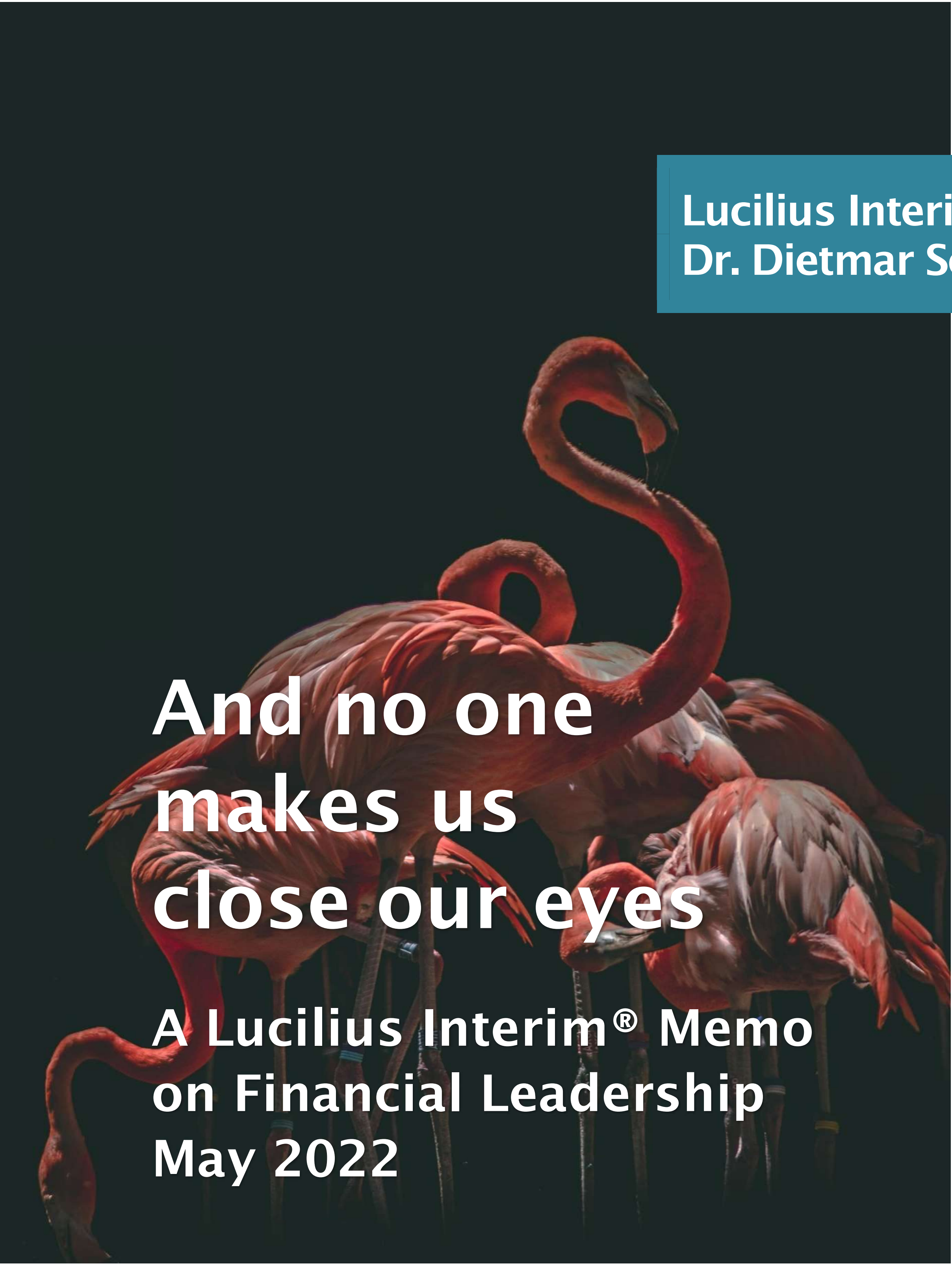


Lucilius Interim
Dr. Dietmar Scheja

And no one makes us close our eyes

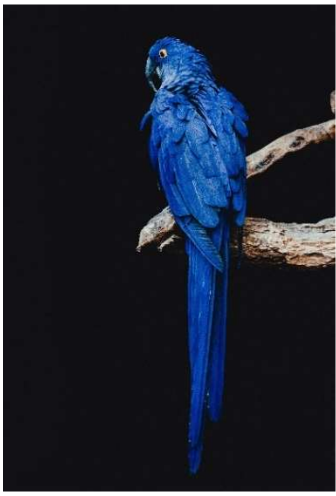
A Lucilius Interim® Memo on Financial Leadership
May 2022

A large number of CFOs has recently been promoted to CEO positions. This paper suggests a possible reason for this surge: The need for a specific sort of leadership at the top, one which finance managers are more bring along than others. The memo outlines the power of what I will call Financial Leadership - even though both its mindset and its tools are available to everybody. And it argues why Financial Leadership is more important in today's business world than ever. --- I'd like to thank Alison Budge for her extensive comments on an earlier version of this memo.

Anna Borg at Vattenfall in 2020, Marcus Ochsner at ABB Germany and Robert Davis at Merck in 2021 are just a few former chief finance leaders becoming CEOs in the last two years. Tim Höttges, the former CFO of Deutsche Telekom, is the most prominent example in Germany. Already back in 2015 and 2017, Korn-Ferry and McKinsey, respectively, wrote white papers[1] on the topic: A striking number of CFOs have made it to the top job in recent years.

No doubt, each case can be explained in its own terms. But it is worthwhile to explore another possible explanation for the rise of the CFOs: Perhaps shareholders wanted their top person to have a specific managerial capability which finance mangers are more likely to bring along than others. Not their functional expertise because their old roles will have given plenty of scope for that, but a certain way of managing which shareholders wanted the new CEO to bring to bear on how their company works, on where it invests and why, on how it develops its people, picks its strategies and deploys its tactics, in short, on the entire firm in all its facets.

So: If managers raised through finance do lead in a special way, what is the essence of Financial Leadership?



Let's start out from a familiar role: the financial analyst. Like a scout who tries to find the best route - the shortest, safest, most evenly paved - the financial analyst looks for the best option available to a decision-making body, such as a corporate board. The scout may struggle to deal with trade-offs – how much more safety is needed to justify an additional 5 miles? The financial analyst surveys all the various pros and cons of an alternative and translates them into dollars. The common currency lets the analyst weigh advantages and disadvantages from different domains and determine what's best (under the assumptions made). This may be hard and will require judgment, but it is doable, and the result can be tested, e.g., in an experimental auction.

Analysts already will not stop at calculating and presenting results. They will lobby for the alternative they're convinced is best. Rightly so, because at this stage, by virtue of his or her role, the analyst is the one member of the team preparing the decision who had to think through the issue from all its angles and had to weigh the arguments brought by all members.

Financial leaders take the analysts' way of working to a yet more action-oriented level. They will make sure that any advice they lead from is gained through a thorough, full, and wide-ranging appraisal, that all relevant parties had a voice, that assumptions are balanced, and

[1] Korn Ferry 2015: Gary Burnison – CFO to CEO. McKinsey 2017: Michael Birshan, Thomas Meakin, and Kurt Strovink - How functional leaders become CEO's. (With a narrower focus than the title suggests.)

the math is correct. Mindful of their mandate, financially minded CEO's will demand the same of every manager in their organization and by and by form their way of leadership into a corporate skill.

Inviting and enticing me to rise

A firm will want to possess this skill for two reasons: It ensures that any position or decision the company takes is grounded in as rich and unbiased an understanding of reality as it can achieve. As important is a second aspect: Like an omnipresent swarm of babel fish, financial leadership helps – or pushes - the company understand its preferences. Let's say adding a feature to a product increases purchase intent by 2% but causes a 3% loss of manufacturing efficiency. A production engineer and a market researcher may not be able to understand – let along agree – if the feature is worth having. Financial evaluation makes the two effects comparable. And by laying open how the translation into numbers works, everybody involved can challenge the result. By mastering this skill, therefore, the organization learns its best attainable way of acting from the shared understanding of the best attainable insight.

Which may not equal certainty but is as good as it gets in this world. No amount of probing will ever remove all uncertainty from the future. But in a life in which certainty cannot be had by anybody, those who systematically and efficiently sift and distill facts enjoy a comparative advantage over those who don't. Financial leaders will never tire to make sure that this lesson is remembered and appreciated.

None of this is easy, and financial leaders, thus, work under a paradox: the richness of their understanding goes hand in hand with being conscious of its limitation. They cannot, therefore, hope for simple messages. Staying open, transparent, faithful to the analysis, they will argue their case based on its results and will not hide any imperfection. This does make for a more complex reasoning than a case built on emotion, tribalism, cliché, ego, vanity or received opinion, and not everyone will invest the time to follow their argumentation, but if well-made, many will, and those who do, will feel appreciated, taken seriously and treated as adults.

And no one sings us lullabies

Leadership of this kind needs time and patience and careful communication. Moving to the political sphere - the key traits of financial leadership being universal: When Ronald Reagan explained the dynamics of taxation in his address to US citizens in July 1981, he showed how a rational case for an abstract, complex issue can be made with supreme efficacy.

In business, the same principles hold. Financial leaders will spell out all the results of their analysis that are relevant to the choice they recommend – not just the convenient ones. They will be patient and will respect their audience and its capacity for understanding and for wanting to do the right thing.

One final thought: It is not quasi-programmable decisions, like automating the packaging stage of a production line, that benefit most from financial leadership - they're just easiest to take care of. It is in fact some of the hyper-complex, do-or-die questions facing businesses today where financial leadership matters most: As we take the side of political freedom and free enterprise, how can we best manage the energy price shock about to hit? How can we reconcile a fundamentally spoilt rich-world consumer base with the economic necessity of rising prices? What exactly is the CO2 footprint of beef compared to its alternatives? Are we creating a truly sustainable business model? Or are we grasping at anything that is just a tiny bit less catastrophically unsustainable than business-as-usual to label it 'sustainable'?

When navigating waters that are boiling with issues like these, financial leadership plays to its strengths: How it is willing to engage openly and deeply with whatever facet of reality is accessible. How it makes members of different spheres and persuasions communicate about their respective facets of reality. And finally, how it determines, promotes, and executes the best course of action available.

If superior leadership skills were what the boards had in mind when they chose a CFO to become the next leader of their firms, it has been a most timely choice: There is plenty to do, and open eyes will sorely be needed.

Credits: The text quotes from Pink Floyd's undying 'Echoes'. Photos: Marko Blazevic (the flamboyant flamingos so ably standing in for the original albatross, twice) and Dominik Lange (skeptical blue parrot), both on unsplash.com. Thanks a million.

Frankfurt and Düsseldorf, March/April/May 2022.

Lucilius Interim Dr. Dietmar Scheja
Financial Leadership – Restructuring – Finance Upgrade & Transformation