

Ram Charan Grades the President

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Management guru Ram Charan

For almost four decades, Ram Charan has worked behind the scenes to help improve many of the world's great companies, including **General Electric**, **DuPont**, **Avon**, **Novartis**, and **Procter & Gamble**. A former faculty member at Harvard Business School, he is a corporate problem solver and an acclaimed expert in corporate governance, innovation, knowledge management, and leadership. Among his many fans are former GE chief Jack Welch, former **Honeywell** and AlliedSignal CEO Larry Bossidy, and current **Verizon** chairman and CEO Ivan Seidenberg. Charan's latest book, titled *Leadership in the Era of Economic Uncertainty*, is about managing effectively amid the global downturn.

Here he discusses President Obama's handling of the economic crisis, whether we're on the right track to solving it, and what the U.S. auto industry must do to turn itself around.

Think of the Obama administration as a company, with Obama as CEO. How would you rate his performance so far?

Given the context of the times, the bottom line for me is that as a leader, he is doing well. Obama's central strength, other than inspiring and communicating, is consensus building. He has this innate ability to build consensus, which is so important. He's also selected good people. The president, [Federal Reserve Chairman] Ben Bernanke, and [Treasury Secretary] Timothy Geithner — it's a very good team.

Internal to the U.S., there has been a widespread lack of confidence, a ton of anxiety, and great fragmentation of opinion, so people were feeling a lack of leadership. Externally, there is the perception that the U.S. is a declining nation, and that it has to accommodate itself to that reality. It cannot lecture others when it comes to the correction of the economy, because it is widely perceived — and there is a lot of truth to this — that the downturn has emanated from the U.S. In this context, despite several mishaps, I think there has been real progress. There is a definite deceleration in the deterioration of the economy. It is not rescued yet, but the pace of decline has been reduced.

What, specifically, do you think has worked?

I think several actions of Bernanke and Geithner have been very important to change the psychology of the situation. Bernanke has used the balance sheet of the Fed to flood the market with money and to reduce interest rates to close to zero. In effect, this has given credit to large, robust creditors, without taking huge risks. When the time comes, the Fed can contract the balance sheet, and there are incentives for the institutions to pay back sooner rather than later.

Second, both Bernanke and Geithner have attacked the major cause of the downturn — the flow of credit within financial institutions. The key point here has to do with toxic securities on balance sheets. The majority of these securities are in less than a dozen institutions, including [AIG](#). As the *Financial Times* recently reported, the notional value of credit default swaps has gone down from \$60 trillion to \$28 trillion in two years. That is an important part of un gumming the balance sheets.

What else has the administration done to facilitate the exchange of information and thereby restore order and confidence?

In early March, [IntercontinentalExchange](#) became the clearinghouse for credit default swaps. The idea is to create a centralized market in order to reduce counterparty and systemic risks. In effect, CDSs will be traded in a similar manner to bonds, creating a more transparent and efficient market. That is important; this was not the case six months ago.

How would you rate Geithner's performance?

You need people with domain expertise, which he has. Geithner is able to figure out solutions; he is not a pawn of any constituency in the financial market. I've seen him in action and found him a very clear thinker — he is able to see the second- or third-order consequences of a given plan. He has made some errors in communication, but he has moved ahead, and I think his plan to stabilize the banking sector, if done quickly, could correct the system.

At least now there is a mechanism for banks to find some kind of price point for their assets. If banks are not selling assets, that is because they think prices will rise. Private equity will come back to banks if [investors] see the banks have cleared the toxic stuff. Then we will see the flow of capital again. I think we will see that in six months.

How well do you think the administration uses information?

Obama has a platform of transparency — I think he wants to explain the situation and show the public what is being done so that they have a better understanding of what is happening. The problem is that the information we are getting is structured on an old framework of 30 or 40 years ago. We are using the same metrics, when we need new ones for this context. Right now, for example, the most critical need is to show information from 30 or 40 major banks — how much lending is going on and in what categories. Then people can see progress and get more confident. At the moment, though, we do not have this kind of information — or, if we do, it has not been publicized.

Evaluate the administration's management of the auto industry.

The Detroit Three [GM, Ford, and Chrysler] today serve some 45 percent of the U.S. market. That's down from 50 percent in 2007, but the market is there, and some of the products are very good. It is the structure of the business model that has been defective for some time. So the administration's approach is to use both carrot and stick: You guys — suppliers, creditors, unions, management — figure out a way to make sacrifices to get to a viable cost structure so that the companies become healthy. If you fail, you will go bankrupt and [a plan] will be designed for you.

This is a good approach, much better than giving a handout or a guarantee. The administration is saying, "You have to have a plan, and there's a time limit to do it." It is forcing the various parties to do what they haven't been able to do on their own for years.

What is a broadly applicable piece of advice that companies today can benefit from?

First and foremost, you have to tailor your approach to changes in the external context. For example, in 2007, 71 percent of U.S. GDP came from consumption. That is not coming back; the new context will be somewhere between 60 and 65 percent. Why? Because I expect the sense of anxiety to remain for a while; people will therefore **keep saving**. Also, the availability of credit will be lower, so there will be less leverage. That means people will be spending their money differently. You have to do the analyses and get operations ready for that change. And then you have to match your investment to the new realities of consumer behavior.

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