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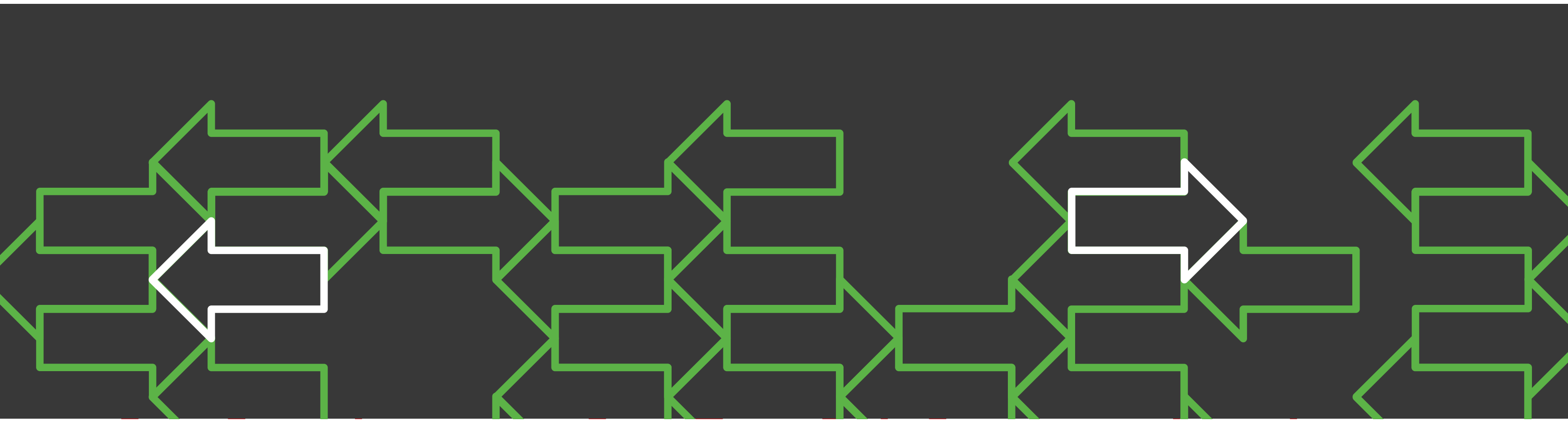
Picking the wrong leader can cost you your investment



Private-equity firms investing their limited partners' capital are generally adept at collecting and analyzing hard data as part of due diligence and postacquisition planning. But what about assessing the most-critical success factor not represented on the balance sheet? In other words, how to answer the crucial question, Who is going to run my company successfully, get a good sale price, and allow me to invest in the next opportunity?

THE CEO

Assessment of the chief executive of a newly acquired portfolio company, like the selection of a new executive for any company, should take the form of a comprehensive process designed to lead to a thorough understanding of the executive and that executive's strengths, weaknesses, and true fitness to lead the portfolio company during the next phase of growth under private-equity ownership.

The first step is clarification of what will be required of the executive: what specific outcomes will the executive be held accountable for in the next one to three years in terms of financial targets, operational goals, talent building, culture building, board deliverables, communication expectations, and so on? Such a calculation can be called the leader's role accountability matrix. It sets the stage for a dispassionate, clear-sighted, evidence-based evaluation of the incumbent executive against the specific criteria that define success for that role in the new context.

Once the critical-outcome criteria have been clearly defined, assessment of the executive leader begins. Historically, an interview has been the primary selection tool used. However, we have found that, although important, an interview alone is not sufficient to gather the data necessary to predict success. That's because an interview is fundamentally backward-looking. One's history is important, but it is incomplete because by definition it does not reveal growth potential, traits, abilities, or competencies that are present but dormant. A history neglects the powerful interaction effects of leader and future environment. We advocate instead a multidimensional assessment of the individual leader—one that encompasses personality, motivations, cognitive abilities, business acumen, experience, performance, learning agility, and potential for growth within the future environment.

THE MANAGEMENT TEAM

Assessment of the team of executives under the CEO involves a process similar to that of the chief-executive assessment but with one important difference: alignment of the talent is absolutely critical. First, however, it's important to take time to confirm whether or not the current management team structure makes sense for the future needs of the business. If any restructuring of roles or team makeup is determined to be required, that restructuring must occur first; with a change in control, investors have a rare opportunity to make foundational structural and role alterations. Only then should role accountability matrices be defined and existing members of the team evaluated.

Being a productive member of a management team means not simply serving as a strong functional contributor or group leader but also contributing value to the shared, enterprise leadership work of the senior team. It is critical that the members of the management team form a genuine team, which means (1) they align with the vision, mission, and values set by the CEO and board and (2) they behave in accordance with principles and standards that are either explicitly stated or implicitly understood. Many companies have A players within their management ranks, but those people are not aligned as a cohesive, collaborative leadership team. Such a situation very often limits results.

FIGURE 1: TYPES OF ASSESSMENT AND DEVELOPMENT ACTIVITIES MOST RELEVANT FOR PE-OWNED PORTFOLIO COMPANIES

Assessment	Development
• CEO assessment • Board effectiveness assessment • Management team assessment • Talent audit • Organizational effectiveness assessment • Culture assessment	• Board and CEO alignment advising • CEO/senior leader executive (integration) coaching • Executive team alignment • High performance team development • Talent development strategy • Organization design changes • Strategic culture change • Post-merger culture integration

Source: AlixPartners

THE ORGANIZATION AND ITS CULTURE

Of course, organizational effectiveness beyond just the leaders themselves plays a significant role in a portfolio company's success. A private-equity transaction represents an inflection point that typically requires certain new skill sets for all employees to acquire. And that raises a host of other questions: Who has those skills? Who doesn't? Who can develop them? How will it be done? Who is being recruited? Who is being promoted? Is talent being deployed effectively? Would a different structure better meet future demands? How do communication and decision making support the desired direction?

Those visible behaviors – communication patterns, decisions and decision-making patterns, and numerous others – are the manifestations of culture. Culture is that set of implicit shared values, beliefs, and assumptions that influence how individuals in an organization think, behave, and react. The proficient assessment and proactive advancement of a culture that is aligned with business strategy are critical elements in value creation.

The question at any transition point in the life cycle of an organization is, Does the organization have the right culture to align with and amplify the business strategy and achieve the desired results?

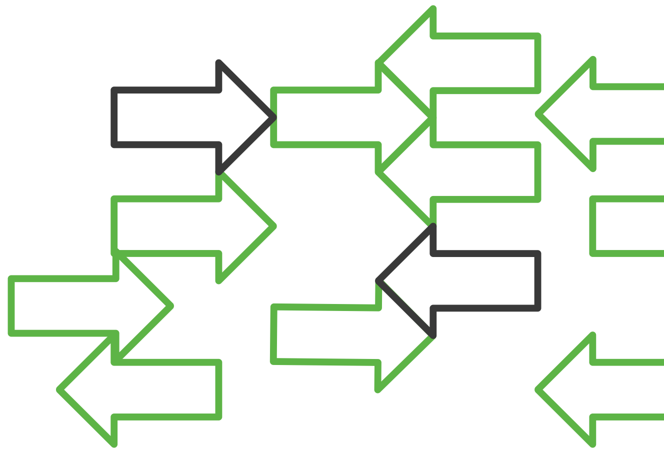
While companies may spend significant time and resources installing the right structures and operational processes, they often overlook the power of their organization's culture to guide workforce productivity and outcomes such as innovation, lean operations, customer engagement, or pursuit of a new growth strategy.

Organization-level assessment is typically accomplished by collecting necessary data by way of a combination of methods, including surveys, focus groups, select interviews, talent audits, and performance reviews and then of course analyzing these data. All of those methods can be conducted quickly and efficiently when the questions have first been constructed clearly.

In addition to understanding a culture's elements and determining whether those elements support—or inhibit—achievement of the business strategy, it is useful to evaluate employee engagement, readiness for change, and attitudes toward or specific understanding of such major issues as diversity, strategy, goals, and regulatory requirements.

CONCLUSION

Just as it doesn't make sense to acquire a company without first digging into its books or operations, it doesn't make sense to do so without first examining the company's executives, talent, and culture. It's just as important to address a misaligned or poorly functioning management team as it is to examine, say, a 50% rise in selling, general, and administrative expenses. Leadership challenges can be ambiguous and difficult to assess, and it's for that very reason that investors neglect them at their peril. A



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