Learning From The Oldest: Developing Leadership by Allowing Risk

Written by Joe Blake

WHEN WE THINK ABOUT THE MARINE CORPS, FEW OF US WOULD THINK ABOUT COMMUNITY BANKING. We think about John Wayne, the memorable Pacific campaigns of the Second World War, or the larger-than-life memorial to the five Marines who raised the flag on Mount Suribachi. We may even think about the kid down the street who joined the Corps and somehow was never "just a kid" again. But the world of the Marines would seem to be the antithesis of community banking. After all, the Germans labeled them "devil dogs" in the First World War.

The Marines are well known for their relatively small size compared to the other military services, the strength of their discipline and training, and their intense unit cohesion and pride. They are often characterized by the phrase "lean and mean." Yet, in our experience, the more successful community banks are often lean and mean and know how to maneuver around larger organizations with considerable skill and success. Ironically, the Marines are the oldest branch of the military services based on their founding in Philadelphia on Nov. 10, 1775, before the drafting and signing of the Declaration of Independence. And yet, a search for details about the banks that claim to be the oldest in the United States revealed that none of them was founded before the revolution.[1] That begs a question: Can an organization that is older than the American republic and that confronted the challenges of many conflicts teach community bankers how to maneuver in today's competitive environment?

Recently, the book entitled *The Marine Corps Way: Using Maneuver Warfare to Lead a Winning Organization* (McGraw Hill, 2003) by Jason Santamaria, Eric Clemons, and Vincent Martino set out seven guiding principles of maneuver warfare that have given vitality if not effectiveness to Marine leadership and strategic thinking for a very long time. These principles are targeting critical vulnerabilities, boldness, surprise, focus, decentralized decision-making, rapid tempo, and combined arms. These principles help explain the greatness of the Marines, but do they relate to community banks both old and new? The intent of this discussion is to make the principles of the Marine leadership on the battlefield relevant to the competitive world of community banking.

TARGETING CRITICAL VULNERABILITIES: In essence, we want to hit the competition where it hurts the most. The goal is simple: Find the spot where you can do the most damage. All Marines from top to bottom are taught to find the enemy's weaknesses and hit them hard. Marines also understand that two can play this game, so defensive measures are a must. Specifically, they identify their own weaknesses and prevent them from being targeted.

There are examples of this seen in community banking, such as the way Commerce Bank developed a strategy based on "open all hours." Its management knew the competition had habits that they were reluctant to change. Commerce was willing to break the mold and open seven days a week including evenings. The customers liked the convenience and were willing to accept low rates for their deposits in exchange for it.

In many community banks, including de novo banks, the key to asset growth is the requirement that the CEO be more a salesman than an executive. The commercial loan officers need to be aggressive if not hungry for loans combined with the marketing sense to open the doors and close the loans. David Lobach, the CEO of Embassy Bank, has said his slogan is, "Yes is the answer — what is the question?" Now we all would nod agreement, but we have to mean it.

We have all seen the ditech.com ads with the loan officer who promises to deliver but fails to even convince his mother or his psychiatrist. His bank "talks the talk but does not walk the walk." To avoid the same outcome, how do we make this work? Management has to cut through the bureaucratic obstacles that often develop in the name of preventing loss or excessive risk. We want to promote responsible risk taking subject to appropriate limits. To do that, we need to determine whose approval is needed, when it is needed, and what role is appropriate for the board in the loan approval process. That means that management must be able to identify and keep good people with experience and judgment.

BOLDNESS: The success of any plan is often a function not only of the boldness of the design, but also the boldness of the execution. This means leadership and open communication at all levels of the planning and execution. The Marines encourage an obligation to dissent in the decision-making process. They will tolerate mistakes that stem from bold zeal but not for indecision, timidity, and lapse of integrity. They practice the old sports adage, "the best defense is a good offense."

In terms of strategic plans, BNK recommends that your bank have a vision called a 10-year plan. A 10-year horizon is beyond the normal business cycle and stretches our thinking beyond what is familiar. You should also develop various scenarios for the bank's

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[1] Our research found three banks that were more than 200 years old: Bank of New York, 1784; Washington Trust Company, Waverly, R.I., 1800; and Beverly Trust Company, Beverly, Mass., 1802. Bank of Boston also was founded in 1784, but its name is quickly disappearing in recent acquisitions.

future path rather than merely projecting where we are as if the future were a straight line. **BNK**Strategies℠ often works closely with banks to develop these plans and monitor the bank's progress on a quarterly basis.

To start this process, you should first envision where you would like to be and then plan backwards. That backwards analysis forces you to establish specific goals in terms of asset size, capital, and number of employees. These are milestones that measure your progress to the plateaus or breakthroughs needed to achieve the vision. If you establish interim targets/goals, you can identify if you are getting there. You still need three-year strategy plans because you have to give reality to your 10-year dreams. But if you only think in terms of three-year plans, breakthroughs to new thresholds may be rare or hard to detect. That is where boldness of plan and execution are essential to realizing the dream.

Some organizations thrive when there is a culture that encourages employees to take risks, to act responsibly based on well-understood goals, and to think outside the box when circumstances require it. For that to work, management must have open dialogue with the employees, leadership must be encouraged, and training and compensation incentives must be part of the development of every employee. Management clearly does not want its staff to be reckless; but boldness will not be found if management means "thin and cheap" when it says "lean and mean."

SURPRISE: Marines want to hit the other fellow when he "ain't lookin'." In banking terms, this concept refers to the use of information to impair the competition's decision-making ability to respond quickly or, better yet, to anticipate our subsequent strike. To do this means we need to use stealth, ambiguity, or even the overused smoke screen to throw the competition off the track.

Clearly, the element of surprise in community banking will include marketing campaigns that are creative if not unexpected. The surprise concept in banking is like a sparring partner who uses a series of bunny punches to wear down the opponent. You need to anticipate the opportunities with potential customers so that you take advantage of their mistakes not by default but by positive punches. Mergers have given many banks chances to take the larger banks' disgruntled customers. Nonetheless, their unhappy customer is not necessarily our happy customer. To keep the other bank's unhappy customer, we need to have a marketing strategy that surprises both the new customer and the competition. The first punch would be to have a marketing strategy that addresses the customers' needs and exceeds customer expectations. We all say we offer price and product based on what customers want. However, if that is true, why does every bank offer free checking but few customers can really differentiate the many free checking products? For that matter, can the bank's staff? If you throw a bunny punch, the surprise should be that you have a product that is well designed, marketed, and understood both by the depositor and your staff. The momentum must be to innovate and offer new products. One of our clients offers nine- and 12-year mortgages, which happen to fit the bank's interest-rate-risk tolerance and the desire of the borrower to have a mortgage that can be repaid more quickly. Oddly, none of their bank competition offers the product because it does not fit their business model — basically to originate, sell, and service 15- and 30-year residential mortgages. Surprise requires that we develop those punches and keep them coming. (We will say more about tempo later.) You must continuously be jabbing the competition with those bunny punches.

FOCUS: If we want to hit the competition as hard as we can, then everyone must understand the goal. The Marines rely heavily on information to locate lucrative targets (growth opportunities) as they arise and to commit available forces quickly and in a *coordinated* fashion. While no community bank can stand still for long, it is especially true of the entrepreneurial segment, de novo banks. All banks must be focused to grow in ways that increase the value of the franchise to all stakeholders. Banking is a very mature business whose core competence — the granting of credit — was well documented long before the armies of Alexander sought to spread the benefits of Greek culture in the Mediterranean world several millenniums ago.[2]

Focus means that management needs timely information and well-understood goals to establish criteria for prioritizing issues and making decisions. It is easy to be distracted and lose focus. In warfare, we ambush the enemy to impede their progress and make them stop their advance. In banking, distractions are not as deadly as an ambush, but they can be time consuming and annoying. It is especially true when an organization is new or embarks on a major strategic step like opening a new branch or buying another bank. Frequently, bureaucratic requirements are a common source of distractions because banking is more heavily regulated than most businesses and by multiple agencies. Because regulatory compliance is a prerequisite to being in the business, the CEO may be easily drawn away from the priorities set by the board. For the de novo bank, this distraction can be lethal because the CEO needs to be selling the bank and developing its franchise in the community. But to do that, most CEOs need to have a pragmatic bureaucracy "freak" that can cut to the quick of the issue and keep the bank focused on mission. Otherwise, despite their efforts to the contrary, they incur overheads they do not need or are limited to working on the mission in their spare time.

Another way that focus can be lost is the ad hoc way tasks are assigned, especially when job functions and descriptions are not well defined. Under these circumstances, managers will assign tasks on an ad hoc basis using the availability of time as the criteria

[2] In his book, *The History of Interest Rates*, Sidney Homer included mention of the earliest loan documents, namely stone tablets, from the time of Hammurabi.

for the assignment rather than where the task should be assigned based on function and skill sets. Without adequate job descriptions, it becomes very difficult to get an effective division of labor.

Likewise, all organizations have informal reporting relationships based on a "go to" mentality where a few key people are sought more often to take care of projects. Therefore, some people are overloaded (the key go to people) and others are underutilized. From an organizational perspective, employees can perceive the overload that some experience as a result of being capable and willing. Just when we want people to be willing to perform at their best, we have employees who see that if they want to avoid being overloaded, they should limit their demonstrated capability. They have learned what the cynic meant by the remark, "Your good deeds will not go unpunished." As a result, there is not only poor productivity but also the division of functions so that we lose both efficiency and accountability. The net effect is a lack of consistent involvement that one might expect to find in a well-focused bank.

DECENTRALIZED DECISION-MAKING: For the Marines, this can be summarized as empower, lead, and train. The goal is to empower those closest to the action with the latitude they need to take advantage of the opportunity without waiting for approval.

Within Marine units, leaders:

- establish a baseline of trust with those in their charge,
- tailor communications with the aim of arming junior leaders with the bigger picture into which their actions fit, and
- vigilantly supervise the implementation of all directives issued.

We might well call decentralized decision-making the central premise behind the subtitle of this article, "developing leadership by allowing risk." That may sound as if cowboys will be let loose, but it really is the way a confident, well-led organization demonstrates that it has communicated its vision and goals, established prudent limits of authority and adequate controls to monitor risk, and selected and trained its staff to lead, decide, and take responsibility for the future of the bank. It presumes that management has accepted that it may often be preferable for employees to beg for forgiveness than ask for permission — provided their actions are in harmony with the organization's overall strategic objectives.[3]

To make decentralization work, establishing the right policies is critical. The bank needs safe and sound policies for the sake of prudence and to avoid imploding. But management does not want to micro-manage the process so that, like Jimmy Carter as President, management schedules the tennis court. Scheduling the tennis court is the equivalent of a bank that requires board approval for 90% of the loans that are booked. Decentralization means that we trust the professionalism of our people and the institutional judgment that hired and promoted them. That means we establish authority for our loan officers, limits for the loan committee, and limits that if exceeded require board approval. Again, we need to know what is important and focus on the pre- and post-approval process and measure our effectiveness based on analytical comparisons of actual versus expected results.

When Alan Greenspan testified about the large expenditures being made by large banks to improve their credit management, his observations captured the essence of this philosophy.

> **"Before smaller banks rush into expensive mathematical models to gauge risk, remember that these models seek to replicate on a mass basis the very loan evaluation competence small bank institutions have. There is no superior insight into loan risks than that of a loan officer of a small bank who knows his customers for years and has a sense of their credit worthiness independent of available collateral. The most complex mathematical models hope to simulate that experience and insight."**

Big banks do not have that advantage because the size and scope of their activities preclude the loan officer from ever really knowing the customer by name. To say you know the customer means you know the capital they have, their capacity to repay, and their character.[4] These standards have been essential parts of the credit culture for decades. The challenge now is to make sure that we do not need to forgive employee mistakes very often because these standards are part and parcel of our decision-making culture.

RAPID TEMPO: Marines want to hit the other fellow as quickly as possible. In simple terms, don't give the other fellow time to react. In the banking world, that means that we can identify opportunities, make decisions, and act faster than our competition. It means we keep them on the defensive so that they are reacting to us as we maintain the momentum. In the Marines, it means leading from the front where decision-making is accomplished. That rarely means that a general must be in the front like George Patton, but it does mean that the lieutenants and sergeants are in the front. Authority must be pushed down to the lowest level possible.[5] In the Marines this affects how planning time is allocated. The rule is simple — $1/3$ of planning time is given to the commander and $2/3$ to his subordinates. How often have boards spent many hours with outside consultants to develop a strategic plan but did not communicate, involve, or empower the people who were to implement the plan?

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[3] The words "leadership by allowing risk" suggest the words from a Theodore Roosevelt's Paris address in 1910: "The credit belongs to the man who is actually in the arena, whose face is marred by dust and sweat and blood, who strives valiantly, who errs and comes up short again and again, because there is no effort without error or shortcoming, but who knows the great enthusiasms, the great devotions, who spends himself for a worthy cause; who, at the best, knows, in the end, the triumph of high achievement, and who, at the worst, if he fails, at least he fails while daring greatly, so that his place shall never be with those cold and timid souls who knew neither victory nor defeat."

[4] Some years ago, the senior credit officer of a major bank in New York City was asked for a simple standard to use when making a working capital loan to finance inventories. He replied, "If you kick the boxes of inventory and they move, don't make the loan." One team leader who did not understand the message exclaimed, "Kick boxes, are you nuts!"

[5] In the Marines, we used to call this "kicking butts and taking names." It really means leading by example, in terms of professionalism, courage, and integrity.

This may be another way of saying it is better to have a good plan well executed than a perfect one badly executed. Good execution is more likely to follow the plan if everyone believes that he had a part in creating it. A sense of ownership is a strong motivator. Even Sad Sack who might otherwise feel disenfranchised should feel he has a role in achieving the plan. Years ago, the Western Electric plant at Hawthorne conducted studies in employee productivity with a test group. The management expected to find different responses to various environmental factors. They actually determined that the test group responded positively regardless of the environmental stimulus. The study concluded that the employees felt that what they were doing was important because management involved them and made them feel important. Can you do the same thing at your bank?

COMBINED ARMS: For Marines, this would be the integration of complementary weapons and capabilities to increase their collective effectiveness. Community bankers say that they still do relationship banking and that their goal is to provide the services that generate other business from the customer. The combined arms concept begs these questions: What skills and products do we combine? How do we combine them? And who combines them? Some may want to call this combination process cross selling, but that means more than just access to the rates available on all the bank's products. In the age of the Internet, most banks do that via their Web site. Successful relationship banking means more than cross selling or schmoozing the customers periodically.

The Marines keep all "mission essential" critical functions in-house, including air, artillery, infantry, armor, and communications. The Marines make the investment in human capital necessary to ensure the efficient functioning of the combined arms team, which is a unique collocation of dedicated full-time experts. In a bank, this would include not just the lenders who make loans or the marketing folks who garner deposits; it would also include those many fee-based services, such as asset management, insurance, and brokerage services.

The classic example of combined arms is how the bank manages the relationship in terms of deposits and loans. Cross selling is a team effort because we know that the loan officer cannot sell deposits and the customer service representative cannot negotiate loans. We know these specialists must be a team that can draw on each other in an effort to maximize the potential relationship with the customer. Very large banks are not as effective at a team approach because their very size prevents them from being consistently lean and mean.

We recently heard that a director of a community bank wanted to renew a deposit at the bank, but he thought the rate being offered was not attractive. Despite a request for an alternative investment recommendation, when none was forthcoming, he logically went elsewhere and purchased a municipal security with a very attractive tax-equivalent yield. This happened despite his specific request for a recommendation (the bank's services included a brokerage subsidiary). Combined arms failed there because the bank did not identify him as a depositor whose wealth warranted individual attention beyond rate quotation when the deposit matured. There was also a lapse of discipline because customer service failed to answer his request. While the director was certainly aware that the bank had the critical functions in-house to execute the trade, he is not obliged to give the business to the bank when the service is not there. Was this lapse explained by a failure of communications, training, or loss of focus because of distractions? We can only speculate about why this happened, but we do know for certain that the bank lost the business.

Bringing It All Together

To bring it all together, say what you mean and mean what you say. Some banks will even say the customer is a stakeholder and should be involved as if he were an owner. To give the impression that the customer is an owner, banks often have advisory boards, but management rarely does more than note the ideas of the board. If you ask for ideas, act on them. If you say you have fast decisions on loan requests, make sure you have made the process responsive. If you say you want to empower your employees, develop and train them as if you mean it. All too often, managers say one thing but do another. The Sad Sack banker in the ditech.com ads plays to the stereotypes based on exactly the type of leader who is all too often just seen as an empty suit. He is sometimes even derided behind his back as "the suit" because he doesn't lead, he won't decide, and he certainly cannot be held responsible.

If there is something to be learned from the pathetic example of "the suit," it is the importance not only of leadership but also of discipline in the achievement of the mission. One veteran Marine acquaintance characterized the role of discipline this way:

The key word is "discipline" from the 4-star general right down to the private. The 4-star general must have the discipline to allow everyone below him in rank to do what it is they do best. In turn, the rank and file, from the private on up, must have the discipline to know they are receiving the appropriate tools from their superiors to accomplish their goals. When this process is allowed to happen, the result is a successful mission.

Bringing it together also means you have answered the question, "Why does the customer want a relationship with you and why do you want one with the customer?" To develop the relationship long term, there needs to be that intangible something else beyond making a profit. BNK believes that the customer must see the vision that management has for the bank and its customers. That vision must be more than a rainbow that keeps moving away. It must be felt in the service given, the products offered, and the satisfaction felt about the way problems are resolved. There will always be a bank with a cheaper loan, deposits that yield more, or branches in every county, but your success will be a function of how you bring it together. As a veteran Marine, my recommendation for successful banking is to plan, communicate, train, compensate, empower ... and lead!