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Firms more inclined to promote insiders as CEO

Developing leaders pays off, experts say

By Barbara Rose | Tribune reporter

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Forty-four percent of the region's 100 biggest public companies, based on market capitalization, have named new chief executives since 2005, and half of the newcomers were recruited from outside the company, according to Hinsdale-based recruiting firm Crist Kolder Associates.

Even in cases where companies recently appointed veteran insiders to the top job—Gregory Brown at [Motorola Inc.](#) and Robert Pullen at [Tellabs Inc.](#), for instance—the new CEOs replaced outsiders who had lasted less than four years.

Yet studies suggest that CEO turnover at the biggest public companies may be stabilizing, and companies are more inclined to pick an insider than in the past. This is good news because insiders generally stay longer and perform better than outsiders, experts say, and rapid turnover is a factor in escalating CEO pay.

"The turnover represents a broken leadership pipeline," said Noel Tichy, director of the Global Leadership Program at the [University of Michigan's](#) Stephen M. Ross School of Business. "There's clearly been a failure in developing the next generation of leaders."

CEO turnover climbed during the 1980s and 1990s, and median tenure fell to less than five years currently.

Harvard Business School associate professor Rakesh Khurana, author of "The Irrational Quest for Charismatic CEOs," concluded that a chief executive was three times more likely to be fired for the same level of performance at the end of the 1990s than 20 years earlier.

Boards too often chased dynamic personalities rather than creating internal systems to groom leaders, he concluded.

"The thinking used to be, 'Let's just get somebody new. The bigger the marquee name the better,' " said Crist Kolder's Peter Crist, adding, "The pendulum is swinging" away from that approach.

"Boards are very risk averse today," he said. "Picking the inside person signals we have succession planning, we've done the right thing. And when you promote somebody from inside you just dodged a huge compensation adjustment" to meet the outsider's salary expectations.

An annual study by global recruiting firm Spencer Stuart found that 85 percent of the newly-appointed CEOs last year among the S&P 500 were promoted from inside, up from 60 percent in 2005.

Turnover has fluctuated between 11 percent and 14 percent annually in recent years, according to Spencer Stuart's studies.

"Our view is that turnover has stabilized," said Gary L. Neilson, senior partner in Chicago at management consulting firm Booz & Co.

The firm's most recent study, based on the world's biggest 2,500 public companies, found that about 30 percent of departing CEOs were forced to resign because of poor performance, ethical problems or board disagreements.

One reason boards delay replacing poor-performing CEOs is because there is no successor in place, Neilson said.

"Too often we see people groomed in the mirror of the current need," he said. "They are a great supporter of the current direction but they really haven't developed the skills to lead if something changes."

Companies are focusing more on developing leaders at all levels, he added. "What they've found is going to the outside is not the magic answer."

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