VIDEO SERIES

LEADERSHIP IN THE FIELD: Interviews With Global Leaders

By Russell Reynolds Associates
with Roger O. Crockett

Jim Rohr, PNC Bank's Chairman & CEO talks about managing risk, partnering with regulators, and acquiring top talent in the Digital Age.

PNC Bank's Chairman & CEO On Risk, Regulation and Talent

An Edited Transcript

Chapter 1 - "Sometimes it's the things you don't do that help save the company."

Roger Crockett: **You led the company to some of its best years and that meant avoiding the sub-prime disaster right? What are your secrets to anticipating some severe events in the market such as that, so that you can be successful?**

Jim Rohr: That's a great question. We use the concept of a risk-adjusted return on capital, and every single activity that we have we look at the risk adjusted return on capital. To use your example of the mortgage business, in the late 90's Fannie and Freddie had taken all of the profitability out of the basic mortgage business, and they grew their balance sheets to a combined $7 trillion. With their funding and their leverage ratio as a government agency, frankly, the banks really didn't make any money on the basic mortgage business. So, the head of our mortgage company came to me and said, "Here's our risk-adjusted returns and there has been a lot of focus on it. The only way you can move these up will be to go to sub-prime." And he said, "Let me explain what happens in sub-prime. There's no down payment, there's no coverage for the income, and when the recession comes it ends in tears." And so we sold the mortgage company. We weren't getting the right return. We'd looked at the future, and the risk profile that was going to be required simply wasn't consistent with the kind of returns required. So we sold the mortgage company in early 2002.

Sub-prime lending went from 3% to 37% of the mortgage business. Everybody went to sub-prime. Everybody basically made a bet on US housing prices. Those housing prices had gone up for 25 years, but like some things in life, they're good until they're not. And if they're not, then they're very bad. And that's what happened to us this time. So a lot of times it's things you don't do that help save the company.

Roger Crockett: **And perhaps it has to do with staying true to your core principles because it would be very enticing to go after the numbers that everyone else did in sub-prime, right?**

Jim Rohr: Well, for sure. We were criticized actually in 2004, 05 and 06 by some shareholders who said, "You're not growing loans fast enough." And we said, "We didn't like the kinds of loans that other people were growing, and we didn't get the right risk-adjusted returns. You have to maintain your discipline around your values.

Chapter 2 - Managing Risk

Roger Crockett: **Jim, would you share a few of the approaches you take as a company to making sure that everyone understands and manages risk appropriately?**

Jim Rohr: Risk is in everybody's business and it's always been in everyone's business. But I think frankly the pace of change today and the kinds of flexibility that all of this communication and the Internet provides, has caused change to be much more rapid. So the sense of risk is different, and it takes an empowered group of people, the entire company, to be in the risk business. We tell everybody in the company, every single town hall meeting I ask people whoever's involved with risk please raise their hand. If they don't all raise their hands then we have a misunderstanding.

We're serious about it. Because many people around the company have heard me say, "If we have a teller cashing a fraudulent check it doesn't matter who the chief risk officer is, we have a risk and we're not managing it." Virtually every company is in some form of risk business, so it's the management of risk, not just the taking of risk that makes you successful over time.

Roger Crockett: **Now are you speaking just of financial risk, or are you speaking of risk more broadly than that?**

Jim Rohr: Every single person in the company, no matter what activity they're involved in, is in the risk space. So it's easy to say that somebody who's lending money or trading securities or buying bonds is in the risk space. Let's take our advertising group, not one that would be immediately thought of as risky. However, if we say the wrong thing in the press, reputational risk today is maybe as costly as anything that a bank does, or maybe any company for that matter. So every single part of the company is really in the risk space. Operational risk, we take a great deal of operational risk processing people's checks. We've got many people who are trying to crack into our systems every day, we have to protect our depositors' money, and so those are all different kinds of operational risk. There's lots of different risks that the company takes, and everybody in the company has some piece of it.

Chapter 3 - "Regulators are real people."

Roger Crockett: **Well, let's turn to another area of change, which is the area of regulation in your industry. Companies in all industries are now forced to be far more transparent. How does your board manage this new era of regulation?**

Jim Rohr: I think we have to be very transparent with the board as well. We have our regulators meet with the board. We actually have the regulators meet with different committees of the board so that the board understands where the regulators are coming from. So that it's not always the exact way you read about it in the paper. Regulators are real people. Frankly, the regulators want the industry to succeed. They get no pleasure or benefit out of the industry failing. And so in the end, the regulators can actually be your partners. In many ways they are, and that's a good thing. You have to understand that they have a perspective that's different than yours, sometimes broader and as a partner that can help. So that's good, but you also have to understand that they're in the business of protecting the depositor. And the company has a broader responsibility to shareholders, employees and depositors. By the way, the shareholder doesn't do too well if the depositors doesn't do well. So it's not in conflict, but we do have a little broader agenda than they do.

It's good to have these broad communications with the board on the regulatory front. Every board meeting we have a regulatory presentation. We have a chief regulatory officer and he makes a presentation to the board on where we stand on all of our exams, all of our ratings. We're very transparent with the board ourselves and so are the regulators. It's a big part of our business, bigger than ever now with the regulations changing. And you have to manage it.

Roger Crockett: **And, of course, you had to grow over the years in coming to that understanding of the importance of regulation. Talk about some of the lessons that you've learned over time in adjusting to the pressure of regulation.**

Jim Rohr: Well, we did have a time where we agreed with the auditors on an accounting issue. The regulators disagreed, and it was a problematic issue for the company.

You have two different sets of regulators and we had a conflict between the SEC and the Fed. You've got to work your way through that, and we were not as proactive as we might have been, and we learned from that. We needed to be much more proactive and understand that they were our partners.

Chapter 4 - "Talent acquisition starts from the top down."

Roger Crockett: Let's talk a little bit about talent acquisition. You mentioned earlier that you have talent on the team that focuses on regulation, for example. You've also been successful at recruiting unique talent from different parts of the industry. What is your approach in this day and age to talent acquisition?

Jim Rohr: Talent acquisition is as important a thing as you do within the company, because the people are the company quite frankly. And so I think we realized some time ago it's not just the recruiting department that was in the talent acquisition business. I often use the example of our diversity officer. If our diversity officer was in charge of hiring all the diverse people that we need the company has no chance of being successful. Just like if the risk officer was in charge of all the risk we couldn't possibly be a success. So you have to really understand that it's everybody's business, if not everybody then many people's business, to recruit people to come to the company.

I myself get involved in recruiting senior leaders. Any company needs to understand they have to have a group of diverse people with diverse talent and diverse culture in order to pull together the kind of expertise they need to be successful in their business. And you have to do that at the top but also all the way down too.

Roger Crockett: Well in particular, you've brought in some talent that has been impressive on the financial side - your CFO; also in PR and in technology. Why were those areas important for you?

Jim Rohr: Well, every company has to understand which areas are the most important areas in the company. As the CEO, bluntly you've got to understand what you're good at and what you're not good at. And that's true for every manager really. So, you have to be able to go out and recruit and develop the kinds of people who have the expertise that you don't. In the case of a financer, we went out and recruited an excellent finance person in the area of asset liability and management. Today we have a real expertise in asset liability and management that we didn't have before. And on the public relations side, we had a long history of not being particularly good at public relations, and it is a business. You have to understand that public relations is a fulltime business. In communications and public relations we went out and hired a group of people that I'm particularly confident in, and I think we're pretty good at that now.

So, you've got to really be honest with yourself. It starts with honesty with yourself, about what you're good at and what you're not. And you've got to be honest about your team as to who's good and who's not and who's developable and who's not. Hopefully, we're able to develop from within in all of those areas, but if you don't start with excellent leadership you have a hard time.

Chapter 5 - The digital transformation.

Roger Crockett: Well, one of the most dramatic areas of change of course has been in the digital technology area and I know you've hired there. How important in your mind is it to have digital acumen on your team in this day and age?

Jim Rohr: Six years ago there was no Skype, no Facebook, no Twitter. Apple was on the verge of bankruptcy and Blockbuster Video was the number one entertainment company in the United States. That's six years ago, and my goodness how things have changed.

It's not going to stop. Change is going to be with us right along. And so if you embrace change you have an opportunity to really win. If you want to just say, "Okay, well I'm not going to change and I'm going to keep doing it the old way," you have no chance. And so what we've done in PNC is we've used some outside consultants, and we've hired some people inside. But what we really do is we rely on the businesses to talk every quarter about what things are developing in the new world, the digital world—whether they're going to use Twitter or how the online system is changing, what kind of electronic payments systems do we have, what are the enhancements we're building to 'myCFO' so the small business can interface with the internet differently? So that's embedded in each business. I know some companies will set up an innovations office. So, there's an innovation officer who comes and tells you how to interface, and that might be successful for them. But really the way we look at it is that every business, every activity is in some mode of change. And so everybody in those activities has to have this pace of change mindset so that they can keep up with what's going on in their part of the company.

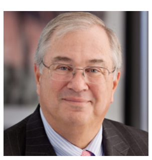
Roger Crockett: **So, everyone across the company needs to be serious about innovating?**

Jim Rohr: Yes, everybody. Whether it's operational, whether its communications or whether it's the payment sector, everybody has to be in the innovations business.

Roger Crockett: **You say you've brought in some outside consultants. You've also brought some CEO's and Presidents in the tech industry to talk to your board—to remind them how important change is, right?**

Jim Rohr: Absolutely, we've done that with various presidents of different technology companies who come and speak to our board every year. So the board gets a sense of how rapidly things are changing. Now, some of the board is intimately involved in technology themselves; we've got the retired Chief Operating Officer of Verizon.

So, it's important to bring refreshers to the board in terms of CEO's of technology companies. And obviously we're in the marketplace every day talking about it across the company.



Jim Rohr is Chairman and CEO of PNC Financial Services Group. Since becoming CEO in 2000 and Chairman in 2001, Rohr has earned praise for leading PNC amid challenge and change. Under his leadership the bank avoided catastrophe during the nation's sub-prime mortgage crisis and survived an accounting investigation that forced a restatement of the bank's earnings. Rohr's steady hand comes from years of experience at PNC. After arriving as a young prospect in 1972, Rohr excelled in various marketing and management roles before rising to president in 1992 and COO in 1998. Rohr is also a director on the boards of BlackRock Inc., ATI, EQT Corp, and the RAND Board of Trustees.

Roger O. Crockett is a veteran business writer, thought leader and speaker. He is the former Chicago Deputy Bureau Chief for *BusinessWeek* magazine and a contributor to *Harvard Business Review*. His perspectives on business, leadership and diversity are trusted by many of the world's top executives and entrepreneurs.