
There are seven CEOs working for your organization today— do you know who they are and do you know what to do?

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You have a relatively new CEO. Fifty-seven years young. Became CEO a year and a half ago at 56. Doing well. Came from inside. Consensus choice. Replaced a great decade long CEO.

She has confided in the board that she will step down as CEO when she is 62. Assuming her party wins the election, she has plans for public service and is slated for a post as ambassador in the country she and her family love and want to retire in.

That means that you, she and the board have five years to find and prepare her replacement. A replacement that will face a tougher, more competitive world with global challenges and increasingly complex issues.

Why might this be difficult?

Why is it that companies come up short when it comes to this straightforward replacement challenge? Study after study shows that companies simply aren't adequately prepared for CEO succession. Here's a sample of some recent failure-to-plan findings:

- A survey by the National Association of Corporate Directors, according to Charan (2005), reports that almost 50 percent of the companies with revenues over \$500 million have no CEO succession plan. Charan also reports on another study—The Corporate Leadership Council's—that surveyed 276 large companies in 2004 and found that only 20 percent of respondents were satisfied with their CEO succession planning process.
- In a Hewitt study, 95 percent of the Top 20 companies identify high potentials versus only 77 percent of the non-Top 20. And 100 percent use the succession planning process to choose senior managers versus 86 percent of non-Top 20 companies. (*Hewitt, 2005*)

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- A DBM study (Drake Beam Morin, 2002) found that only 2 percent of the companies surveyed rated their succession planning efforts as excellent; two-thirds rated them as fair or worse.
- Pricewaterhouse Coopers' latest survey of CEOs in 364 of the fastest growing companies found that, of the 42 percent who said they would be stepping down in the next five years, only 22 percent had given succession planning a lot of thought and 19 percent said they hadn't thought at all about their successor. (*Industry Week*, 2005, March).
- An interesting finding...while only 39 percent of the CEOs have picked a likely successor, 45 percent have a disaster contingency plan that kicks in if they're unable to lead; 60 percent have an estate plan that addresses disposition of their company if they die—and 85 percent of those have updated that plan in the past five years. The current CEOs are planning for disaster but not traditional succession—a much more likely scenario.
- A recent article in *Nonprofit World* (Santora, 2004, July/August) revealed that less than 50 percent of nonprofits plan for leadership succession.

Some CEO trends...

A little more background...there are some trends we all have to deal with.

The top job is taking a toll...

First, there is the retiring baby boomers trend. A significant portion of managers and executives will be retiring in the next 7 to 10 years. Most organizations that have done actuarial studies found that portion to be over 50 percent. And CEOs are retiring at increasingly younger ages. Lucier, Schuyt, & Tse (2005) noted in the Booz Allen Hamilton 2004 CEO study that 17.5 percent of the CEOs who retired in 2004 were 55 or younger, representing a 61 percent increase from 2003.

The job is getting tougher...

Second, the work itself is getting tougher. It's getting more global. More competitive. Faster. Competitive edges have a shorter half-life. Large third-world markets are beginning to flex their lower labor rates muscles. China and India are rising. South America and Africa might be next.

First-time tough-job managers are stumbling...

Third, the average age at which people get their first significant jobs is decreasing—they're moving into tougher jobs earlier in their careers with less experience. Bunker, Kram & Ting (2002) talk about this phenomenon in their *Harvard Business Review* article, "The Young and the Clueless." But unfortunately, what will inevitably happen is that these first-time tough-

job managers will stumble and fail at a greater rate than their predecessors. They will have less experience going in than their elders. The derailment rate will increase.

Increasing failure and decreasing tenure...

Fourth, are the increasing failure rates—with corresponding decreasing tenure rates—of new CEOs. Here are the alarming statistics:

- A Booz Allen Hamilton study (Charan, 2005) found that the average global tenure for CEOs is 7.6 years, almost two years less than it was in 1995 when the average tenure was 9.5 years.
- An MIT study found that CEOs appointed after 1985 were three times more likely to be fired than those appointed to CEO before 1985. (Bennis, 2001)
- In his *Harvard Business Review* article, Ciampa (2005) found that two of every five new CEOs fail within the first 18 months of their tenure.
- A Drake Beam Morin study (Drake Beam Morin, 2002) that analyzed CEO turnover for 2000 and 2001 in 481 of the world's largest public and private companies found that 30 percent of the companies studied changed CEOs at least once during those years. 58 percent had changed CEOs at least once in the last four years—from 1998 to 2001. The study also revealed that the average tenure for CEOs, as of December 31, 2001, was only 2.75 years, a decrease from their 1999 CEO study when the median CEO tenure was between three and four years.
- CEO tenure is the shortest in Europe and Asia, according to research by Lucier, Schuyt, & Tse (2005). At 16.8 percent, Europe's CEO turnover rate is 425 percent higher than it was in 1995. At 17.5 percent, the non-Japanese Asia turnover rate is 256 percent higher than it was in 1995.
- The DBM CEO study (Drake Beam Morin, 2002) had similar findings—they reported that the median CEO tenure in France is four to five years, three years in the U.S., and two to three years in Japan and the United Kingdom. Only 16 percent of CEOs in Asia and Australia had been in that role for five years or more, compared to 28 percent in both North and South America, and 32 percent in Europe.
- A unique phenomenon in Japan: 70 percent of the CEOs in Japan had been with the company for 35 years before becoming CEO but 41 percent had held their position for less than two years (compared to 34 percent overall); and 16 percent had been in the position for five years or more (compared with 30 percent overall); and 6 percent had been in office for ten years or more (compared with 13 percent overall).

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The interesting aspect of all of this failure is that there's often not anything the CEO can do to fix things. A study by Khurana (2002) found that 30 percent to 45 percent of a CEO's performance is attributed to industry effects, and 10 percent to 20 percent can be attributed to year-to-year changes in the economy. So, depending on the circumstances, over 50% of a company's performance might be *outside of the control of the CEO*.

CEO involvement in succession planning...

Fifth, is the trend to involve the CEO in his or her own succession planning. According to Hewitt's study of the Top 20 companies in leadership development, the current CEO was involved in his/her own succession planning in 100 percent of the Top 20 companies and in only 37 percent of the non-Top 20. Ninety-five percent of the Top 20 holds the CEO accountable for developing his/her successor and succession team. And the CEO is involved in succession planning in 54 percent of companies with an above-median ROE—versus 28 percent of companies with below-median ROE. (*HR Focus*, 2004)

Performance-related succession...

Finally, the number of CEOs being forced to resign is growing. And it's probably not for the reasons you think. Most CEOs are fired for underperformance and not because of ethical or legal or political reasons. They're also not being forced to resign as a result of mergers and acquisitions. According to a recent survey (*Leadership IQ*, 2005) of 1087 Board Members who have fired CEO's, the reasons were, 1. The inability to bring about needed change (31%), Alienating or ignoring key customers (28%), tolerating poor performers in the organization (27%), denying or not facing up to reality (23%) and poor execution (22%).

The Drake Beam Morin two-year CEO study (DBM, 2002) found that only 25 percent of CEOs had left office because of mergers and acquisitions compared to the 48 percent who left office in the two previous years. Further, only one in eight CEOs in companies that had been acquired became CEO of the new combined organization.

In Booz Allen Hamilton's annual study, *CEO Succession 2004* (Lucier, Schuyt, & Tse, 2005), the authors found that the number of CEOs forced to resign for performance-related reasons increased 44 percent from 2003. That figure, a result of a study of 2,500 of the world's largest companies, represented 31.4 percent of all CEO departures in 2003.

Some industries were more susceptible to forced CEO resignations than others. According to Lucier et al. (2005), information technology had the highest rate of turnover (44.8 percent of all CEO successions.)

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The pace is picking up in Europe for performance-related terminations—42 percent of CEOs were forced to resign in Europe in 2004 versus 31 percent in the U.S. And they're given less of a chance to prove themselves, too. (Lucier et al., 2005)

In the U.S., under-performing CEOs were forced to resign after 5.2 years; in Europe in 2.5 years. Asia/Pacific had the highest succession rate with 17.5 percent changing their CEO in 2004—an increase of 230 percent over 2003; Europe was next with 16.8 percent; Japan with 15.5 percent and North America with 11.7 percent. (Lucier et al., 2005). The study also points out that this high turnover rate now almost matches the overall employee turnover rate for U.S. companies, 12 percent per year.

A question of supply and demand?

What is the result of all this turnover and failure, or perceived failure? Simple. The supply of people able to run large, global, diverse and consolidated organizations is short of the need. There are more jobs to fill than there are exciting, proven candidates.

Where are the CEOs coming from and why does it matter?

More and more companies are going outside to fill their CEO positions, with often mediocre effects. Here are the inside/outside hire (and fire) stats:

- An article in *Directorship* (Cohn & Khurana, 2003) reported on a long-term study of CEO succession planning and found that the percentage of outside versus inside CEO selections from 1980 to 2000 changed from 7 percent to 50 percent. Another sign of the lack of an internal succession plan.
- A 1999 survey found that 37 percent of the top executive positions were filled from outside. (Zhang & Rajagopalan, 2003)
- In *Good to Great*, Collins (2001) noted that ten of the eleven companies who jumped from good to great had internal CEO succession candidates.
- Charan (2005) reports on a study by Burson-Marsteller that found that over 37 percent of Fortune 1000 companies were outside hires. He notes that Booz Allen Hamilton's 2003 report found that 55 percent of the U.S. CEOs who were forced to resign were outsiders (34 percent were insiders); 70 percent of the European CEOs forced to resign were outsiders. And, reporting on the Corporate Leadership Council (CLC) study, Charan notes that 45 percent of respondents said they chose an outsider because it "would take too long or be too expensive to develop successors internally." (p. 75.) And, only 24 percent of the respondents think their development efforts are aligned with the organization's strategic goals.

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- In their two-year CEO study, (Drake Beam Morin, 2002) DBM found that 86 percent of the organizations they studied appointed their CEOs from inside the company—most of them were senior executives—29 percent were Chief Operating Officers, 13 percent were Presidents. This varies a little by industry: 25 percent in retail trade, and 23 percent in the transportation, communication, electric and gas group, came from outside the company compared to 14 percent overall. And 59 percent who hired outsiders chose executives who were CEOs at other companies.
- Leonard (2001) suggests that it takes 18 months for CEOs to get up to speed on all of the job's complexities and four to seven years in large organizations for change to take hold.
- A Booz Allen Hamilton study (Lucier et al., 2005) found that, for the first time since 1995, CEO outsiders in North America outperformed insiders (6.8 percent outsiders versus 5.6 percent insiders). The same was not true in Europe, however, where insider CEOs outperformed outsiders by 6 percentage points. The figures also show consistency in performance between first and second half of the CEO's tenure: Outsiders produced 5.1 percent higher returns than insiders during the first half of their tenures while insiders produced 4.7 higher returns than outsiders.
- Lucier et al. (2005) found that CEOs who were forced to resign generated returns that were 7.7 percent lower than CEOs who left voluntarily. A related finding is that outsider CEOs joined companies whose shareholder returns were 5.2 percentage points lower than for companies that promoted insiders.

Four things we need to know about CEOs in waiting...

Here are four things we need to know about CEO candidates. Before we can determine if they are viable candidates, we need to know their:



1. **Ability to perform across diverse challenges.** (The younger the candidate, the tougher it is to estimate this measure of potential.)
2. **Motivation to succeed** (what Jim Collins (2001) calls a passion for results.)
3. **Willingness to move around the globe** (Ramping up for the CEO role usually requires one or more out-of-home-country assignments.)
4. **Potential to learn new perspectives and skills** that will be needed for future success.

Some things are easier to assess than others.

Candidate's age	Ability to perform across Challenges?	Motivation to succeed?	Willingness to move?	Potential to learn?
50's	Easiest	Known	Real	Easy
40's	Moderate	Known	Known	Easy
30's	Hard	Clearer	Actual	Easier
20's	Hardest	Unfocused	Intention	Hardest

The succession line of the next 6 CEO's starts here...

First in line at about 50...

Under ideal conditions, wanting to promote from within, that person should work for you today. He or she is around 50—the normal accession range is 46—52 according to Charan, (2005)—and already a proven performer: Has had multiple assignments. Been in more than one function, geography and line of business. Been with a couple of companies before joining yours. Probably has been in one or more international assignments. He or she is an officer, well known by the board and waiting in the wings to be called. There is one other competitor but, if things stay the same, it isn't a real contest. The competitor is expected to leave when the announcement is made. Unfortunate but usual.

Under the same ideal conditions, the next four CEOs are already working for you.

Next in line at 42...

The next one is about 42. Noticeably, a strong performer. In his or her first significant general manager job. Promoted ahead of others of the same class year. Needs some "finishing school" assignments. Hasn't had an international assignment. Known by some senior executives and board members but not all.

And at 35...

The next is about 35. Has left some performance tracks in the sand. Spent about five years with another company in another country before joining yours. A foreign national. Has done well in several areas. Raw talent. Has a lot of work to do on him or herself and needs a lot more diverse experience to get prepared to be an officer. Performance across diverse challenges is still unproven. Hasn't had an international assignment with your organization. Open but skeptical to another significant move. A few in top management know about this person.

Next at 28...

Although young, this 28-year-old has already done extremely well in two assignments. A result of an intense recruiting campaign at the best schools. A minority. Speaks Chinese. In first management job and poised for more. Performance in tougher jobs is an open question. Willing to move anywhere for growth and development. Name hasn't surfaced yet in the enterprise succession system. Only known by close-in management.

And at 23...

Next, there is a 23-year-old MBA who has just joined the organization. Good school. Great grades. Two internships—one with your organization. Speaks two additional languages (Spanish and French); studied in France for a semester. Very self-confident. Aside from assumed potential, little is known about ability to perform.

Finally, at 18...

Finally, there is an 18-year-old summer intern. Good school. Great grades. Speaks Chinese. International Business major. Very mature and poised. Parents are both executives in large name companies. Two siblings are also at work in large companies. Everybody who knows him or her is very impressed. Local management wants to lock them in for further internships and offer to pay for further schooling.

Job One: Creating a "string of pearls" for mission critical and wealth-creating roles

You have to start earlier. You have to identify potential talent sooner. You have to start the disciplined process of managing their careers sooner. You have to start the succession planning process sooner—and go deeper. Most organizations do horizontal reviews, looking at directors and above with top management and the board. You have to start doing deeper vertical reviews.

What's important is the talent backing up the top 20 or so positions in the organizations over the next few generations. Like lining up airplanes

coming in for a landing at night—air traffic controllers call it the *string of pearls*—in the annual reviews to begin to get a hold on the backup chain. Of course, from a practical standpoint, you would have to have more than one candidate as you go further down in the organization. It would look something like this:

Key Position Backup	Ideal (Pick one, get one)	Practical (Pick many, get one or a few)
Incumbent		
Next up (age around 50)	1 (Consensus Fill)	2 (Viable Candidates)
Next (42)	1	4
Next (35)	1	8
Next (28)	1	16
Next (23)	1	32
Next (18)	1	64

The same reasoning applies to all of the other key jobs. You should know the next six COOs, the next six CFOs, the next six functional VPs (marketing, manufacturing, sales, etc.), the next six SBU general managers, and the next six significant country managers. You get the picture. This same article could be written about any of those positions. It's more fun studying CEOs. Not many equivalent studies of Country General Mangers, for instance.

Assessing early performance, potential and motivation

In order for all this to work, you would have to get better at assessing early performance, motivation and potential.

Expanding your view of performance...

Early performance calls can be improved by expanding what we look at. We need to look toward life-long performance in work, school, hobbies, extracurricular activities, sports and family. Providing very early assignment diversity would also help early performance calls. Instead of letting target

candidates move through three linear or silo and upward jobs in the same function, business and geography, it would be better to get them into three diverse assignments.

You should also get more rigorous about assessing performance over time (three or more assignments). What we are looking for in a performance profile across tough jobs. You should keep a running assessment on things like:

1. **Quantity of Output of Work** (How much do they get done?)
2. **Timeliness of Delivery of Output** (Do they deliver on time?)
3. **Quality of Work Output** (Is their work right the first time?)
4. **Use of Resources** (Do they get things done within budget?)
5. **Customer Impact/Value Added** (Are customers delighted with what they do?)
6. **Freedom from Unplanned Support** (Can they perform on their own?)
7. **Team/Unit Contribution** (In addition to getting their work done, do they help others succeed?)
8. **Productive Work Habits** (Are they personally effective and efficient in how they operate?)
9. **Adding Skills and Capabilities** (Do they learn along the way?)
10. **Alignment and Compliance: Walking the Talk.** (Do they behave and act in line with agreed upon practices and principles?)

The important thing about the assessment of performance is the evaluation of performance over time across diverse challenges.

Checking earlier for potential

Potential is easier to assess. Potential shows early and stays relatively constant. There are validated tools in the market (e.g., Lominger's CHOICES[®]) available to aid early assessment of potential. Consistently monitoring learning agility and emphasizing a learning enhancement plan will facilitate their CEO trajectory.

This also argues for doing a better job of looking for early potential in the recruiting process. It's easier to hire it than to develop it. There is another tool (Lominger's LFE[®] - Learning from Experience) designed to help find people with better potential to start with.

Developing an understanding of motivation

Motivation is a little harder to assess. Young people don't really understand their passions and they don't know about how careers are made. Because of the relatively new phenomenon of dual career couples, moving around has been somewhat chilled. Talking early and often with our emerging talent can give them an idea of how careers are made and the steps required. Given the reality of dual careers, developing this high potential talent may require unique and creative developmental remedies outside of simply moving to a new geographical locale.

This also argues for organizations working on the enhancement of potential. Extensive arguments showing that potential (learning agility) can be enhanced are presented in *The Leadership Machine*. We would suggest using Lominger's *FYI for Talent* along with a learning enhancement workshop.

This we know. The task is now harder and it's just going to get worse. The science and the best practices of this early identification and development system exist and all that's left is execution. Those organizations that catch on and install early identification and development systems are going to win in the long term.

Finding the other six ...

To make certain you have the six successful CEOs (or other mission critical roles) within your leadership pipeline—the string of pearls—you and the Board should be able to respond to the following questions.

- Do you know who is the high potential and high professional people within your string of pearls---the next five CEOs, COOs, CFOs, functional VPs, SBU general managers or significant country managers? If you don't know, others will take them before you find them.
- Do you have a consistent and sustained process for evaluating, calibrating and validating the performance and potential of your talent pipe-line? The performance/potential matrix is widely used, but does it have a research-based definition of potential such as learning agility? If you don't, you are increasing the likelihood succession is accomplished through chance.
- Do you bring new talent into the organization with the potential to grow rapidly into new assignments and challenges?
- Do you provide for the care and feeding of your high potential pool ensuring they are retained throughout their career with your organization? If you don't, they will leave.

- Do you provide your high potential and high professional talent with aggressive developmental experiences designed to prepare them for the issues, problems and challenges of the future? If you don't they will not be prepared when called upon.

If your organization doesn't do what's suggested above, those six CEO candidates now work for another organization. You will have to find them. Pay big money for them. It will be a needle in a haystack search. What are the chances those other organizations are going to prepare your CEO's for you and on time? You are delegating the job of developing your next CEO to another organization. What are the chances that you will be able to successfully find the ones you need?

Better to do it yourself.

The key succession and talent management question...

If you knew who these six replacements (for any key role) were, would you do anything different for or with them to get them prepared? Would you give them any special attention? Would you give them special assignments? What extra experiences would you provide? Would you introduce them to senior leadership sooner? Would you assign senior mentors? Give them an international exposure sooner? Introduce them to the board sooner?

From a research standpoint, the answer is clear. Great leaders are those who have learned from the diversity of assignments along the way to the top. They have worked with a variety of bosses and been exposed to different functions, issues, challenges, geographies, and usually, more than one line of business. They have learned about Wall Street and the investment community. They have managed key stakeholders including key customers. They have dealt with the political system and regulators. They have established useful networks both inside and outside the organization. They have a worldview. They will have done startups, turnarounds and stints in HQs. Some will have spent significant time in special causes and probably serve on the board of one or more non-profit or charitable organizations.

That's a lot to do over a career. The earlier you start, the higher the likelihood of success. In his *Harvard Business Review* article, *Ending the CEO Succession Crisis*, Charan (2005) says to fit in all the experience a person needs to take over as CEO; you need to start age 30.

So there are potentially 6 CEOs, COOs, CPOs, CMO, CTOs, CFOs and all of the other key officers working for you today. To insure a consistently successful business over time, you better begin to know who they are and do the right thing for and with them.

Timely talent always wins.

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