/LR).** The buccaneer enjoys very high returns for very low expenditures. Typically, the buccaneer figures out how to achieve high returns on investment by means no one has thought of before, so he or

she has few competitors. A buccaneer won't spend many years developing a product or service — he or she doesn't typically have the patience to do that. The focus is on high gross margins and low resource yield — a difficult feat to pull off, but some leaders and enterprises achieve it, to the delight of their shareholders.

- **Conglomerator (MV/HR).** The conglomerator uses a hybrid financial approach that fits between the high- and low-gross-margin types. His or her product is usually not particularly well differentiated, but it isn't a commodity either. Often the conglomerator, as the name implies, has built up a portfolio of products and services, either through internal development or acquisitions. Together, those meet the medium levels of value-adding and gross-margin characteristics of the signature. However, this approach involves high expenses because of the cost of building the product portfolio, the cost of acquiring the portfolio, or both. The conglomerator's financial signature therefore leads to high expenses that aren't totally offset by the gross margins the company generates. It's a speculative approach that relies on the balance of the portfolio to generate enough revenue growth and market share to keep the company in the black.

- **Consolidator (MV/MR).** The consolidator is a middle-of-the-road, fairly cautious leader. He or she isn't a big-picture thinker or strategist but shies away from cut-throat, low-margin businesses. He or she invests just enough to keep gross margins up. As befits the title, the consolidator consolidates organizationally and product-wise. He or she isn't particularly innovative, preferring to add rather than to develop. That makes the consolidator

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not very exciting, with unspectacular, albeit rather changeable, returns.

- **Arbitrageur (MV/LR).** The arbitrageur seeks opportunities carrying decent returns without much risk. He or she leverages low-cost opportunities so as to make profits on the medium-sized gross margins that will be generated. The arbitrageur is focused on return on investment, but not so much that he or she will spend more than the absolute minimum to pursue the opportunity. The arbitrageur cannot be found in mass-market retail or other commodity products — they don't bring high enough returns.

- **Mercantilist (LV/HR).** The mercantilist financial mission represents the leader who uses a high level of resources but isn't particularly focused on adding value to products. He or she may invest in sales and marketing, or in general and administrative expenses, or even in research and development, but not to add any value. The mercantilist looks for ways for high levels of resource utilization to lead to company returns without product intensity, usually by increasing market share. This, of course, is risky. If the high investments don't pay off, the relatively low gross margins reaped by the company aren't going to bail it out, and it will have major problems.

- **Trader (LV/MR).** The trader is typically a leader in a small company who lacks the resources of a big company and has to pursue projects without much available funding. Like the mercantilist, the trader is low on the value-adding scale, buying low-value products cheaply and selling them for a high enough gross margin to cover costs and any deficit from his or her investment

activities. The trader must constantly speculate to ensure the two are kept in balance to generate some kind of earnings.

- **Discounter (LV/MR).** The discounter is a risk-averse leader who never speculates. His or her very low levels of added value are offset by extreme thriftiness. The discounter is generally not focused on adding value to products *per se*. The discounter tends to the details and is very control-oriented — he or she doesn't focus on the big picture. This type of leader is more concerned about points of market share and gross margin than dominating the market. The emphasis is on lowering resource use to match the gross margin.

Mission and Signature

The nine different financial missions represent nine different ways companies can create value. Each reflects different choices that lead to different financial performance patterns. Organizations are invariably unaware of the financial signatures of their leaders or the members of their top management teams. Yet those financial signatures drive the entire financial culture of the organization, its financial strategies, and ultimately its financial performance. Only by understanding the leader's financial signature can we understand the financial mission.

There's an important difference between a financial signature and financial mission. A financial signature is fixed; a financial mission is not. A financial signature expresses itself in behavior — that behavior constitutes your financial mission. You can't change your innate financial signature but you can change your financial mission and behavior, adjusting them as your experience dictates.

The Three Financial Styles

The nine different financial missions a leader can follow can be reduced to three financial styles: surplus, deficit and puzzler.

Leaders who have a surplus style are consistently profitable in the long term. Deficit leaders are consistently unprofitable in the long term — although they can be profitable in the short term — by virtue of their financial signature and mission. Puzzler leaders generate zero earnings over the long term, although their short-term results can be all over the board, including being profitable.

The three styles that generate positive earnings gaps are:

- **Buccaneer (HV/LR).** With value adding high and



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resource utilization low, a pattern develops of fast growth and rising earnings. Sandy Weill of Citigroup and Pierre Omidyar and Jeff Skoll of eBay are examples of the buccaneer style.

- **Profiteer (HV/MR).** Through high value adding and medium resource utilization, this style leads to gently rising growth and earnings. Jim Kilts of Gillette is an example of the profiteer style.

- **Arbitrageur (MV/LR).** This leads to a positive earnings gap as value adding is medium but resource utilization is low. Growth can be slow and earnings increases are moderate. Rupert Murdoch of News Corp. is an example of the arbitrageur style.

The three styles that generate no earnings gap are:

- **Venture Capitalist (HV/HR).** With the leader high on both value adding and resource utilization, the company shows an inconsistent pattern of growth and earnings. Growth occasionally spikes but also declines a virtually equivalent number of times. An example of the venture capitalist style is Paul Allen of Interval Research, who was Bill Gates' original partner in Microsoft.

- **Discounter (LV/LR).** While both resource utilization and value adding are low, growth and earnings are inconsistent. In the short term, there may be periods of apparent survival but over the long term death is inevitable. An example of the discounter style is Bernard Ebbers of WorldCom.

- **Consolidator (MV/MR).** Both resource utilization and value adding are at medium levels but growth and earnings are inconsistent. The company shows periods of both growth and decline, which averages out over the long term. An example of the consolidator style is Leland Brendsel, the former CEO of Freddie Mac.

The three styles that generate negative earnings gaps are:

- **Mercantilist (LV/HR).** This style creates a large earnings gap as resource utilization is high while value adding is low, leading to a fast decline in growth and earnings and often to company failure. Dennis Kozlowski at Tyco was an example of the mercantilist style.

- **Trader (LV/MR).** With resource utilization medium while value adding is low, the company experiences a slow decline in growth and earnings. An example of the trader style is William Clay Ford, CEO of Ford Motor Co.

- **Conglomerator (MV/HR).** High resource utilization

and medium value adding lead to declining growth and earnings over the long term, although short-lived earnings spikes may also occur. An example of the conglomerator style is Robert Allen's tenure as chair of AT&T.

Conclusion

Companies need to be sensitive to the financial signatures and missions of their leaders. The needs of companies can differ depending on the specific situation of the company and the stage of its life cycle. It's important to understand the financial style of the leader, and how it relates to the business strategy the company seeks. **e**

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