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# Prepare to tell long-serving bosses their time is up

Andrew Hill, Financial Times

You should be able to divide any list of chief executives into three categories: the indispensable, the interchangeable and the irredeemable. The past week has provided examples of all three.

The US Securities and Exchange Commission decided Elon Musk was vital to the success of Tesla, requiring him to renounce the chairmanship as part of a deal over governance and disclosure failings, but letting him stay on as chief executive. Pfizer announced it would exchange Ian Read, the pharmaceutical company's chief executive since 2010, for another insider, Albert Bourla. General Electric ejected John Flannery, who has run the group for barely a year, and installed Larry Culp, a director and an outsider, in his place.

Mr Read is not impartial, but he judged his succession "a smooth and thoughtful planned process" after nearly eight years at the top. It so happens that when he took over in 2010, eight years was roughly the average tenure for a departing US chief executive. Now a report shows heads of S&P 500 companies are leaving having served nearly 11 years in the top job, the longest average tenure since 2002.

According to the Conference Board, the US business group that prepared the annual data, chief executives of companies that do well are enjoying greater job security than they used to. Bosses who fall short are facing Mr Flannery's fate: underperforming companies replaced their chief executives in 2017 at a rate three times faster than outperformers did.

You may say this is how governance should work, but the findings are worrying. There comes a point when almost every long-serving leader starts to get complacent. Indispensable becomes immovable.

All such averages are the outcome of many individual cases. Mr Musk behaves like a founder-chief executive. Founders often stay longer for sensible reasons linked to their skills, deep knowledge and leadership qualities.

They also get enviable room for manoeuvre. Jeff Bezos of Amazon pointed out to Forbes recently that he is rarely "pulled into the today". Instead, Mr Bezos works on strategy two or three years ahead: "Friends congratulate me after a quarterly-earnings announcement and say 'Good job, great quarter', and I'll say, 'Thank you but that quarter was baked three years ago.' I'm working on a quarter that'll happen in 2021 right now."

Even founders can cling on beyond their time, though, sometimes shielded by special classes of stock that impede investors' efforts to oust them.

Companies that are not founder-led need to strike the delicate balance between inertia and churn.

GE's case shows, though, that this is easier said than done. The conglomerate was supposed to be a model of leadership development. That GE directors decided Mr Flannery was irredeemable within 18 months of appointing him suggests the former industrial bellwether is undergoing a crisis deeper than even its unhappy investors guessed. It also points to potential flaws in the group's admired long-term succession model.

Crisis almost always shortens chief executive tenure. In 2009, in the midst of the turmoil threatening the world financial system, S&P 500 chief executives were lasting on average only 7.2 years.

Longer tenure at the top may, therefore, be a sign that the good times are back. But boards should be alert to the risk of smugness among the supposedly indispensable long-servers, and of panicky fear among recently appointed chief executives.

Academic studies suggest long-serving, older chief executives tend to underperform. The reasons for keeping them on — boardroom clubbiness, nostalgia for past glories — become less convincing. A reluctance to change the people at the top embeds itself in the whole culture.

At the other end of the scale, the fearful incoming chief executive could be tempted to front-load his or her compensation, favour decisions on investment or on acquisitions with a positive short-term impact, and obsess about quarterly performance.

This is where the board comes in. Directors have a duty to prepare for the exit of the longstanding incumbent chief executive as part of a Pfizer-style "smooth and thoughtful" succession plan. They also need to set sensible long-term incentives for their replacement.

In the US at least, this responsibility is increasingly pressing. The average age of S&P 500 chief executives is now 58.3; nearly 17 per cent reached retirement age of 64 in 2017, the highest proportion since the Conference Board started tracking the data in 2001. Age is no bar to high performance, of course, but history suggests some once-indispensable chief executives are about to become, if not irredeemable, then at least interchangeable.