Thorndike Jr., William N. – The Outsiders

HBR Press, 2012, [Business] Grade ★★★★

William Thorndike has done the world of skilled but less-than-flamboyant CEOs and long-term investors alike a massive favour. Via eight years of painstaking research in collaboration with Harvard Business School students – one year per CEO/company studied – Thorndike has written a reference book for measuring and identifying outstanding CEOs. The simple approach behind the book is both its beauty and its beast; by screening for U.S.-based managers whose 1) total shareholder returns was higher than that of the poster-boy of great CEOs, Jack Welch at General Electric and 2) did it over a longer time frame. This dual herculean demand of 20,9 per cent annually over a minimum of twenty years weeded out all but eight CEOs. *The Outsiders* bring you the stories, common traits and lessons from these truly outstanding leaders.

William Thorndike is a Harvard and Stanford alumni and founder of the investment firm Housatonic Partners. His investor angle shines through in several ways; mainly in the call for a clear numbers-based yardstick in defining greatness (total shareholder return over the long term) and in the great effort of finding common, identifiable traits between these leaders. The line-up of CEOs and companies profiled in the book are save a few not exactly household names; Henry Singleton (Teledyne), Tom Murphy (Capital Cities), Bill Anders (General Dynamics), John Malone (TCI Liberty), Katherine Graham (The Washington Post), Bill Stiritz (Ralston Purina), Dick Smith (General Cinema) and Warren Buffett (Berkshire Hathaway). But the shareholder returns they have created are far from unassuming; outperformance vs S&P 500 of a factor of 20 times! Truly mindboggling.

Henry Singleton of Teledyne is the Godfather-figure that knits these CEOs together, where Thorndike cleverly uses the "Graham-and Doddsville" approach. In essence, as opposed to the pure luck factor in explaining winners of a coin-tossing game, if there are several successful members from the same population, one can safely assume a clear involvement of skill. The CEO-inhabitants of "Singletonville" have upon deeper studies a number of skills (areas of focus) in common, even though a few are borderline pattern-seeking. Among the more important ones in my opinion are the laser-like focus on capital allocation (where timely buy-backs are a heavy ingredient), decentralisation taken to an extreme, running the business on cash flow instead of earnings and keeping a very low public profile. Given the importance of capital allocation, one wonders what proportion of CEOs are actually picked based on this skill as opposed to production, marketing or "leadership" skills. Crucially, Thorndike manages to bring out supporting anecdotes and real-life evidence in all eight CEO-studies, making these shared specific traits reality, rather than just fancy words.

There are of course plenty of things separating these managers as well - had there been a Singletonian blueprint for how to produce a 20 times shareholder relative return, it would soon have lost its allure. Some used more debt, some less. Some diversified outside of core operations, but most did not. Some restructured heavily, some kept compounding away. However, they were all *unconventional*. Again the ghosts of Keynes' 'failing conventionally' and Templeton's 'you must do something differently' whisks by. But oh how hard it is, both to do and to believe in. Upon learning more about the sheer "madness" (at the time) of Teledyne's unheard of buy-backs or General Cinema's foray into retailing, I am also reminded of Philip Fisher's stocks-as-restaurant analogy.

Like restaurants, certain stocks are just not for everyone. And so it is with most of these eight companies. Even with two decades of proven success, the audacity with which Teledyne reversed course in the early 1970s spooked most investors, causing the stock to trade at a single-digit P/e. Another reminder that investing actually does offer second chances.

Henrik Andersson, April 15, 2013

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