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Culture and CEO Tenure:
How Culture Can Get You Feted or Fired

The average CEO's tenure is 8 years but that can differ widely depending on various factors. In this brief we review those factors and particularly the role played by corporate culture. Some CEOs fail because they migrate between sectors with very different cultures. Some cultures simply change CEO more often. Other cultures can impact financial performance which, in turn, impacts CEO survival. Specifically, firms with a 'Focused' culture, where there is a clear shared strategic vision and decisions are made and implemented quickly, grow 8% faster than their competitors and benefit from 25% better staff retention.

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He lasted five days. *Five days*. On 27th June 2012 Bill Johnson signed a contract to become CEO of Duke Energy. By 2nd July he was gone[a]. In the turbulent politicised arena of leadership this is surely the shortest reign on record. Even Lady Jane Grey managed nine days as Queen of England, although she didn't then go on to land a cushy gig with the Tennessee Valley Authority.

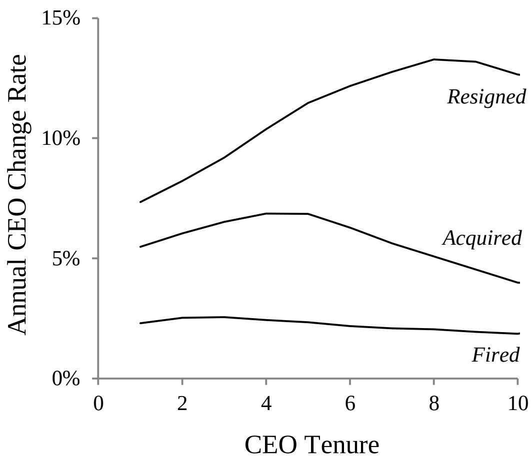
So what determines how long a CEO lasts? Or how long other members of the leadership team, including Marketing Directors, Commercial Directors and Finance Directors last? In this brief we discuss the drivers of CEO tenure, outline the role that corporate culture plays both indirectly and directly in that process, and what senior managers can do to positively impact their existing culture.

Whilst nebulous and hard to define, the powerful effect of corporate culture on business performance has long been recognised. As Peter Drucker allegedly[b] once said 'culture eats strategy for breakfast'. Culture can drive financial performance and deliver competitive advantage. Culture can block efforts to mobilise and change an organisation. Culture can inspire staff loyalty. Culture can get you feted or fired. So what is culture and what can you do about it?

The Execute in Executive

The typical CEO lasts 8 years and their CMO lasts about 4 years. In other words, the average CEO fires two CMOs – the first when they arrive and the second when they have to pacify shareholders after some poor sales figures. Perhaps the Chief Scapegoating Officer, or CSO, would be a more appropriate title, though this will presumably irritate the Head of Strategy and the Chicago Symphony Orchestra.

Figure 1: Executive Demise



CEO tenure stretches from ol' nano-job Johnson's long weekend to Warren Buffett's sixty years at Berkshire Hathaway. Figure 1 shows how the annual departure rate evolves over time across three key causes of termination[c]. For example, during their fifth year, the chance of a CEO exit is 11.4% overall, with 2.3% getting fired outright, 4.5% ousted as part of a takeover and 4.6% leaving voluntarily.

The figures in the chart reveal some interesting facts. For example, only a quarter of CEOs get fired and half of them survive to resign. Moreover, the risk of getting fired is constant over tenure whereas the risk from takeovers peaks at about four years and then drops. Essentially, a company with a new CEO is either easier prey or actively looking for a buyer after its turnaround plan has been implemented and the executive option schemes are heavily in-the-money.

CEO departures are also driven by a company's characteristics. CEOs are more secure when they own a significant equity stake or sit on the Board. Conversely, firms that are bigger, more capex driven, or are underperforming are associated with greater job jeopardy. Underperformance can relate to the company, its sector, or the economy in general. Trigger-happy Boards don't care about the cause. The shares are either up or the CEO is out.

CEO survival is also heavily influenced by corporate culture. Just how long was Antony Jenkins, promoted in 2012 to clean-up Barclays' scandal-plagued culture and thereby nicknamed 'St Antony', really going to last? Three years, it turns out. Or to quote Jeff Bewkes when he fired Jack Griffin after just a few months 'his leadership style and approach did not mesh with…Time Warner'.

Corporate Ethnography

The literature defines culture as (deep breath) the collective values and assumptions which underpin a company and that manifest themselves in practice as shared behaviours. For example, you might describe a firm's culture as decentralised because decisions tend to be delegated away from the leadership or friendly because there are more out-of-office social events.

Figure 2: Culture: Our Company Is…

Pacesetting	Responds to market changes quickly
Commercial	Holds people accountable for results
Purposeful	Has clear goals and a shared vision
Transparent	Has clear discussions and little politics
Nurturing	Encourages people to acquire skills
Decentralised	Allows managers to act autonomously
Meritocratic	Recognises and rewards achievement
Friendly	Has colleagues I consider friends

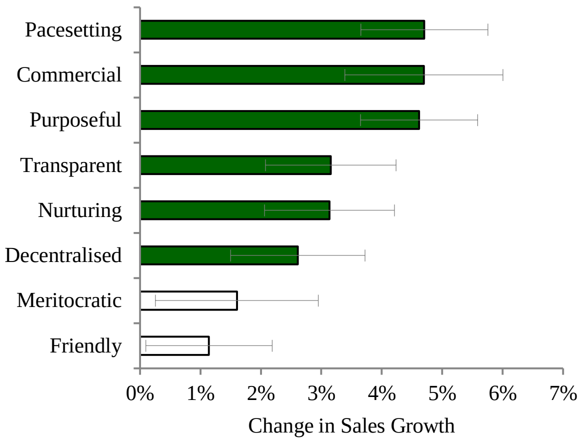
Based on this prior research[d] we asked 980 staff from 47 different industries to rate their employer across 36 culture statements. Their responses yielded the eight attributes shown in Figure 2. These replicate the prior findings and extend them by adding Meritocratic and Friendly. There are clearly other cultural attributes, such as ethicality and customer centricity. But these eight are widely recognised and intuitive. Accordingly, they seem like a good place to start.

As noted, culture can have a direct effect on CEO retention where a given CEO doesn't fit with a given culture. But it's also the case that certain cultures change CEOs more often in general. For example, Fiordelisi and Riccia[e] find that Commercial and, to a lesser extent, Pacesetting cultures exhibit higher CEO turnover. Interestingly Pacesetters are also more likely to appoint internal replacements, questioning Apple's decision to appoint John Browett, then CEO of Dixons, to run their retail network, but explaining why he left after six months.

A Focused Culture

There's also an indirect link between CEO turnover and culture because culture influences financial performance. Consistent with the existing research our analysis in Figure 3 shows that having a Pacesetting or Purposeful culture boosts a company's annual growth rate by about 5%. We term this a 'Focused' culture because these are organisations that know where they are going and work quickly and efficiently to get there. The finding supports the 'strong culture hypothesis' that certain office environments deliver the best performance. Whilst these effects probably vary by industry, we didn't find any reliable effects, in part because industry itself is so tricky to define[g].

Figure 3: Performance Cultures[f]



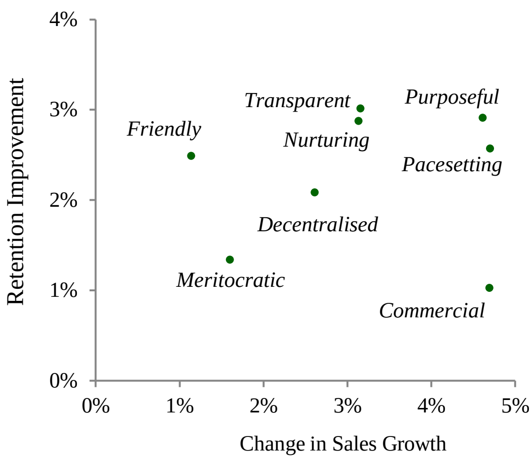
Conversely, Meritocratic and Friendly cultures have no statistically significant impact. These types of company don't grow any faster than others. As we discuss below, being a Friendly firm may have other benefits, but stronger sales performance isn't one of them. Likewise, a Meritocratic culture may be the most subjective of the attributes and in itself a potential distraction from company performance.

Indeed Focused and Unfriendly pretty much summarises our understanding of Amazon. There are regular sackings to keep workers on their toes, described by one manager as 'purposeful Darwinism', and high performing staff are referred to as 'Amabots'. Sales were $107Bn in 2015 having grown on average 26% per year for the last five years.

Loyalty Rewards

Of course sales growth is only one financial effect. Culture can also have cost implications, for example via staff retention. Vacancies, recruiting, training and lost know-how all incur both real and opportunity costs. Generally staff turnover is around 15% per year, slightly ahead of the CEO attrition rate. But does staff turnover also vary with culture? The scatterplot in Figure 4 shows the sales effect from Figure 3 on the horizontal axis and the staff retention impact on the vertical axis. So, for example, having a Friendly culture will reduce annual staff turnover by 2-3% down to 11%-12% per year.

Figure 4: No Trade-Off Required



The graph highlights that there's no relationship between sales growth and staff retention. Which is good because it means you can have both. No trade-off between them is necessary. Specifically, what we've called Focused companies, with a clear strategy and a higher 'metabolic rate', simultaneously retain staff and grow faster. To a lesser extent this is also the case for companies that are Transparent and don't tolerate office politics or which are Nurturing and invest more in staff development.

The other four cultures either produce one of these benefits or neither. Meritocratic cultures are the worst. They suffer from too much focus on individuals, rather than teams, and all the associated problems of measuring performance to anyone's satisfaction. Consequently, whatever benefits a Meritocratic culture may bring in theory, these then neutralised by all the resultant in-fighting.

Summary

CEO tenure is influenced by factors such as takeover activity, Board composition, and corporate culture, with Commercial and Pacesetting firms changing their CEOs more often. CEO tenure is also influenced by absolute financial performance, regardless of any global or sector headwinds. And this financial performance is also affected by culture. Focused firms, that are both Purposeful and Pacesetting, grow faster and experience less staff turnover. Specifically, they grow 8% more and lose 25% less staff each year.

Okay, so we want some of that. The next question is "How do I create a Focused culture, a firm that knows where it's going and acts rapidly to get there?" Here, alas, the literature veers into anecdote. People have tried to instigate cultural change within their companies and qualitatively track progress. But no one, apart from the brothers who own Aldi, has yet been rich or insane enough to run that particular randomised controlled trial[h].

Yet there is evidence that company culture *can* change and the following three steps are undoubtedly necessary to make that happen:

- *Assess*: You have to devise a method to measure culture. This could be employee statement ratings or more objective behavioural measures.
- *Aim*: You have to decide what culture you want. We say Focused but you could also benchmark against stronger competitors or simply go with your instinct.
- *Act*: You have to start doing 'things' to change culture. Because of 'Assess' you'll know if you've made progress. As it's not a randomised trial you won't know why.

Behavioural measures of culture are clearly preferable assuming they are credible. We want to measure Purpose and Pace. So, for example, how do staff score on a test about the strategy? How many hours do they spend hearing or talking about the strategy? How long does it take to make a pricing decision? How quickly can you get a new product to market? How many decisions does the firm take each week?

Regarding what actions to take, it's useful to reflect on the origins of corporate culture. In part it comes from the commercial pressures of a sector. So there will be cultural commonalities within industries and between industries with similar market dynamics. But there are still differences between companies within a sector and these must come from within – from the founders' and incumbent management's style, from the formal practices that they put in place and from the type of staff that they recruit and promote.

Here are three examples, which could be used to influence Purposeful by targeting these three sources. First, has the senior management team actually set aside time to crystallize its strategic vision for communication to staff? Second, how can the organisation re-purpose its existing schedule of firm-wide meetings to disseminate that vision more effectively? Finally, are staff motivated, either by intrinsic disposition or some form of incentive, to incorporate that vision into their daily work?

Whatever hand dealt by sector-specific forces, firm history and dumb luck, the conscious and explicit management of corporate culture is a powerful commercial lever. The CEO who can control culture and steer it in the right direction can simultaneously raise financial performance, secure their own position and bestow a lasting legacy.

References and Footnotes

a. Lublin, J. (2012, July 6) Behind Duke's CEO-for-a-Day. *The Wall Street Journal*. Johnson, then CEO of Progress Energy, was announced as Duke's next CEO 18 months earlier when Duke unveiled a $26Bn merger with Progress. But once the deal closed on 2nd July he was ousted by the original Duke CEO, Jim Rogers.

b. Drucker doesn't appear to have said this. But that doesn't seem to stop people attributing it to him. Likewise, delightfully, Michael Cain never said 'not a lot of people know that', which was actually coined by Peter Sellers whilst doing an impression of him.

c. This section is largely drawn from Coates, IV, J. C. & Kraakman, R. (2010) CEO Tenure, Performance and Turnover in S&P 500 Companies. *Harvard Law and Economics Discussion Paper No. 595* and Kaplan, S. N. & Minton, B. A. (2012) How Has CEO Turnover Changed? *International Review of Finance, 12*, pp: 57–87.

d. Christensen, E. W & Gordon, G. G. (1999). An Exploration of Industry, Culture and Revenue Growth. *Organization Studies, 20(3),* pp: 397-422 is a good introductory paper that summarises the culture literature and reports new findings using a proprietary data set.

e. Fiordelisi, F. & Riccia, O. (2014). Corporate Culture and CEO Turnover. *Journal of Corporate Finance, 28,* pp: 66–82. They notably measure corporate culture by applying computational linguistics to the annual reports. Yes you *can* measure poor Purposefulness with the frequency of buzzwords like 'actioning', 'pre-plan', 'potentialities' and 'solutionise'.

f. The bars estimate the impact of a one SD movement (e.g. from 50th to 68th percentile) in culture using a single variable regression. Lines show the estimation errors. Unfilled bars aren't significant.

g. As evidenced by, for example, the rise of Factor Investing. Factor Investing is when, rather than using imprecise and subjective binary allocations to asset classes or sectors, securities are decomposed into their underlying factors to then re-construct them into a diversified portfolio. See Wrigglesworth, R. (2016, June 15) 'Factor Investing' Wages Battle Against History. *Financial Times.*

h. You divide the business into two, leave one half as the control and try changing the culture of the other. As Karl and Theo Albrecht did when they separated Aldi into Nord and Süd after an argument in 1968 about checkout tills. But then you do something more radical than starting Trader Joe's.