Introduction

An Intelligent Iconoclasm

It is impossible to produce superior performance unless you do something *different*.

—*John Templeton*

The New Yorker's Atul Gawande uses the term *positive deviant* to describe unusually effective performers in the field of medicine. To Gawande, it is natural that we should study these outliers in order to learn from them and improve performance.[1]

Surprisingly, in business the best are not studied as closely as in other fields like medicine, the law, politics, or sports. After studying Henry Singleton, I began, with the help of a talented group of Harvard MBA students, to look for other cases where one company handily beat both its peers and Jack Welch (in terms of relative market performance). It turned out, as Warren Buffett's quote in the preface suggests, that these companies (and CEOs)

were rare as hen's teeth. After extensive searching in databases at Harvard Business School's Baker Library, we came across only seven other examples that passed these two tests.

Interestingly, like Teledyne, these companies were not generally well known. Nor were their CEOs despite the enormous gap between their performance and that of many of today's high-visibility chief executives.

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The press portrays the successful, contemporary CEO, of which Welch is an exemplar, as a charismatic, action-oriented leader who works in a gleaming office building and is surrounded by an army of hardworking fellow MBAs. He travels by corporate jet and spends much of his time touring operations, meeting with Wall Street analysts, and attending conferences. The adjective *rock star* is often used to describe these fast-moving executives who are frequently recruited into their positions after well-publicized searches and usually come from top executive positions at well-known companies.

Since the collapse of Lehman Brothers in September 2008, this breed of high-profile chief executive has been understandably vilified. They are commonly viewed as being greedy (possibly fraudulent) and heartless as they fly around in corporate planes, laying off workers, and making large deals that often destroy value for stockholders. In short, they're seen as being a lot like Donald Trump on *The Apprentice*. On that reality television show, Trump makes no pretense about being avaricious, arrogant, and promotional. Not exactly a catalog of Franklinian values.

The residents of Singletonville, however, represent a refreshing rejoinder to this stereotype. All were first-time CEOs, most with very little prior management experience. Not one came to the job from a high-profile position, and all but one were new to their industries and companies. Only two had MBAs. As a group, they did not attract or seek the spotlight. Rather, they labored in relative obscurity and were generally appreciated by only a handful of sophisticated investors and aficionados.

As a group, they shared old-fashioned, premodern values including frugality, humility, independence, and an unusual combination of conservatism and boldness. They typically worked out of bare-bones offices (of which they were inordinately proud), generally eschewed perks such as corporate planes, avoided the spotlight wherever possible, and rarely communicated with Wall Street or the business press. They also actively avoided bankers and other advisers, preferring their own counsel and that of a select group around them. Ben Franklin would have liked these guys.

This group of happily married, middle-aged men (and one woman) led seemingly unexciting, balanced, quietly philanthropic lives, yet in their business lives they were neither conventional nor complacent. They were positive deviants, and they were deeply iconoclastic.

The word *iconoclast* is derived from Greek and means "smasher of icons." The word has evolved to have the more general meaning of someone who is determinedly different, proudly eccentric. The original iconoclasts came from outside the societies (and temples) where icons resided; they were challengers of societal norms and conventions, and they were much feared in ancient

Greece. The CEOs profiled in this book were not nearly so fearsome, but they did share interesting similarities with their ancient forbears: they were also outsiders, disdaining long-accepted conventional approaches (like paying dividends or avoiding share repurchases) and relishing their unorthodoxy.

Like Singleton, these CEOs consistently made very different decisions than their peers did. They were not, however, blindly contrarian. Theirs was an *intelligent iconoclasm* informed by careful analysis and often expressed in unusual financial metrics that were distinctly different from industry or Wall Street conventions.

In this way, their iconoclasm was similar to Billy Beane's as described by Michael Lewis in *Moneyball*.[2] Beane, the general manager of the perennially cash-strapped Oakland A's baseball team, used statistical analysis to gain an edge over his better-heeled competitors. His approach centered on new metrics—on-base and slugging percentages—that correlated more highly with team winning percentage than the traditional statistical troika of home runs, batting average, and runs batted in.

Beane's analytical insights influenced every aspect of how he ran the A's—from drafting and trading strategies to whether or not to steal bases or use sacrifice bunts in games (no, in both cases). His approach in all these areas was highly unorthodox, yet also highly successful, and his team, despite having the second-lowest payroll in the league, made the playoffs in four of his first six years on the job.

Like Beane, Singleton and these seven other executives developed unique, iconoclastic approaches to their businesses that drew much comment and questioning from peers and the business press. And, like Beane's, their results were exceptional, hand-

ily outperforming both the legendary Welch and their industry counterparts.

They came from a variety of backgrounds: one was an astronaut who had orbited the moon, one a widow with no prior business experience, one inherited the family business, two were highly quantitative PhDs, one an investor who'd never run a company before. They were all, however, new to the CEO role, and they shared a couple of important traits, including fresh eyes and a deep-seated commitment to rationality.

Isaiah Berlin, in a famous essay about Leo Tolstoy, introduced the instructive contrast between the "fox," who knows many things, and the "hedgehog," who knows one thing but knows it very well. Most CEOs are hedgehogs—they grow up in an industry and by the time they are tapped for the top role, have come to know it thoroughly. There are many positive attributes associated with hedgehogness, including expertise, specialization, and focus.

Foxes, however, also have many attractive qualities, including an ability to make connections across fields and to innovate, and the CEOs in this book were definite foxes. They had familiarity with other companies and industries and disciplines, and this ranginess translated into new perspectives, which in turn helped them to develop new approaches that eventually translated into exceptional results.

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In the 1986 Berkshire Hathaway annual report, Warren Buffett looked back on his first twenty-five years as a CEO and concluded that the most important and surprising lesson from his career to date was the discovery of a mysterious force, the corporate

equivalent of teenage peer pressure, that impelled CEOs to imitate the actions of their peers. He dubbed this powerful force the *institutional imperative* and noted that it was nearly ubiquitous, warning that effective CEOs needed to find some way to tune it out.

The CEOs in this book all managed to avoid the insidious influence of this powerful imperative. How? They found an antidote in a shared managerial philosophy, a *worldview* that pervaded their organizations and cultures and drove their operating and capital allocating decisions. Although they arrived at their management philosophies independently, what's striking is how remarkably similar the ingredients were across this group of executives despite widely varying industries and circumstances.

Each ran a highly decentralized organization; made at least one very large acquisition; developed unusual, cash flow–based metrics; and bought back a significant amount of stock. None paid meaningful dividends or provided Wall Street guidance. All received the same combination of derision, wonder, and skepticism from their peers and the business press. All also enjoyed eye-popping, credulity-straining performance over very long tenures (twenty-plus years on average).

The business world has traditionally divided itself into two basic camps: those who run companies and those who invest in them. The lessons of these iconoclastic CEOs suggest a new, more nuanced conception of the chief executive's job, with less emphasis placed on charismatic leadership and more on careful deployment of firm resources.

At bottom, these CEOs thought more like investors than managers. Fundamentally, they had confidence in their own analyti-

A Distant Mirror: 1974–1982

In assessing the current relevance of these outsider CEOs, it's worth looking at how each navigated the post–World War II period that looks most like today's extended economic malaise: the brutal 1974–1982 period.

That period featured a toxic combination of an external oil shock, disastrous fiscal and monetary policy, and the worst domestic political scandal in the nation's history. This cocktail of negative news produced an eight-year period that saw crippling inflation, two deep recessions (and bear markets), 18 percent interest rates, a threefold increase in oil prices, and the first resignation of a sitting US president in over one hundred years. In the middle of this dark period, in August 1979, *BusinessWeek* famously ran a cover story titled "Are Equities Dead?"

The times, like now, were so uncertain and scary that most managers sat on their hands, but for all the outsider CEOs it was among the most active periods of their careers—*every single one* was engaged in either a significant share repurchase program or a series of large acquisitions (or in the case of Tom Murphy, both). As a group, they were, in the words of Warren Buffett, *very* "greedy" while their peers were deeply "fearful."[a]

a. Author interview with Warren Buffett, July 24, 2006.

cal skills, and on the rare occasions when they saw compelling discrepancies between value and price, they were prepared to act boldly. When their stock was cheap, they bought it (often in large quantities), and when it was expensive, they used it to buy other companies or to raise inexpensive capital to fund future growth.

If they couldn't identify compelling projects, they were comfortable waiting, sometimes for very long periods of time (an entire decade in the case of General Cinema's Dick Smith). Over the long term, this systematic, methodical blend of low buying and high selling produced exceptional returns for shareholders.

This reformulation of the CEO's job stemmed from shared (and unusual) backgrounds. All of these CEOs were outsiders. All were first-time chief executives (half not yet forty when they took the job), and all but one were new to their industries. They were not bound by prior experience or industry convention, and their collective records show the enormous power of fresh eyes. This freshness of perspective is an age-old catalyst for innovation across many fields. In science, Thomas Kuhn, inventor of the concept of the *paradigm shift,* found that the greatest discoveries were almost invariably made by newcomers and the very young (think of the middle-aged former printer, Ben Franklin, taming lightning; or Einstein, the twenty-seven-year-old patent clerk, deriving $E = mc^2$).

This fox-like outsider's perspective helped these executives develop differentiated approaches, and it informed their entire management philosophy. As a group, they were deeply independent, generally avoiding communication with Wall Street, disdaining the use of advisers, and preferring decentralized organizational structures that self-selected for other independent thinkers.

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In his recent bestseller, *Outliers,* Malcolm Gladwell presents a rule of thumb that expertise across a wide variety of fields requires ten

thousand hours of practice.[3] So how does the phenomenal success of this group of neophyte CEOs square with that heuristic? Certainly none of these CEOs had logged close to ten thousand hours as managers before assuming the top spot, and perhaps their success points to an important distinction between expertise and innovation.

Gladwell's rule is a guide to achieving mastery, which is not necessarily the same thing as innovation. As John Templeton's quote at the beginning of this chapter suggests, exceptional relative performance demands new thinking, and at the center of the worldview shared by these CEOs was a commitment to rationality, to analyzing the data, *to thinking for themselves*.

These eight CEOs were not charismatic visionaries, nor were they drawn to grandiose strategic pronouncements. They were practical and agnostic in temperament, and they systematically tuned out the noise of conventional wisdom by fostering a certain simplicity of focus, a certain *asperity* in their cultures and their communications. Scientists and mathematicians often speak of the clarity "on the other side" of complexity, and these CEOs—all of whom were quantitatively adept (more had engineering degrees than MBAs)—had a genius for simplicity, for cutting through the clutter of peer and press chatter to zero in on the core economic characteristics of their businesses.

In all cases, this led the outsider CEOs to focus on cash flow and to forgo the blind pursuit of the Wall Street holy grail of reported earnings. Most public company CEOs focus on maximizing quarterly reported net income, which is understandable since that is Wall Street's preferred metric. Net income, however,

is a bit of a blunt instrument and can be significantly distorted by differences in debt levels, taxes, capital expenditures, and past acquisition history.

As a result, the outsiders (who often had complicated balance sheets, active acquisition programs, and high debt levels) believed the key to long-term value creation was to optimize free cash flow, and this emphasis on cash informed all aspects of how they ran their companies—from the way they paid for acquisitions and managed their balance sheets to their accounting policies and compensation systems.

This single-minded cash focus was the foundation of their iconoclasm, and it invariably led to a laser-like focus on a few select variables that shaped each firm's strategy, usually in entirely different directions from those of industry peers. For Henry Singleton in the 1970s and 1980s, it was stock buybacks; for John Malone, it was the relentless pursuit of cable subscribers; for Bill Anders, it was divesting noncore businesses; for Warren Buffett, it was the generation and deployment of insurance float.

At the core of their shared worldview was the belief that the primary goal for any CEO was to optimize long-term value *per share,* not organizational growth. This may seem like an obvious objective; however, in American business, there is a deeply ingrained urge to get *bigger.* Larger companies get more attention in the press; the executives of those companies tend to earn higher salaries and are more likely to be asked to join prestigious boards and clubs. As a result, it is very rare to see a company proactively shrink itself. And yet virtually all of these CEOs shrank their share bases significantly through repurchases. Most also shrank their operations through asset sales or spin-offs, and they were not

shy about selling (or closing) underperforming divisions. Growth, it turns out, often doesn't correlate with maximizing shareholder value.

This pragmatic focus on cash and an accompanying spirit of proud iconoclasm (with just a hint of asperity) was exemplified by Henry Singleton, in a rare 1979 interview with *Forbes* magazine: "After we acquired a number of businesses, we reflected on business. Our conclusion was that the key was cash flow. . . . Our attitude toward cash generation and asset management came out of our own thinking." He added (as though he needed to), "It is *not* copied."[4]