

## HISTORY TEACHERS FIASCOS REPEAT THEMSELVES



IVAR KREUGER



CONRAD BLACK



LORENZO DE MEDICI



BERNIE MADOFF



TONY HAYWARD

## TAKING A LESSON FROM THE SUB-PRIME MEDICIS

The past has things to teach us, if we will reflect on it, Schulich professor notes

PAUL MARSHMAN  
SPECIAL TO THE STAR

It's 2001, and the business world is reeling as Enron Corp., one of the world's biggest energy companies, collapses amid revelations of fraudulent financial statements and billions in concealed debt. To many, it's a new low in business history.

But maybe it's not.

Go back about 70 years, to 1932, when Ivar Kreuger, head of the giant Swedish Match company, commits suicide, spawning international headlines and igniting a financial scandal that costs American investors more than \$250 million and leads to the formation of the Securities and Exchange Commission.

Kreuger, a world-famous business leader and *Time* magazine cover boy, had been running an early version of a Ponzi scheme, paying dividends out of the company's capital, falsifying the books, running dummy corporations, even forging Italian bonds to raise cash.

Today, few remember Ivar Kreuger. That is, except for the students in Managing Globally, Prof. Matthias Kipping's MBA course at the Schulich School of Business.

Unlike most MBA courses, Kipping's course focuses on the past, not the present, and on what we can learn

from business leaders' mistakes, as well as their successes.

"If you look at management books today," he says, "they focus on successful companies. But go 10 years down the road and those companies may not be great anymore. And while they're good, it's difficult to find out why."

Looking at the past is a useful approach, Kipping says, because we can see how a company's business strategies really turned out.

And students can learn as much from mistakes as successes, even if those mistakes are centuries old.

"I was amazed at how many parallels there are from even 500 years ago," says Nik Ljiljanic, an executive MBA student who took Kipping's course this year.

He points to the Medici family, one of the high-profile subjects of the course. The Medicis built a powerful financial empire in Europe during the 15th century before finally being done in by bad loans to nobles, who were clients.

The Medici bank's failure seems eerily foreshadow the recent U.S. banking crisis.

"Eventually the bank folded, because credit was extended to borrowers of questionable credit-worthiness," says Ljiljanic. "In the U.S., major banks extended increasingly risky loans to clients who had exceedingly high debt ratios."

In both cases, he points out, the banks made the same fatal mistake: In pursuit of profits, they ignored their own policies.

Kipping's course covers companies that succeeded, including historic trading companies such as Jardine Matheson & Co. and the Hudson's Bay Company; those that eventually failed, such as the Medici Bank; and those that went down in a storm of scandal, such as the Swedish Match company.

Although scandals, such as those of Bernie Madoff and Ivar Kreuger, seem to be more and more common these days, that may be just because we're paying more attention, Kipping suggests.

"We've had corporate malfeasance as long as we've had business," he says. "My course tries to teach people not to forget."

Most business people are basically honest, says Kipping, and most business failures are due to common mistakes, many of which speak to the quality of a company's leadership. He names four:

• Taking things for granted. "Things that have always worked may not continue to work," notes Kipping.

• 7-Eleven found this out in the 1980s, when its business model simply stopped working due to new competition from gas station convenience stores. It took a total rethink of the company's business model to right the ship.

The lesson is that business leaders need to be alert for signs of change, and willing to alter course when they see the rules of the game changing.

Ljiljanic says he's taken that to heart in his job as central Canada sales manager for a plumbing and heating company.

"Although I have a large sales force, I try to spend time in the field and with our customers, and get direct feedback, as opposed to relying on second and third layers of relationships," he says.

• Holding on to subsidiaries when they fail. "Managers find it extremely difficult to let go," Kipping says. "Their own reputation is at stake."

Instead, he says, they should follow an old adage of Jardine Matheson, which transformed its Asian opium trading business into a conglomerate through nimble deal-making: It's better to lose face than to lose money.

• Relying solely on systems: Although having good systems is essential, it's people who make a company successful, Kipping says.

"The key is to get good people and train them well. That will go much further in keeping them honest than any system."

Too often, Kipping says, companies think what they need is more risk management. "No, we need more good people," he says.

• Getting caught up in the euphoria. Ivar Kreuger, Kipping points out, was widely celebrated in the press, until his company collapsed. No-one thought to look into his business practices.

A business leader has to stand back and look at what's really going on, he

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*Eventually, the Medici bank folded, because credit was extended to borrowers of questionable credit-worthiness*

NIK LJILJANIC, EXECUTIVE MBA STUDENT

says, no matter what the press and the analysts are saying.

"You have to do your job as if you're looking 20 years back and seeing yourself."

And, if you do make a mistake, what happens next is critical.

As costly as these mistakes can be, failing to respond effectively when things go wrong can be just as big a misstep, says Prof. Daniel Diermeier, who teaches a course on corporate crisis-management at the Kellogg

School of Management at Northwestern University.

Diermeier argues that a company's reputation is a precious asset in today's world, and a weak response to a crisis can hurt that reputation, driving away customers. His recent book, *Reputation Rules*, deals with high-profile cases where companies' reputations were put at risk.

Diermeier calls such crises "the crucible of leadership." He points to the BP oil spill as a case where a company mishandled an already catastrophic event.

In these circumstances, he says, the public is watching intently, and the actions of top executives can be crucial.

"When you then have unfortunate comments by (CEO) Tony Hayward, such as, 'I want my life back,' or, 'The Gulf of Mexico is a big ocean,' and the chairman of the board is not acting decisively either, there are now concerns over whether the management is able to lead the crisis successfully."

In such stressful circumstances, business leaders often make the mistake of narrowing their focus to the technical aspects of the problem,

when they should be reassuring people by showing transparency, commitment, accountability and empathy for the victims.

These crises can also point out underlying problems with the company, such as BP's poor safety culture, he says.

Conrad Black's crisis with Hollinger International Inc., he says, pointed out a problem with the company's governance.

"This was a situation where there was a dysfunctional board," says Diermeier. "That can be utterly critical in a crisis, because the board can provide additional supervision, and it also can step in and remove a CEO when it really has to."

Black's aristocratic personal style worked against him, he says. "That can work nicely when things are going well and it's flamboyant, but when things turn the other way, it becomes a liability very quickly."

In the end, says Kipping, problems can occur all the way along the corporate chain.

He believes the key to preventing them is good leadership.

"A CEO is not responsible for somebody selling a dodgy mortgage somewhere," he says. "But he is responsible for not having a system in place that makes people do the right thing."

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