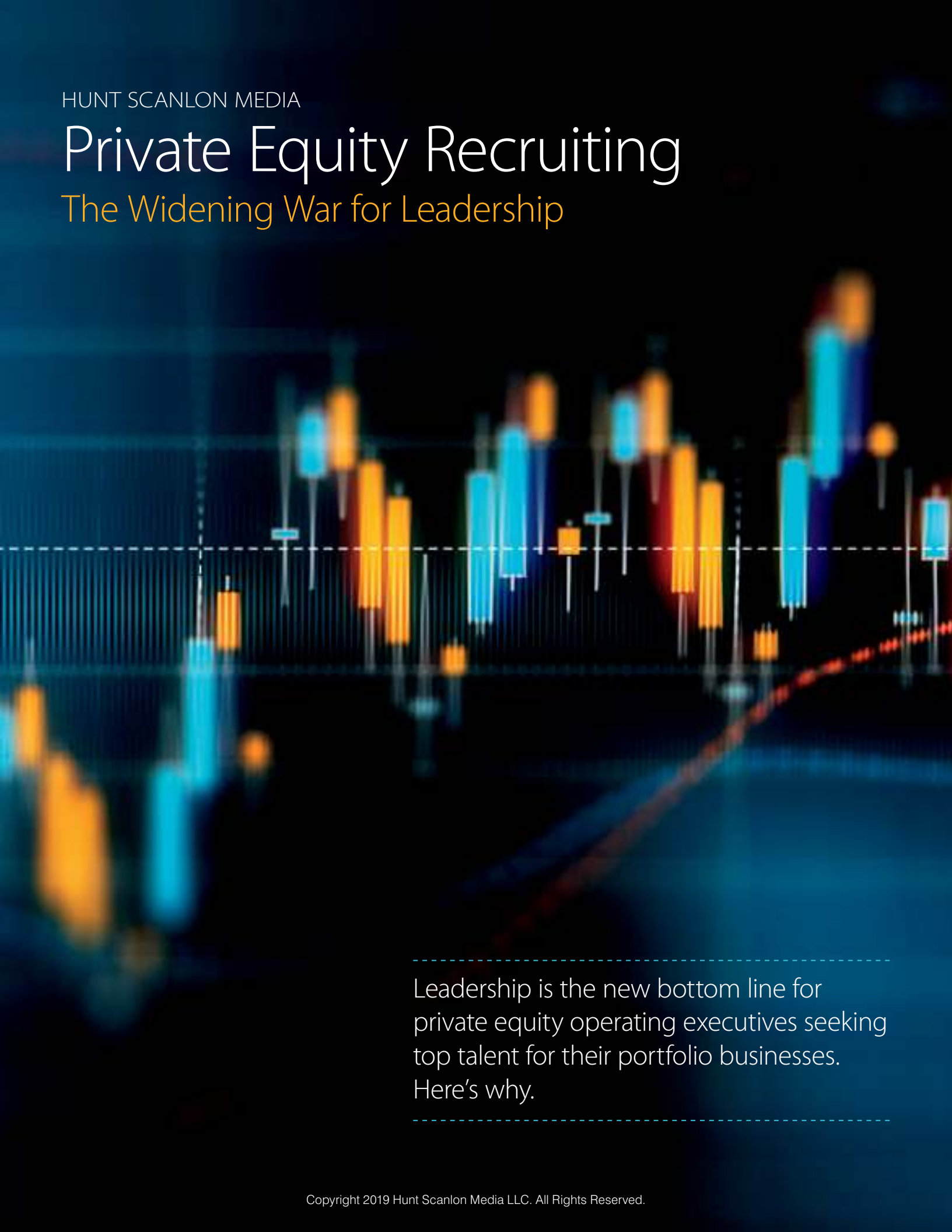
HUNT SCANLON MEDIA

Private Equity Recruiting

The Widening War for Leadership



Leadership is the new bottom line for private equity operating executives seeking top talent for their portfolio businesses. Here's why.

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ABOUT HUNT SCANLON MEDIA

Hunt Scanlon Media is the most widely referenced, single source for information in the human capital sector. Our mission is to inform, engage, and connect you — the most avid members of the talent management community — with daily news and expert commentary. We have assembled a team of trusted, experienced reporters and editors to track who is making news and what's driving the market around the clock. And we have one of the best management teams in the field.

Hunt Scanlon Media has been defining and informing the senior talent management sector for over 30 years. Our global staffing intelligence data comes in many forms: daily newswires, annual leadership and state of the industry reports, market intelligence sector briefings, industry rankings and our flagship newsletter Executive Search Review. Our exclusive news briefings, interviews, industry trends reports and rankings, forecasts and expert commentary offer unique insight and market intelligence as we track global talent management developments. Since our inception, talent management professionals worldwide have turned to Hunt Scanlon Media.

Hunt Scanlon Media's global news network is the most comprehensive in the talent management field, and all of our lead stories, rankings tables, news alerts, and thought leadership articles provide the latest thinking in a sector that is highly evolving and in transition. Our editorial team covers news nationally and globally, originating exclusive news briefings each day that provide up-to-the-minute coverage of the entire talent management and leadership solutions sector. Today, Hunt Scanlon Media interfaces annually with more than 20 million human capital professionals in over 191 countries — from CHROs, chief talent officers, talent acquisition specialists, company directors, and top decision-makers in finance, IT, sales, private equity, and marketing, to the global leadership and talent solutions consultants who service them.

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SECTION 1

Executive Summary

SECTION 1

Executive Summary

The private equity sector is now the chief driver of growth at recruitment firms across the U.S. Last year, records continued to be broken as upwards of 40,000 deals involving venture capital or private equity financing, mergers or acquisitions were consummated across the country, according to research group **PitchBook**.

Indeed, business has been booming across the industry. Last year, PE firms in the U.S. enjoyed a total deal value of $713 billion from a record 4,828 deals, up 17.2 percent and 5.5 percent respectively from 2017. In the last seven years, PE firms have raised $3 trillion, according to industry data provider **Preqin**. And—for better or worse—$1.14 trillion in dry powder waits to be deployed.

One hardly needs to look beyond **Blackstone Group's** latest buyout fund to get a sense for just how sold investors continue to be on private equity. Blackstone's eighth buyout fund hit $22 billion this spring, and with no set target seems certain to soon break **Apollo Global Management's** $24.6 billion fund record, set in 2017. More mega-funds – from **Vista Equity Partners**, **Advent International**, **TPG** and **Warburg Pincus** – seem to be in the offing, according to Preqin.

Yet beneath the unflagging optimism that PE firms will continue to produce stellar returns lurks a growing pressure to deliver the goods. Raising the heat is a constant murmur about an imminent decline in the economy (not all bad, admittedly, for an industry that thrives on cheap deals). Many professionals, meanwhile, are uneasy about the mounting stockpiles of unused capital. And though competition grows ever more fierce, there are fewer deals to go around, especially at good prices.

The Search for Talent

At the same time, massive societal change is underway. Technology is reshaping the face of work, and forces like artificial intelligence and machine learning are poised to bring about even greater disruption. "The resulting job displacement could be massive—think Industrial Revolution massive—affecting as many as 800 million people globally by 2030 and requiring up to 375 million of them to switch occupational categories and learn new skills," says a recent report by **McKinsey & Company**. Companies are already feeling the heat. Fully 60 percent of global executives in a recent McKinsey survey expect that up to half of their organization's workforce will need retraining or replacing within five years. An additional 28 percent of executives expect that more than half of their workforce will need retraining or replacing. More than one-third of the survey respondents said their organizations are unprepared to address the skill gaps they anticipate, reports the consultant.

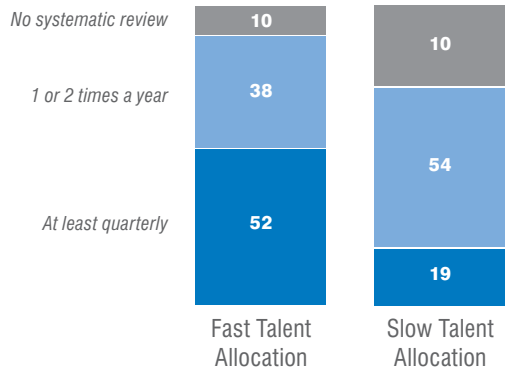
To overcome such obstacles and to continue to provide value for their investors, private equity firms are looking to top talent more than ever before. These days, and for the indefinite future, finding the best leaders for their portfolio companies is not just important—it is imperative.

Finding those individuals who can create value is growing increasingly challenging – and it has given rise to the executive search industry's recent explosive growth across the sector. (see table page 10). With Baby Boomers retiring, the talent pool only grows smaller. Near-full employment is also making finding good people a much more difficult task.

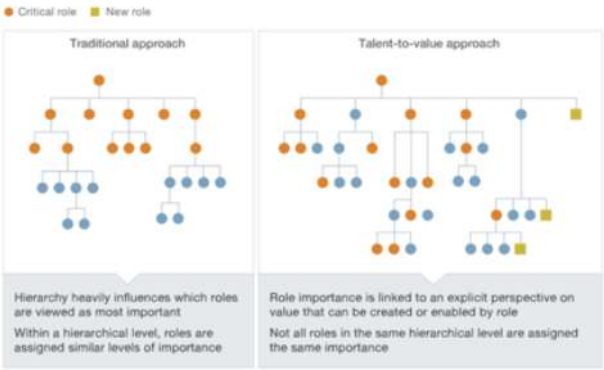
BY THE NUMBERS

About Half of the Companies Identified as Fast Talent Allocators Review Talent Placement at Least Quarterly

Frequency of talent-allocation review
% of responders (n=628)



Roles That Drive or Enable Value Can Be Found Across an Organization



Source: McKinsey & Company

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Note: *denotes the firm works primarily in the Private Equity sector

"I don't know if it's a crisis," says George Davis, CEO and founder of advisory firm **Davis Partners Group**. "But the demands are higher than ever. The stakes are higher than ever. Because there's so much money at play right now and the deal valuations are so high, it's really going to take performance to get the returns, and that means leadership."

"There are a record number of funds," says Mr. Davis. "Not only are the sums themselves huge, but they haven't spent it yet. With so much dry powder, when you buy something the prices are incredibly high. And once they're incredibly high you've got to create a multiple to really get something that you paid a lot of money for, and you've got to make so much in increased revenues just to break even on your deal. That puts a real strain on the talent equation."

Strategic, Not Transactional

Alan Guarino, vice chairman in the CEO and board services practice at **Korn Ferry**, says that business, and PE in particular, has entered what he calls "the talent age," a new day in which technology no longer trumps talent and talent is fast becoming the key to success.

"If you were to look at both private equity firms and public companies and you identified the ones that have outsized returns, I suspect the returns would have been driven far more by the people than by the actual products or services," says Mr. Guarino. "It stands to reason that if you're trying to optimize your investment, you need to optimize the people. That costs money, and that requires technical skills provided through the human resources function; so leaders and boards must invest more heavily in that function."

Mr. Guarino speaks of companies needing to bring an integrated approach to their efforts to maximize value. "A holistic approach means strategic human resources, not transactional human resources," he says. "So it

Q&A

It's All About Human Capital

George Davis is the founder and managing director of Davis Partners, an advisory firm specializing in board and CEO evaluation, succession planning, strategy implantation and management effectiveness and assessment. He previously served as a managing partner and executive committee member of Egon Zehnder, where he led the global CEO and board practice areas.

In the following interview, Mr. Davis discusses a broad range of human capital issues and the hunt for great talent.

How has your experience working in executive search helped you transition into private equity?

It's all about human capital. The acquisition is about financial capital but the performance and the return is going to be all about human capital, and after 30 years of specializing in leadership selection it was a quite natural transition.

Describe your expertise.

Having led a global CEO practice really gave me the expertise to hone in on the key leadership roles immediately on whether to assess the current management teams capabilities or their gaps or to replace members of the team overall.

Explain the leadership needs of portfolio companies.

The key needs of any portfolio company to be addressed first is the quality of the CEO, the person who's got efficient strategy and can then operationalize that strategy. The second one is an operational CFO. I think that's one of the hardest requests that we get and have the hardest time. There's a lot of controller types but someone who really knows how to understand the levers of the business and how to move the business could be a huge asset to any CEO or leadership team.

Can you give us an overview of the current state of the private equity sector?

Private equity is hot right now. There is so much money free in the market. I've seen everybody just flat out busy. Valuations are high. So trying to find real value in terms of what they're acquiring is harder and harder. I also see a trend to much more value long funds where people are holding these assets for longer periods of time. So instead of three to five years, it's now maybe five to seven years. And the huge consequence of that is it's all about the human capital factor because you have to grow your way to success. You can't just cut costs and get a quick buck return. It's rather all about people. And I've seen a tremendous surge in private equity firms seeking experts who can help them with their talent needs. It's an explosive time for the PE sector.

THE PEOPLE DIMENSION

New Leadership for Portfolio Value Creation

Korn Ferry's global PE practice works with clients to grow and proactively manage people and organizational risks. The firm draws on its knowledge in leadership and organizational consulting, global reach, and deep industry and functional expertise.

Along with that, Korn Ferry brings predictive research-based intellectual property across key disciplines, including executive assessment, top-team composition and effectiveness, organization design and restructuring, CEO and executive leadership development, succession, and talent management.

As a result, Korn Ferry plays an integral part in ensuring value-creating transactions for its clients. In addition to advising PE firms on talent pre-acquisition, the firm also works with PE firms' portfolio companies on all people and organization dimensions of their growth plans, across the investment lifecycle.

Leadership Offerings:

- Due Diligence Leadership Assessment
- Post-Investment CEO and Top-Team Effectiveness
- Organizing for Growth
- Talent Strategy

Source: Korn Ferry

requires a focus on talent strategy that is equally as intense as the focus on the business strategy."

The talent plan, of course, must follow and be aligned with the business strategy. "And so holistically that means everything from an organizational design that's going to be optimal to execute that strategy, to assessments using sophisticated HR assessment tools to determine whether you have the right athletes in each role," says Mr. Guarino. "A great CFO for one strategy may be the wrong CFO for another strategy. And so it's not about whether the people themselves are good or bad, but rather are they optimal for the role in the context of that strategy."

Mr. Guarino speaks of companies needing to bring a comprehensive approach to their efforts to maximize value. "A holistic approach means strategic human resources, not transactional human resources," he says. "So it begins with the same level of intensity oriented on a talent strategy that you probably already are putting into the investment of a business strategy."

Keith Giarman, managing partner, private equity practice, for **DHR International**, recognizes that having plenty of capital and plenty of deals are all part and parcel of the PE industry. "The most scarce resource is the people," he says.

There is no shortage of talent per se, says Mr. Giarman. But the kind of talent that is most needed today can be tough to find. "There is not enough talent that really operates with the disciplined accountability that goes hand in hand with very tightly defined value creation plans, and the key performance indicators that need to be measured along the way," says Mr. Giarman. "The CEOs of the world come in different shapes and sizes as do the CFOs. On the CFO side clearly things have evolved into a much more important emphasis on strategic and operational capability not just accounting process and control and reporting. Really drilling into the business, understanding it, working with the peers, to drive profit and cash flow. But yes, when you think about what they're trying to do with a very tightly defined plan, where execution and minimal tolerance for poor performance is part of the process, the pool of talent that thrives in those environments is smaller and you can't just look at the ones that have experience doing it or there won't be enough to choose from."

David Ferguson, portfolio manager for **Perella Weinberg Partners**, a middle market private equity group, says that finding good talent often depends on geography and the functional area of any given role. "There are a lot of private equity firms today and

HIGH IMPACT

Chief Talent Officers in Private Equity Sponsored Companies

The importance of chief talent officers within private equity concerns cannot be overstated. To run efficiently, PE firms need top-flight C-suite executives and equally talented management teams to support them.

For more than a decade, Keith Giarman has been overseeing board, C-suite and senior-level search assignments. With a 'value creation' mentality, he serves as head of the PE practice at DHR International.

What is the importance of chief talent officers within private equity?

Private equity firms recognize that for a company to run smoothly, it needs a highly qualified CEO and equally talented management team across all functional disciplines. Increasingly, PE firms also realize that to support their CEOs and position them for success, they need a CTO to provide human capital services to operating partners, portfolio company boards, and management teams. The specific responsibilities placed on the CTO can vary.

Describe some tasks a CTO might be required to perform?

CTOs may be asked to oversee key executive searches, provide information about the technical aspects within HR, or help identify organizational weaknesses before a deal closes. They also may be asked to serve as an internal consultant when search, executive assessment or organizational design firms are being considered for specific assignments. Generally, though, certain elements remain consistent. CTOs need to build long-term relationships with peer deal and operating partners as well as portfolio company leaders, and take advantage of external help when necessary. They must proactively recruit on an ongoing basis, but also be ready to act quickly when a vacancy unexpectedly arises. Bottom line: they must ensure that CEOs are viewing HR strategically at all times. Chief talent officers, in short, have a powerful, and positive, effect on recruiting, retention, overall operations and productivity, establishing the position as high-impact and essential in effective value creation.

there are a lot of private equity firms who are looking to change, swap out, upgrade their various members of their management team," he says. "So we have found it increasingly difficult to find people like chief financial officers, which you would think there are tons of people out there with that experience who have been training for that job for a long time. But it varies by market. We're in the market in Seattle, in Northern California and in New York City today looking for chief financial officers, and it's really very specific to what it is we're looking for in the individual and where it is we're doing the search. But we are finding it more challenging than it has been in the past."

Not everyone tied to the PE industry agrees that unearthing talent is any more difficult today than in years past. "There's always a demand for talent, especially at the leadership or C-suite level. The reality is if you've got a solid equity sponsor and it's a strong opportunity in a sound industry, you will find the right talent out there. There are always people, particularly at the CEO or CFO levels, who are ready to lead in that particular role," says John Marshall, founder and CEO of **JM Search**. "We commonly see people who may be the No. 2 person in a large-cap equity sponsored business or in a publicly traded company who have the ambition, experience and ability to lead at the top. They know how to get things done, have proven P&L responsibility, and they are hungry for more leadership responsibility. There's talent out there, especially in good situations."

Like Mr. Ferguson, however, he has witnessed plenty of competition for top-notch chief financial officers. "The greatest challenge right now is finding great CFOs, because really good CFOs with the right experience and qualifications are in high demand," says Mr. Marshall. "We just did a CFO search and I was talking to the candidate that we placed. He said, 'You know, I've got to tell you, I probably get 10 calls a week about opportunities.' So it's highly competitive to attract experienced CFOs who have successfully navigated through a deal, and bring the know-how to work with an equity sponsor."

Mike Myatt, chairman **N2Growth**, a global leadership consultancy, also finds the talent pool not to be unduly drained, especially for recruiters that thoroughly understand the unique nature and needs of the PE sector. “I think it’s actually a really good time,” he says. “There’s a lot of change going on in the market. There’s a lot of consolidation both at the macro and microeconomic levels, and so there’s a lot of senior executive talent looking for new opportunities, especially those PE opportunities with near to mid-term event horizons.”

Growing Companies at Scale

“I would say that probably the biggest thing that all investors are facing today is not so much a talent shortage but rather understanding that we’re in a global workforce talent transition,” says Mr. Myatt.

"The significance of technology change on business and business models is huge. If leaders don't really understand digital reinvention, digital reimagination, digital transformation, if they don't understand how to deal with the impact of evolving technology and really work that into the fabric of whatever business they're stepping into, they're not going to get the results that they're looking for. When you look at a PE firm and you look at the valuation bump that you get for a technology forward enterprise, you literally get a force multiplier on valuation if you're a digitally relevant business. Moreover you can attract better talent, you can compete with greater agility, and you can increase value propositions against competitors that are maybe lagging in that regard. It's one thing to vet candidates for 'fit.' But vetting for 'add' is what makes things interesting. Leaders that can grow companies at scale is what PE firms are looking for."

When talking about private equity, change is the operative word. In the 19 years that Lori R. Sabet has worked for **The Carlyle Group**, she has seen a massive transformation of the industry. "In the beginning private equity was much smaller," says Ms. Sabet, a managing director and chief human resources officer. "It was very attractive to people coming out of business schools because you could jump in and start working on deals immediately, whereas maybe in a corporate setting or at the banks it took a little longer to have a seat at that deal table. And so, really, you almost could put a sign out on the curb and you would have candidates lining up. As the industry has matured and the tech firms have built up, and people began wanting more balance in their life, there has been more of a shift. There's just more private equity concerns now than 10 to 15 years ago," she says.

"We also are realizing that having a diverse talent population within our firms makes a difference in value creation, when we're working on deals or in the support we're providing to our portfolio companies. And so that talent pool is much smaller and it's much more competitive."

She says private equity firms are starting to recruit and court candidates much earlier. "I'll give you an

CASE STUDY

How Carlyle Creates Value

THE CARLYLE GROUP

Deep industry expertise. Global scale and presence. Extensive network of operating executives. And a wealth of investment portfolio data. They call it The Carlyle Edge. These are the four pillars of Carlyle's value creation model. By leveraging these core capabilities and resources — Carlyle has established a 30-year overall track record of investing in companies.

A successful partnership involving Carlyle, Bain Capital, Thomas H. Lee and the management of Dunkin' Brands Group drove significant operational improvement and growth in Dunkin' Brands, transforming it from a regionally focused collection of brands, buried deep within a large public corporation, into a thriving franchisor of quick-service restaurants with extensive global reach.

With Carlyle's support, Dunkin' opened 2,125 new domestic Dunkin' Donuts stores, validating the opportunity for Dunkin' outside its core geographies

Key Value Creation Metrics

- Enhanced the leadership team by recruiting senior managers with deep retail, QSR, foodservice and franchise company expertise.
- Entered new U.S. markets with Dunkin' Donuts concept, validating opportunity in new geographies.
- Expanded both brands in key, fast-growing international regions, such as Asia and the Middle East.
- Strengthened Dunkin' Donuts U.S. unit economics with initiatives to lower new store development and food costs.
- Introduced menu innovations focused on the brand's core products as well as new, related offerings.
- Significantly improved marketing for both Dunkin' Donuts and Baskin-Robbins.
- Increased LTM EBITDA by 71 percent during Carlyle's ownership, with margins expanded by 866 basis points.

example: the associate recruiting program process. When I started, you were recruiting in December for second year analysts on the street to join you in the summer. I thought that was crazy, that many months out. Now you are doing it at about 20 months out. So these individuals are graduating college literally are on the street for four months, and we are out there running our recruitment process for them to come and join us 20 months later, because there is such a war on that talent. To get that top talent, out of a class of 2,000, how do you really know that after four months of experience? But you don't want to be the one left at the curb."

Pressure to Evolve

At Carlyle Group, as with virtually all firms, the very nature of the work has evolved. This was evident last year, when Carlyle's new co-CEOs – Glenn Youngkin and Kewsong Lee – stepped in to replace the three founders who built the firm. Hailed as "Private Equity's Next Generation" by Bloomberg, the pair are charged with bringing new ideas and approaches in an industry in flux.

"Deals are moving faster," says Ms. Sabet. "There's new edges, new ways of doing deals and new capital that's out there. There's more competition that an LP can put their money into. So it's not just the big three or four anymore. There's a lot of pressure on firms to evolve. You can't do deals exactly the same way that you used to. Many of us are public as well, and that brings a whole new dimension."

For those who are willing to go for the ride, change can be thrilling. "It's kind of invigorating, like wow, this is almost like it's a new job in a way," says Ms. Sabet. "There's new energy that's been infused, and so that's exciting, for the right person. Not everybody likes change."

Jason Hanold, CEO and managing partner of **Hanold Associates**, which specializes in HR officer and board

Q&A

Predictions for 2019

This has been another record year for the private equity sector. Deals have closed, fund raising has taken place, and recruiting for talent across the sector has been as hot as it's ever been.

Here's what to expect for the rest of 2019 and beyond, according to Kevin Mahoney, partner, head of investment banking & private credit at search firm Bay Street Advisors.

What major strategic trends do you see in PE?

We expect 2019 to be another record year for private equity – closed deals, fundraising and recruiting – based on current trends in the market and our own clients' ongoing activities. In addition to PE firms broadening their offerings into private credit and other relevant asset classes, consolidation in the PE market is on the rise. We're currently working with large, diversified asset managers looking to acquire established private equity firms in order to spur growth and improve diversification. In turn, senior partners at the PE firms are considering a merger or sale as an alternative to an IPO in a challenging public equity market or to selling a minority stake.

Do you expect the robust fundraising market to continue?

Like our clients, we remain cautiously optimistic on fundraising through 2019. Despite record fundraising over the last two years and more than $1 trillion in dry powder, our clients continue to increase their fundraising activities across PE, from mega-buyout funds to emerging managers focused on new strategies and innovative structures. Many firms will continue building fundraising teams in-house to handle accelerated fundraising cycles, new product launches as well as increasingly complex ongoing investor relations.

What are PE firms doing to improve value creation?

We see PE firms building depth in their own operations and infrastructure, as well as creating "resource teams" to improve value creation across their portfolio companies. Many firms are recruiting high quality C-suite non-investment professionals (COO, CFO, CTO, General Counsel). We have also been working hand-in-hand with more established PE firms to recruit in-house capital markets professionals who can optimize deal execution and capital structures.

searches, says that finding talent for PE firms was historically predominantly about stripping out costs and removing inefficiencies to prepare companies for a more successful IPO or selling the company. "But PE firms have collectively come around," says Mr. Hanold. "They're much more sophisticated than they were even 10 years ago, where now they appreciate the value of a healthy culture. They appreciate the notion that if they have been through an acquisition spree and a company's value has increased, that they have actually integrated the very companies that they've acquired, from a people, culture, processes, and methods perspective. If those acquisition targets have been integrated, they've realized, the company is actually more valuable."

What that's done is if you're serving a PE client today, "It's actually opened the aperture for talent," says Mr. Hanold. "They're no longer looking for someone who had a foundation in only finance who migrated to HR to now rip out costs. They're looking for a broader set of true leadership and great leaders who know how to grow an organizational culture and how HR leaders are going to have perspectives on the business beyond the people practices. And they're investing more in leadership. For those of us recruiting these folks we not only have more options from a quantitative perspective but qualitatively we're doing much better as well. These portfolio companies are now growing with better, stronger leaders, not just operational efficiency experts in every functional role."

Short and simple, to make money, PE firms must put their investors' money to work. Gone are the days of buying a company that was broken, cutting costs, refinancing it, then selling it at a tidy profit, says George Davis. "Now they're buying things at a higher premium than ever before and the only way you can make money is to outperform the industry averages," he says. "And to get the returns that their investors want, you're going to have to way out-perform the market. So that means you have to get really super talented people in the door. The demands and the stakes are higher than ever, and if you don't get it

right you aren't going to make money. You're going to get crushed."

Driving Long Term Equity Value

What's more, many firms are allowing for longer holding periods. Where once it was expected that a PE firm would exit a deal after three or four years, hold periods are now frequently being extended to five years, and beyond, according to **Bain & Company's** "Global Private Equity Report 2018." While they still happen, of course, "quick flips" have fallen off considerably. And some firms are even looking to exit much further down the road. "Several large PE firms, including CVC, Carlyle and Blackstone, have been launching buyout funds with longer lives," says Bain & Company. "Blackstone raised $5 billion for a fund with expected holding periods roughly double those of the traditional buyout fund. Two first-time funds, Core Equity and Cove Hill, also raised more than $1 billion each in short order, with anticipated holding periods of up to 15 years."

Mr. Ferguson, of Perella Weinberg Partners, tells of one business that his firm has owned for several years, which has outperformed its investment plan and created significant value over the last three years. "But we also realized that there was a huge opportunity," says Mr. Ferguson. "And in our business the most difficult thing is finding good businesses with good management teams. And so what we said as a board was 'OK, we can make an easy three or four times our money here. We've owned it for three years, that would be a great return. But we think the opportunity to lean in and invest more in this business over the next year or so with an exit at year five or thereabouts will create meaningfully more equity value.' And that's the kind of conversations we have at the board level. It's not about did you make your number last month or last quarter; it's about what are we doing to drive long-

CASE STUDY

Investment Thesis: Capitalize on Growth

Bain Capital Private Equity acquired discount retailer Burlington Coat Factory, now known as Burlington Stores, from its family owners in 2006. Its investment thesis was to capitalize on stable growth in the discount channel and to build on the firm's deep retail expertise to expand the store footprint and realize operating improvements.

In the early years of the investment, Burlington's same-store sales growth lagged due to a challenging macroeconomic environment and inconsistent execution of the company's everyday low price (EDLP) off-price strategy.

To manage through the recession and bolster the company's execution capabilities, Bain Capital made significant investments to grow the management team. This included hiring a CFO, an EVP of Stores, a Chief Merchant, a Chief Marketing Officer, an EVP of Planning and Allocation, and EVP of Supply Chain, and an EVP of HR, as well as ultimately recruiting an experienced CEO from a leading retailer to drive improvements across the business. Bain Capital worked closely with this new management team to transform its customer experience.

During Bain Capital Private Equity's ownership, Burlington opened 174 new stores – a 47 percent increase in store count. The company realized a successful IPO in 2013 (NYSE: BURL).

At exit in 2015, Burlington was a $5.1 billion retailer operating 570 stores nationwide. The company's growth reinforced its thesis that discount retailers such as Burlington could not only weather a recession, but could thrive as consumers became more value-focused in challenging economic times.

Source: Bain Capital Private Equity

term equity value, and that's the conversations we're going to have with our companies every time that we're with them."

All this, understandably, is intricately tied to talent. And indeed, many senior executives are interested in building, and serving, for the longer haul. "You've got to be prepared for an environment where it's not just about leveraging companies through a down

and up cycle and selling them," says Mr. Giarman, of DHR International. "You really have to put the management team and infrastructure in place to get true investor threshold return. That may not happen in three or four or five years. That may take seven years. It might take 10 years. There are funds that have been started recently very much with a focus around, 'We know that these will take longer to produce the kind of return we're looking for.' There are funds that might help capitalize family-owned businesses, knowing that they may not want to sell for many years. And so I think the world is recognizing that it's about operational value and having the right people systems, process and strategies in place when you sell the company, and the results to prove it."

Indeed, a report last year by McKinsey & Company emphasizes the need to dig deeper into an organization in order to mine the greatest value. "Identifying and quantifying the value of the most important roles in an organization is a central step in matching talent to value," says the report. "These critical roles generally fall into two categories: value creators and enablers. Value creators directly generate revenue, lower operating costs, and increase capital efficiency. Value enablers, such as leaders of support functions like cybersecurity or risk management, perform indispensable work that enables the creators. These roles are often in counterintuitive places within the organization. Typically, companies that consciously set out to pinpoint them find about 60 percent are two layers below the CEO, and 30 percent are three layers or more below the CEO."

The ability to achieve true role clarity is closely tied to overall organizational performance and health, according to McKinsey research. "In the pursuit of such clarity, it is critical to think first about roles rather than people," says the study. "The initial goal

is assessment of where the greatest potential value is and what skills will be necessary to realize that value—not identification of the top performers. This approach allows leaders to think more strategically about matching talent and value rather than merely focusing on an individual's capabilities."

THE LIST

7 Powerhouse Women in Private Equity

For private equity firms and their talent solutions partners, allocating talent is as important as allocating capital. Talent is the oil that runs the machine – and it is through the lens of human capital where transformation takes place. No one knows this better than these 7 Powerhouse Women in PE.

KENNA BAUDIN

Based in New York, Kenna Baudin leads Egon Zehnder's private equity practice in the U.S. She focuses on senior-level executives at private equity funds (partners/managing directors, principals, heads of IR/fundraising, etc.) and in PE-backed portfolio companies. Kenna also has a particular specialization in chief financial officers and is active in the firm's diversity and inclusion council and in its consumer and media, entertainment & sports practices.

MERCEDES CHATFIELD-TAYLOR

Mercedes Chatfield-Taylor is managing partner of Caldwell's private equity and venture capital practice areas and a member of the firm's technology, consumer, digital and media teams. She focuses on executive-level search for high-growth technology companies, with deep expertise in B2B SaaS, social, eCommerce, gaming and other transformative technologies. Mercedes has completed over 50 CEO searches as well as other CXO level assignments for her clients. She has deep expertise in helping to diversify VC & PE-backed company boards and leadership teams.

HEATHER HAMMOND

Heather Hammond serves as the area manager for the New York and Stamford offices at Russell Reynolds Associates. She co-leads the global banking and markets practice and conducts a broad range of senior-level searches across the financial services industry. She is also a member of the firm's private equity practice where she has completed searches for funds and their portfolio companies, including investment leaders, senior fundraising professionals, capital markets professionals, operating partners and advisors. Heather has 14 years of executive search, assessment and advisory experience.

JILL HILL, PH.D.

As lead of the Americas private equity practice at YSC Consulting, Dr. Jill Hill advises leading global private equity firms on their toughest leadership and talent challenges. Acting as a strategic partner, she specializes in providing management due diligence, senior executive assessment, coaching, board effectiveness, and high-performance team development to investors, boards, CEOs, and portfolio company management teams.

Balancing scientific rigor and relationship capital, Jill works at pace to actualize the talent lever in maximizing value creation and mitigating leadership failure. A licensed psychologist, she brings substantial psychological training and expertise to her role underscored by more than 20 years in assessment practice, research, and development across industries and sectors.

SUSAN LEVINE

Susan Levine is a managing director and head of the North America private equity HR & talent development practice at Bain Capital.

Internally, Susan is responsible for the firm's North America private equity team's investment and portfolio operations professionals. Her primary responsibilities include leadership and professional development for deal and portfolio executives, recruiting, mentorship programs, resource allocation, and culture and connectivity programs for NA private equity business. Externally, she is responsible for talent initiatives at the firm's portfolio companies, including hiring C-level executives, as well as leading assessment activity at the individual, team and organizational level within those portfolio companies.

ANNMARIE NEAL

Annmarie Neal is chief talent officer at Hellman & Friedman. Her primary responsibility is to help H&F drive value by improving the organizational and leadership effectiveness of the firm's portfolio companies. Annmarie has over 20 years of experience working with global organizations on executive leadership, talent management, and organizational design. Prior to H&F, she ran her own consulting firm and held the chief talent officer roles at both Cisco Systems and First Data Corporation. Additionally, she was a senior consultant with RHR International.

LORI R. SABET

Lori Sabet is managing director and chief human resources officer for Carlyle Group based in Washington, D.C. In this position, she is responsible for developing and executing the firm's global human resources strategy. She joined the firm in 2000 and serves as a member of the firm's management committee.

Under her leadership, Carlyle's global human resources team is responsible for providing strategic and innovative guidance in the areas of leadership and succession planning, incentives and rewards, learning and performance, diversity and inclusion, recruitment strategies, employee engagement, and organizational development. She is actively involved in several human resources organization roundtables and is a frequent speaker and panelist on global human resource-related topics.

But who exactly are those leaders who can drive such returns for PE portfolio companies? What are their characteristics? What makes them a cut above the rest?

The Right Talent DNA

"I think that the people who will thrive in a private equity context need to have a certain type of DNA," says Kenna Baudin, who leads **Egon Zehnder's** private equity practice in the U.S. "Not everyone is suited to work in a private equity backed portfolio company. The pace tends to be faster. The reporting requirements can be different. So not everyone is cut out for that."

It depends on the situation, but generally Ms. Baudin looks for certain traits in value-creation minded leaders: "Self starters. Self motivated. Focused on what's right for the business, not just what's right for themselves individually. People who have been successful doing it before. And people who have also had experiences where things haven't necessarily gone exactly according to plan and how they've managed through that. We're looking for people who are resilient."

"It's looking for people who think like owners as opposed to just being an employee. So it's somebody who is looking to see what they can do, what they can bring to the table. Not just what can I get out of this job."

Ben Holzemer, partner and global head of human capital for **TPG**, emphasizes that private equity is a vast industry that's tremendously diverse. "The person to be the CEO of a fast-growing $100 million tech company that you just made a growth equity investment in is going to be a very different profile than the right leader for, say, a carve-out of a multi-billion dollar EBITDA-producing business that needs to go through a fundamental strategic transformation," he says. "Those are vastly different searches and talent challenges."

MAXIMIZING VALUE

The Value of a Great CFO

EgonZehnder

As private equity firms look to maximize value from their investments, it is critical to ensure that portfolio company management teams have the right capabilities to execute against their investment theses. Though in many cases the underlying premise will lie in backing an existing management team, it is increasingly common for private equity firms to bring in a new CFO early in the lifespan of an investment.

Source: Egon Zehnder

At the same time, some common denominators can be found among leaders regardless of sector or deal type. "Financial acumen," says Mr. Holzemer. "You're going to work with a board and a sponsor that are comprised of financially savvy people, so having an interest in that and an ability to articulate and work with financial matters is really important. There's a pace consideration, when you're striving to create value. So measure of decisiveness, moving quickly, taking calculated risks, and getting things done are all important. There's a real premium on that kind of underlying DNA of an executive, whether you're looking for a CEO in a large buyout, growth company or some other play."

The ability to build teams is likewise a critical talent. It all starts with a thorough evaluation of the company's existing strategic goals as well as the PE firm's investment thesis, says YSC Consulting. "From here,

EXPERIENCE

Recruiting for PE & VC Backed Companies

The Tolan Group
EXECUTIVE SEARCH

The private equity and venture capital investor practice group at The Tolan Group has a breadth of experience working from early stage startups to established companies to publicly traded organizations.

The firm works with venture capital and private equity firms hand-in-hand to build stronger organizational infrastructure. It specializes in executive search, board consulting, and leadership development for PE and venture capital backed companies.

the key strengths and leadership skills required to drive these strategic goals are identified, and a structured approach to enhancing these skills at the top of the organization can be launched," says the consulting firm.

"In our view, activating the team starts with gaining in-depth insight into each of the team members as individuals and as leaders," says Isabella Roger, Ph.D., senior consultant, private equity, at **YSC Consulting**. "To attain this goal, we incorporate advanced psychometrics and behavioral interviewing to gain a deep understanding of each leader in a short period of time. Layering on team effectiveness analyses, we develop a clear view of the team's dynamics and opportunity areas. These insights provide the foundation that allows us to recommend targeted, high impact individual and team development actions proven to drive successful performance."

So it is that firms across the PE spectrum pay great heed to making teams come together. "TPG is highly focused on working with its portfolio company partners to build healthy businesses, and developing strong leadership teams is an essential part of that process," says Mr. Holzemer. "As a leader, one's ability to manage change, gel and assemble a great team, and motivate them on a mission to achieve a particular value creation plan are all some of the common denominators."

Essential Elements: Culture & Value

Also, culture and values are critical. "We've all heard the cliché that culture eats strategy for lunch. Well, it's true. Things like culture, diversity and inclusion, and team effectiveness are critical for success. They are a priority at TPG. A company might have a strong leader, but if the team doesn't work well together or the culture is broken it's not going to produce or sustain results. Culture and values are essential," he notes.

Abe Doctor, a partner and head of the North American market with **TritonExec**, says that though many executives express interest in top roles with portfolio companies the risk averse among them usually drop out in favor of a job with more predictable results. Mr. Doctor points to a couple of key personality traits for PE portfolio roles.

"First, we look for somebody with extremely effective natural leadership abilities, meaning they're intuitive, they are savvy about interpersonal interactions and they have the ability to work with any type of people, because coming from a Fortune 50 or a Fortune 100 many executives go through a bit of shock when they go into a private equity-backed business that is smaller in scale and maturity."

Secondly, portfolio company executive opportunities tend to attract "somebody who's not quite a thrill seeker but who believes in their ability to add value to an organization and who is motivated by impact of growth and building something," says Mr. Doctor. "I think those types of people can get bored with something after a few years. So by design a three year or five year hold is kind of the perfect attention span for someone to build a business up and create value in it and help achieve a financial outcome for themselves and the private equity investor."

Oftentimes, those most drawn to such roles are "professionals who have not yet achieved enough

Q&A

Booming PE Sector Feeds U.S. Expansion at One Search Firm

TritonExec provides strategic talent introductions to private equity firms and C-suite executive search services for their portfolio business.

Abe Doctor is a partner in the firm and directs its North American operations.

What led to the firm's expansion into the U.S.?

Our expansion into North America was always the natural first step and a necessary one as part of our drive to scale our business globally – America has always been our main market of interest. Remarkably, however, we were able to expand here in our early years without having a physical presence. Our clients that we began working with in Europe were global businesses and were investing in North America. That's where they saw their own growth happening. Eventually, we reached a point where we had consecutive years of multimillion dollar revenues in the U.S., and our physical presence became absolutely necessary – New York, Atlanta and San Francisco are where many of our clients are based, so those locations were important to us.

Is further expansion coming?

Absolutely. Having established our U.S. base in Atlanta, and our second office most recently in New York City, our strategy includes expansion to San Francisco (where many of our global clients are headquartered). In addition to expanding to new regions in the U.S., our growth strategy includes tripling the size of each office (including London) over the next 24 months.

Explain the leadership needs of portfolio companies within the PE space. What functions and roles are hot?

In short: Supply chains, sales and industrial. Supply-chain technology is particularly important right now for private equity firms that own portfolios of similar and disparate companies; however, they're looking to draw synergies between these businesses. So, for example, we're seeing this synergy played out with private equity firms which may own distribution or manufacturing, who are then going on to buy retail businesses, and are connecting these through supply-chain technology. The operational levers which have been private equity's bread and butter in improving businesses are not sufficient to keep up with the pace of the market. We're finding firms have to find ways through supply chains to drive value.

Give us an overview of the current state of the private equity sector?

Right now there is so much dry powder (money to invest) in the PE space due to the fact that high net worth individuals, endowments and pension funds are putting their money less into traditional investment vehicles, like institutional investment firms, and more into PE firms as LPs (limited partners or investors in their funds).

With additional capital comes a lot of competition for attractive companies on the market. When that occurs, PE firms are overbidding and the multiples are very "frothy," or in layman's terms, over paying for companies compared to historic, expected multiples. Now that sellers are getting many attractive bids for their company, it has become less about who will pay the most money for the asset, but more about which firm will get us the best outcome and the best valuation after the hold period.

financial freedom to not work but who have achieved a level of income where they are willing to sacrifice some short term cash or long term upside," says Mr. Doctor. "Not every executive is in a position to do that with families and so on and so forth."

More Than a Star Athlete

Jill Hill, Ph.D., head of private equity for the Americas at YSC Consulting, says that many firms are broadening their approach to value creation in their portfolio. Now firms are looking beyond pure financial engineering or operational excellence plays and have come to view investment in talent and human capital as "mission critical" for value creation.

"While that may sound simple enough it's often much harder to do in practice. One stand-out quality we see in executive leaders who are successful in portfolio companies is that they are very comfortable with change," says Dr. Hill. "First they must be able to align their teams around new strategic priorities and communicate how these will create value during the

hold period. Next, they need to energize and engage the entire organization to successfully activate and lead through change and transformation. No CEO can do this alone, so the task is to find talented leaders who can be more than a 'star athlete.' Successful leadership in this context requires exceptional collaboration skills, the ability to run effective, high-performing top teams, respect for the ideas and skillsets of others, and openness to partnering with peers, board members, investors, sponsors and others to make sure that everything operates as it should," she notes.

OPTIMIZING TALENT

Bringing Rigorous Science to Leadership

YSC CONSULTING

YSC Consulting works at the C-suite level with 40 percent of the top 20 Private Equity firms. The firm's global private equity practice brings rigorous science to leadership, transforming it into a variable to measure, anticipate and optimize talent.

Historically, recruiters as well as PE firms leaned heavily, perhaps too heavily, on their own networks and contacts. Dr. Hill calls this the 'I know a guy' approach. "We still run into that in the market," she says. "Unsurprisingly, the contact is not always the person who is best equipped to be successful in a particular deal. That's where leadership experts come in. We first determine the requirements for successful performance and then evaluate whether a leader will be able to execute against the mission-critical responsibilities and accountabilities for the role. Additionally, we assess a leader's ability to activate as a strong member of a great team. Successful performance requires an aligned top team rather than a collection of individuals working in concert to accelerate execution against the value creation plan. Overall, it goes far beyond a relationship that this person may have with a particular individual in a private equity firm or relationship with someone on an existing management team. Now, savvy global PE firms say to us, 'Let's find the absolute best talent in the market who will be the best fit for this context.'"

Courtney Hagen, chief talent officer for **Littlejohn & Company**, says that the executives that her firm seeks can differ depending on everything from the industry that the portfolio company is in, to the size of the business, to the PE firm's strategy for the company. "When we're buying a troubled company and we're looking for someone to lead it, that it's a different kind of experience that we need versus somebody where we're investing in what we call our 'good to great strategies,' where we're looking at a company that has a very strong position in its market, where through the capital investments we make as well as the board leadership investments we make in that company, that we see the potential for enormous growth. Those are two different kinds of leaders. As a turnaround leader versus a high growth leader we would not hire the same person to do both of those kinds of different roles. And certainly there are times that we need people who have a very specific experience with an industry or with a set of customers, but the qualities that we're looking for in terms of drive and motivation and collaboration are pretty common across our companies."

Mercedes Chatfield-Taylor, managing partner with **Caldwell's** private equity practice, says that the vast amounts of capital flowing into everything from series A through to private equity-funded companies make for no shortage of need for talent. "And private equity funded companies are looking for folks who are really excellent operators," she says. "So you need someone who can operate not just in rapid growth environments, but in a combination of growth and

UP CLOSE

Wanted: Leaders Who Can Navigate Change

Mercedes Chatfield-Taylor is managing partner of the PE & VC practice areas for Caldwell. She focuses on the executive level talent needs of high-growth technology companies. She has completed over 50 CEO search as well as other top CXO level assignments for her clients. Her strong suit is helping to diversify PE & VC-backed company boards and leadership teams.

Following is an excerpt from a recent discussion on her role, what's hot in PE, and key trends she is noticing in the market.

What got you interested in private equity? How has that field changed throughout your career in search?

I started my career in Bermuda, working in international banking and reinsurance. I met several large PE and VC firm partners early in my career and have always had an interest in the space.

What are some hot roles you're seeing PE firms looking to fill right now?

PE-experienced, at scale, highly operational chief financial officers are always in demand. Highly skilled product and technology leaders (CPOS) too.

What kind of leaders are PE firms seeking at the moment?

PE firms continue to look for people who have successfully navigated companies through change. That includes taking companies private successfully, then through another liquidity event. Leaders with strategic acquisition AND integration experience are also in demand. Diversity, of course, is in big demand.

real operational rigor. That thins the talent pool to begin with. And then there's the added complication of PE firms looking for specific domain plus specific types of functional experience. And then on top of that there is the reality that the equity pools for private equity hires can sometimes look a little less flashy and illustrious from the outside looking in. So as an example, in a VC-backed company often the incoming CEO will be offered five to eight percent of

that company. In a private equity funded company, that CEO might be offered half that much, but the reality is that there's a more direct path to liquidity than there is generally in a series A or B funded company. But the optics are tough. So those are just some of the challenges in addition to the fact that it's been a candidate's market since about 2010, and we're in 2019."

A Crisp Recruiting Methodology

In a candidate's market, Ms. Chatfield-Taylor and her team will try to make the recruitment process as prospect-friendly and streamlined as possible. "We adjust for the things we can control for, which is really coming up with a tight process to direct the search, so that when we bring those highly qualified, highly sought after candidates to the table that the team is in a position to execute very crisply in both assessing that talent and continuing to sell that talent and onboard that talent," she says. "So the thing that I tend to advise my clients around in advance are coming up with a really tight scorecard, the framework by which we're evaluating the candidates, and utilizing that scorecard and then making sure that there are enough touchpoints with the company but not too many touchpoints with the company. The flip side of that equation is that if way too many people make it to interview, you ask the same questions, you frustrate the candidate, and you lose them because other people are moving very quickly. So I would say in addition to having a compelling opportunity you really have to have a crisp methodology around recruiting. And if you don't, it really doesn't matter how good the opportunity is, you're going to lose some great candidates."

"The other parts we can't control," says Ms. Chatfield-Taylor. "We can't control how frothy the market is, we can't control that other companies are making out-of-market offers. We can't control that the great

candidates are getting multiple calls even when they're not at all looking. We can't control for those things. So we control for the things we can."

One feature in portfolio company candidates that tends to be attractive to PE firms is having had similar experience, particularly for a PE-backed business. "One thing I've noticed is that if an operating executive has previously made money for a private equity sponsor they are almost by definition more attractive to another private equity investor," says Tom Nieman, co-founder and partner of **Signal Partners**, a Santa Monica, CA based search firm.

Time and again, recruiters say they look for those with an entrepreneurial bent, but not in a manner of starting a business from scratch, like a venture capital-backed company leader might do. Instead, PE firms want talent with an entrepreneurial spirit, who can roll up their sleeves and make do without a big support system or all the extras. "It depends on the role," says Kenna Baudin, of Egon Zehnder. "But you want people who have worked in entrepreneurial environments, people who have previously been in a private equity context before. At times you look for people who have had entrepreneurial experiences within a large corporate, people who have had a combination of best-in-class training, often in larger organizations and then maybe moved into more entrepreneurial organizations."

PE firms appreciate those with such a background, she says, because they are used to working in more of a leaner environment. "If you're someone who is used to being in a large organization where you have 50 assistants and a zillion people to do the work, that doesn't often work in a private equity context where they tend to be nimbler organizations, with fewer layers of management, fewer layers of people to do the work," says Ms. Baudin. "I used to say, 'You need somebody who is comfortable with a fax machine

Q&A

Compensation: A Cautionary Tail

Tom Nieman is a co-founder of Signal Partners – a search firm purpose-build to help private companies and their sponsors on both executive and mission critical top level searches.

Tom has led searches for companies such as: Houzz (VP Finance, VP Global Sales; VP Industry Solutions; VP Partnerships), Wealthfront (CFO; Chief Data Science Officer), Chegg (CEO), LifeLock (CMO), Rival (Head of People; Head of Finance), Telesign (CEO), Tastemade (CFO), RuffaloNoelLevitz (CEO), Acxiom (Board Members), and Invoice Cloud (President), among others.

You spend a lot of time recruiting executives. How important is compensation up front in the recruiting process?

Not very. In fact, I rarely discuss compensation. At least not until the very end. In terms of what I'm trying to discover or learn, it's just not very high on the list.

Why is that?

Look, the most important part of what we do is, first and foremost, to help our clients find awesome people. And to make that happen we need to figure out what it is they're looking for, what they're looking for in a trade, and to determine whether or not such a trade is feasible. And, frankly, if the base and bonus are factored heavily and front-loaded in that conversation, then we're focused on the wrong things. Don't get me wrong, compensation is ultimately a very important part of the equation. But I find it only starts to matter once we're well down the path.

What happens when an offer is not in line with "market"?

I think it's misguided to rely on "average comp" studies as a negotiating tactic. One must consider the package holistically - both cash and equity - to make an informed decision. Doing so is super-subjective. Nobody knows the actual future value, so it often comes down to your own internal calculus. I know a guy who declined an offer to join Google as employee No. 17, to join a bigger company that could pay him better. I know that's an extreme example, but it's a cautionary tale for anybody using "average comp" numbers as anything more than a signpost.

SPOTLIGHT

Supporting a Diverse & Inclusive Workforce

Paige Ross is the global head of human resources at Blackstone. In this role, she oversees human resource management globally for the firm. Prior to joining Blackstone, she served as the managing director of talent management at Centerbridge Partners, with a focus on leading talent management across the firm's portfolio companies.

Ms. Ross has put an emphasis on diversity and inclusion at Blackstone, saying that "it's not simply an important goal, it's also good for business." Financial services has been an industry that some say has been a bit behind when it comes to diversity and inclusion as it is dominated by white males. This is something she believes needs to be changed. Ms. Ross said that diverse teams have more to offer: "Having a diverse team with varied experiences and backgrounds brings a broader set of insights, and so is key to success," she explained.

and a phone.' Now you need somebody who can work well just with their iPhone."

Bob Llamas, operating partner, portfolio operations, for **Blackstone**, says he wants individuals for the firm's portfolio companies who have broad knowledge and experience but who can thrive in a smaller context. "My own professional view is that we like people with pretty broad playbooks, or a specific playbook related to somewhere we're headed with that company," he says. "So if we have a fast growth company with multi-locations, we'd like somebody who had been successful in that environment. We are looking for what we call a fit-for-purpose resource allocation. We're looking for people who maybe have been where we're headed or have that capability."

"They also have to be pretty entrepreneurial," says Mr. Llamas. 'Our companies aren't huge. A lot of them are in the midsized range. So the people we hire have to have an experience or a playbook that is pretty broad, but they have to be able to go small and they have to be able to go entrepreneurial. An ideal candidate is someone who is well trained, has been to places where that particular investment or company is going to go, but has the ability to relate to it at the level it currently is, do a little bit of building but then also grow with the investment. So it's that combination of experience and a playbook and the ability to be entrepreneurial, to be able to live with this kind of ownership mentality as opposed to big, big company mentality."

Having worked in a PE environment can be a plus, says Mr. Llamas, but it is hardly everything. "We want someone who is very fit for the purpose: They've worked in that industry or that vertical; they've done some of the things we want to do, whether it's consolidate or grow fast or whatever it is in our case," he says. "The experience of having worked in a portfolio company could be a plus, particularly as they relate to our boards and our investors, but it's not necessary."

The Right Mix

"If they don't have it you kind of want to test against bigness or bureaucracy or something that might make them less effective in a private equity or entrepreneurial setting. So you don't have to have it but you can't bring a whole lot of counter-experiences to it. If I can get the experience it would be great. If I can't get it I sure don't want to get someone who is not going to be entrepreneurial and think like an owner and be a builder."

Nor is someone from a large corporate necessarily rejected out of hand, especially if the prospect has had good training and a strong set of experiences. "The major one being that you know what good is," says Mr. Llamas. "You know what a good CFO looks like; you know what a good FP&A looks like, you know what good systems look like. Then the

question is, 'Can they do without a lot of the settings, a lot of the resources? Can they substitute and build some of their own if they have to? Can they be entrepreneurial?' To me that would be a pretty good mix: if they had the good training and the good background but they wanted to and they could go entrepreneurial. That would be very good."

In many ways, however, these are all just a starting point in choosing the right individual for a portfolio company. The consequences for making a wrong choice in a key leadership role is simply too great not to dig deeper, especially when it comes to a PE firm with a limited hold time on its investment. Understanding what makes a candidate tick and how he or she fits – or doesn't fit – into the company's culture – and the PE firm's culture – and its particular needs is crucial.

According to a recent survey by **AlixPartners**, 39 percent of private equity respondents said that replacing a portfolio company CEO in the first year after closing a deal and one year preceding the deal exit causes the most disruption at the portfolio company. And yet that same group said that 58 percent of CEO replacements are made in that time frame. The survey "shows that private equity needs to take further action to avoid costly C-suite turnover at their portcos," says Ted Bililies, global leader of the organization & transformative leadership practice at AlixPartners and a managing director at the firm. "They need to undertake more robust CEO assessment during due diligence, move succession planning to the top of their priority list, and set clear expectations upfront with CEOs regarding goals, performance metrics and communications."

Heather Hammond, who co-leads the global banking and markets practice at **Russell Reynolds Associates**, says that the bar for portfolio company leadership is exceptionally high. "We build our assessments in several ways," says Ms. Hammond.

REVOLUTIONARY LEADERS WANTED

Attracting the Right Talent

Increasingly, America's most dynamic companies all have two things in common. One is that each has an ahead-of-their-time leader who has the drive and the smarts to revolutionize the way the world works.

The second? They're funded through private equity. In today's global marketplace, private equity is the engine propelling forward new ideas, new visions and new ways of thinking and looking at the world.

The private equity practice at Diversified Search leverages the full capability of industry and functional expertise across every major sector to effectively serve private equity firms and their suite of portfolio companies. Leadership, in their mind, is vital to the success of any investment at any stage of the investment life cycle, whether that's IPOs and pre- and post-merger integrations, or executive introductions and talent studies that include management benchmarking and market scans.

The challenge facing PE firms today, according to Diversified Search, is to attract the right talent to impact the investment strategies and drive operations growth within their respective portfolios.

"One is by virtue of our own expertise and the way we compare their experience to that of their peers in the market. We look for patterns, such as continued sustained success in roles that they have had. We look for their success being tested in different environments. So, for example, if you take someone who has come out of a big conglomerate, have they had experiences along the way of perhaps testing that in a more entrepreneurial venture either after that experience or before that experience that you can look at their experience in different environments? Also, you obviously speak to references. And you do psychometric assessments as well to understand how they are wired and what their DNA is all about."

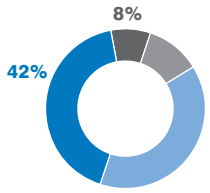
Another consideration, especially with the spectre of darker economic days on the horizon, is the question

of just how well a leader handles tough times. "Obviously we're at the end of an economic cycle," says Ms. Hammond. "Things can get more turbulent sooner rather than later depending on what's going in the macroeconomic sense or the political sense or what have you, and how does complexity and uncertainty test the quality of a portfolio company's leadership? Because that's when the great leaders emerge. They have to adapt and demonstrate decisiveness and judgement on what they're going to do."

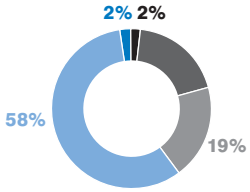
INVESTMENT LIFE CYCLE

If PE Investors are Going to Replace a CEO, They Should Do it Early in the Investment Life Cycle

At which point in time is CEO replacement most disruptive?



Timeframe for CEO replacement



39% of private equity respondents indicated that it is most disruptive to replace a portco CEO after one year of investment and before one year of exit, yet 58% reported that this is the most frequently occuring time frame.

■ Immediately (0 to less than 6 months) ■ 6 to less than 12 months
■ After 1 year of investment and before 1 year of exit ■ Within 1 year of exit ■ Other

Source: Alix Partners

With a decade-long bull market destined to end at some point and many prognosticators expecting an economic crisis within five years, Russell Reynolds and others are paying particular attention to how portfolio company prospects behave when confronted with stormy seas. "You want leaders who are decisive and so on, but you also want people who are humble, who can be even keeled during turbulent times and who can develop constructive relationships, because you need to depend on those constructive relationships when things get tough," says Ms. Hammond.

One of the most difficult factors to assess when a PE firm is doing a deal, in fact, is the leadership derailers of the target company, which tells you how those executives will operate under stress. "Just by the nature of the beast, the companies that private equities invest in are going to have moments where they're under stress, either because they're trying to do a lot or there are a lot of opportunities for business improvements," says Alice Mann, a human capital operating partner with **Blue Wolf Capital**. "And so it's

CASE STUDY

Fast Track to a Successful Hire

B|R

A leading strategy consulting firm struggled to fill a role for a high-performing senior leader for its retail and commercial banking practice. The original search was drawn out for two years, which drained valuable time and resources, and they still had not found a candidate.

For Beecher Reagan – a search firm focused on the senior professional services and consulting talent market - the first order of business was to assess the engagement and uncover the issues hindering the search. Their analysis found that the narrow search scope was preventing its client from considering potentially viable candidates.

Knowing the issues and how to address them, the recruiting firm broadened its search scope to include a full range of sources, such as rising stars at smaller and less well-known firms, those disenfranchised by market changes, and those who had moved from consulting to industry. The approach quadrupled its client's previous list of potential candidates.

The successful candidate—rejected as a poor fit in the initial two-year search—generated significant client revenue within his first year at the firm.

important to understand how leaders operate under stress, and for them to have the tools going into the deal, whether it's self-awareness, mentoring and coaching, or, most importantly, having a great team in place who can do everything in their area of expertise as well or better than the CEO. Being able to rely on a great team and building a great team are what get leaders through those challenging moments. That's very hard to predict ahead of time. And I think that is what executive talent assessment in PE is about — trying to understand ahead of time how a leadership team will operate under the stress of all kinds of different circumstances that may arise, and which teams will even thrive under those circumstances, and those are the teams that lean into uncertainty and risk, and welcome them as an opportunity for innovation, problem solving, and teamwork. Those are the performance driven teams that PE firms want to invest in. They'll take any challenge and turn it into an opportunity to solve a problem."

POINT OF VIEW

How Do Successful Portfolio Company CEOs Lead?

Russell Reynolds ASSOCIATES | 50 YEARS

- Successful portfolio CEOs tend to be more "humble," approaching others in an even manner, empowering their peers and assuming others are reliable.
- While they are fierce competitors, they are quietly self-confident and do not trumpet their achievements.
- They excel in rapidly changing business situations, speeding up their work style as needed and juggling competing priorities.

Source: Russell Reynolds Associates

Miranda Hanes, head of business development at **Hogan Assessment Systems**, says that assessing the leadership of a portfolio company should be a critical part of the due diligence process or at the very least shortly after a PE firm takes control of a new business. Through personality testing, PE firms can start to focus on moving forward. "Understanding what the culture and core values of the leadership team is vital to the Private Equity partner, so they can ensure the current leadership team can adjust to the direction the PE firm is going – and do so quickly," says Ms. Hanes. "Additionally personality assessments can provide insight into how the leadership team responds to problems, can recover from setbacks, and acts with a sense of urgency. Hogan can also help PE firms understand how likely a CEO will be at building and maintain an effective team."

The Hogan Development Survey, which "describes the dark side of personality, qualities that can emerge in times of increased strain," according to the firm's website, can be an important part of that process. Indeed, identifying derailment characteristics ahead of time can prevent problems later on. "We think about derailers as behaviors that emerge during stress, during pressure," says Ms. Hanes. "We also see these behaviors emerge when individuals are put in really ambiguous situations; like a PE acquisition."

"I think the reason behind the PE firm acquisition is critical to look at as well," says Ms. Hanes. "Is this a turnaround situation or is this an injection of money because the organization has been successful. Those are very different situations. Each situation is going to feel very different to the team that's in place in the organization, and those derailers are going to be even more critical to understand. For example, how is this individual going to behave in ways that are going to get in their way or that's going to be detrimental to the organization? And if we know what those behaviors will be how can we help them through this particular time and provide them with resources they need to continue their success?"

She continues: "It's important leaders of the acquired companies are set up for success. Providing

Q&A

Talent as the Ultimate Value Generation Lever


Chris Bull


James Hickey

Since 2001, McDermott & Bull has been redefining expectations within the world of executive search. The firm's practice leaders are uniquely positioned to address the dynamic leadership demands of companies across nearly every industry.

In the following joint interview, Chris Bull and James Hickey examine talent needs across the private equity sector.

Describe your work with private equity firms.

As a firm, we enjoy serving the middle market. We like the entrepreneurial spirit that is so often a big part of these types of businesses, but without institutional sponsorship, they often will not leverage the services of a retained search firm. We also enjoy the nuance of serving both a CEO and a sponsor that often times thinks a bit differently than the operator.

Some experts say that for most private equity leaders, talent itself is now seen as the ultimate value generation lever. Do you agree?

When we think about how we bring value-add to our PE clients, it's always on the consultative side. Most private equity firms are experienced users of retained search, but we do this every day and aren't afraid to work hand in hand with our PE clients in order to conduct a robust search process. Additionally, because we work with a varied group of PE firms, there are best practices we can pass on that we may have developed by working with other firms.

Explain what led your firm to work with private equity firms?

We have been providing interim executives to companies who were owned by PE firms, which led us to be introduced to those PE firms. The more needs we were able to solve, the more portfolio companies we got introduced to. It gave us the sense that when you prove yourself in serving PE firms and their portfolio companies – you will be called often!

Where do you see the private equity sector heading in terms of talent and technology?

There has been a strong shift in the past few years to get more data on every business, and make fast decisions about the business. I think talent related to gathering data and understanding what it means will continue to have high growth opportunity and demand in the PE world.

Has the private equity sector been of high growth for McDermott & Bull? If so, how has it grown?

It has been a strong area of growth. Our ability to serve the Interim needs, and support the management teams regardless of location, but with quality people in a short period of time, has put us on the map with many PE firms. We are quick to determine the needs, and after we've worked with a firm a few times it makes our job easier – we know the expectations of our talent to solve the need.

How has McDermott & Bull been successful in assisting in adding value to its private equity clients and their portfolio companies?

With our interim services, we can help in urgent situations, and make an immediate impact. We generally will make progress in the function we are working in, and that accelerates the value the PE firm is looking for in their portfolio company. Also, when there is a void in senior management, we are able to fill that void and keep the company moving forward.

Are you seeing a greater need to fill roles within PE firms or their portfolio companies?

There is no doubt that PE firms take more interest across the executive suite now than before. They are more involved in operations, sales and marketing than I've noticed in the past. Finance and accounting, along with Internal IT needs, have always been popular areas of focus.

feedback and coaching around their results and really giving them coaching around, 'Here are the strengths that you bring to the table, let's think about leveraging these. Here are some of your derailing behaviors. What triggers these and how can you minimize these behaviors that may get you in trouble. Finally, let's discuss what is important to you and how can you articulate those values to the organization? Leveraging those values that are important to you can guide you through this experience.'"

J.P. Flaum, founder and CEO of **Green Peak Partners**, an organizational consulting firm based in Denver, agrees that not every executive takes well to personal assessments, particularly if they think their job could be on the line. "Do you know who embraces it?" he asks. "'A' players. The reason they're so good is that they get better today, tomorrow, next month, next year, and they're on a trajectory that over a year or two or five they just keep upping their game. They're people who are committed to personal growth

and one of the most important pieces is that they're committed to increasing their self awareness. It's the No. 1 highest correlated trait across the C-suite. If you couldn't know anything else about a C-suite executive, but you knew they were highly self aware, bet on that guy."

The other key ingredient one finds in successful leaders, Mr. Flaum says, is their ability to consistently upgrade their teams. And that means to be relentless in making those tough choices, not just at the beginning of a PE firm's run but throughout their time running the company. "Some CEOs think they're good at it but they're only good at one type of it, which is when they got hired by a PE sponsor and put into a company and they upgraded six of the nine people on the senior team," says Mr. Flaum. "They were relentless, they were amazing, they were great at upgrading talent. But three years in when they've grown a good bit with those same upgraded people that have bled in the trenches with them, that they're now friends with, that they know their wives and husbands, now they

Q&A

We're Looking For Player/Coaches

Tony de Nicola
Co-President
Welsh, Carson, Anderson & Stowe

Following are excerpts from a recent discussion.

How do private equity firms think about CEO hires compared with how equity companies think about them?

Public company CEOs have to sell the company's story to different constituencies, including investors. Charisma and confidence are very important. And they often have large staffs; they're delegating and have less responsibility for day-to-day operations. In the private equity model, we're looking for "player-coaches" who will lead a smaller team and collaborate very closely with owners to create value.

Has your hiring philosophy changed during you career?

Definitely – over 25 years, I've seen what's worked and what hasn't. I used to hire a resume – someone with the skills and experience that fit the specs. We usually reverted to someone who went to the right schools and grew up in the industry. Today I worry less about the right pedigree of industry. I'm more interested in who someone is as a person and a leader and how good the candidate is at identifying talent, motivating a team, and building a culture of excellence.

Is your hiring more data-driven?

Like everything in business, it's become more analytical, quantifiable, and metric-driven. We use scorecards and ratings. We have the same set of people conduct interviews, using the same set of questions. It's disciplined and rigorous. I think we're very good at it, but it's hard to get it right: Our success rate is still only about 60 percent.

Why so many failures?

Sometimes the person lacks a sense of urgency, which can be hard to judge in interviews. Or the team dynamics don't gel. This is a team game; executives won't succeed by themselves.

Source: Harvard Business Review; Green Peak Partners; Welsh, Carson, Anderson, & Stowe

have a blind eye towards those very same upgrades that are needed. So the CEOs that can do it not only upfront but also ongoing. It's the No. 1 correlated skill of CEO success in private equity, specifically in that environment, private equity. It's more important than strategic thinking. It's more important than industry knowledge. It's more important than how long they've managed a P & L, where they went to school, birth order, anything else you want to do, it's the No. 1 thing."

These days, more than ever, PE firms are looking to search firms and consultancies to do so much more than find good people. Like so many businesses, private equity is coming around to the need for talent to drive value in a myriad of ways. At Russell Reynolds Associates, for example, recruitment still matters, of course. "But a lot of what we do and we dedicate a large part of our business to is leadership and consulting and advisory work, onboarding, coaching, helping private equity firms develop their 100-day plans in concert with what good leadership and leadership development looks like," says Ms. Hammond. "So rather than having a 100-day plan that is just purely focused on cost-cutting and putting wins on the board, much of that 100-day plan is also around coaching and onboarding of the executive. We as a firm do a lot of that. Both our search consultants do it as well as our more specifically psychologically-trained industrial psychologists that work on staff with us and help us with that."

At or certainly near the top of everyone's list for identifying the right leaders is culture fit. Mr. Giarman, of DHR International, says finding individuals who work well within a given portfolio company, especially with the special challenges that PE demands, can be tough. "Let's say it's early in the investment cycle when you're bringing someone in. You have to make sure that they fit, that they can operate within the values and behaviors that are established, but you're also very often asking them to create a new way of looking at the world. So they are there to maintain in what makes sense but improve in areas that will generate the investor returns that the PE firms are looking for. You've

got to make sure that their values and behaviors line up with what exists today but also they have the capacity to exercise a change management program over time where they will instill more discipline and accountability. So part of that is having the wherewithal and patience and the EQ (emotional quotient) – not just the IQ – to do it. So EQ is very high on our list of things we look for, the ability to prioritize people, manage people well, handle things respectfully when people need to go. These are all critical in these situations when you're trying to improve operations."

A Degree of Alignment

Another important factor in culture fit is the communication style of the prospective leader. Someone who has lived and worked in Manhattan their entire career might not work well in Wichita, KS, says Mr. Giarman. "When you start those searches you make very conscious efforts not to bring people to the table who might have too much of an edge or a style that might not work well," he explains. "If the company is in northern Michigan or Detroit you look for people that might have loyalty to those areas. Maybe they went to college there. Maybe they worked in Chicago, maybe they left. So you can bring people back home to a place where they started. You look for the Midwest schools, the Notre Dames and the Northwesterns, the Ohio States, and many others, that will generate the talent that might have the cultural preference of the company you're working for at a given point in time. Our team is trained to look for those things depending on the geography of the company and where they sit across the country."

And though different private equity firms have different levels of involvement with their portfolio companies, there must be at least some degree of alignment between the two. "Generally speaking I don't see situations where that's fundamentally misaligned," says Mr. Giarman. "If that was the case you have big problems. But the PE firm might have a need or a feeling to go faster than they perceive the management team is doing. They're generally quite conscious of the fact that that team needs to have a leader that can work well with them or nothing good will happen. There

Q&A

Expanding Need for Global Talent

David Nosal serves as chairman and managing partner of NGS Global – an executive search resource to companies around the world.

Mr. Nosal has handled assignments for public and private companies, working with their boards of directors and search committees in identifying, evaluating and attracting senior management teams.

Do you see executive search firms adding significant value to PE firms?

Absolutely, but not in traditional ways. Doing a specific search is always one way to add value, but we have found that private equity firms also appreciate our providing them with senior talent not specific to a search. Bringing great executive talent to private equity firms that they do not already know is almost as valuable to them as conducting a search.

Describe your firm's PE recruiting practice.

Private equity has continued to represent a significant piece of our growth around the world. Ten years ago it was about 15 to 20 percent and today it represents 35 to 40 percent of our overall business. For our private equity clients we typically conduct searches for the CEO, CFO or chief commercial officer for portfolio companies that may range in size from $50M to $100M on up to $7B to $10B.

What's happening around the global vis-à-vis talent acquisition for PE firms?

Within the private equity community, many portfolio companies are acquiring significant pieces of business outside of the U.S. These organizations now have distributed teams of almost equal size in other regions of the world. With our ever-expanding global footprint, we are now frequently asked to identify candidates who could be based in multiple locations. The same is true for corporate clients who really want to dip into all three major regions of the world for talent at the senior level.

Q&A

Building Winning Management Teams

Invenias Limited is a leading software platform used by more than 1,000 search firms, private equity firms and in-house executive search teams, which rely on its cloud-based platform to transform the productivity of their search operations.

According to Rick Wargo, VP, Strategic Accounts, the ability to capture and leverage high value talent intelligence is central to building a successful strategic hiring capability. In the following interview, he discusses the talent needs of PE firms and how Invenias helps in the hiring of key talent.

Why is talent the No. 1 issue for PE firms?

As a group, private equity firms understand the value of talent more than most. The success of their portfolio companies relies on carefully marrying their financial investments with the right intellectual property, and human capital. This fundamental equation for success has historically led PE firms to be the most frequent and demanding clients of executive search firms and has progressively led the PE industry to focus on and invest in their own talent acquisition Teams to better control the process, deliver more consistent results and codify their human capital IP while building winning management teams.

How does Invenias help PE firms hire key talent?

While executive searches are often conducted in partnership with a hiring manager and two or three additional interviewing managers, talent acquisition in the PE environment routinely encompasses a much broader range of stakeholders. This includes the talent acquisition team, deal partners, subject matter experts/advisors, portfolio company executives and board members, co-investors and due diligence partners. Invenias allows both in-house talent acquisition teams and executive search firms to easily capture high value candidate assessment data and digitally share that information with each stakeholder in a role-appropriate manner.

Who's using Invenias?

Invenias is proud to supply the CRM and database tools used to optimize the talent acquisition process in 25 percent of the 30 largest US-based PE firms, and is recognized as the largest provider of software solutions to the cutting-edge executive search firms who serve the PE industry.

is an element of this in which the team needs to have some sympatico with the private equity firm."

Nothing helps foster such ties any better than having a portfolio company leader who is straightforward and proactive. "Good CEOs are totally transparent," says Mr. Giarman. "They have to be. They don't wait when there's bad news. They don't try to hide things. They're right out front: Here's what's good. Here's what we're working on. The basic blocking and tackling of what a good CEO does generally speaking is going to be the most important thing that gets the PE firm's attention."

Ultimately, success depends on open lines of communication and trust between the portfolio company leadership and the PE firm. "The CEO and CFO have got to able to work in a productive and collaborative manner with the equity sponsor," says Mr. Marshall, of JM Search. "They need to be a great fit with the equity sponsor. Both parties have to trust one another 100 percent. The fit between the CEO and the equity sponsor is extremely important."

"I do my homework, which means lots of due diligence on the equity sponsors our firm works with," says Mr. Marshall. "This includes speaking to CEOs and CFOs who have worked for them, and getting a good feel for the way the sponsor partners with the leaders in its portfolio. Great equity sponsors – and our firm works with many of them – are great partners to their portfolio companies. That's the bottom line."

Certainly one issue that potential portfolio company leaders must often get past is the stereotype of the slash and burn private equity firm that is excessively involved or overly demanding. "Many people who come from corporate environments can sometimes start with a mischaracterization of what PE investors are all about," says Ms. Hammond, of Russell Reynolds. "We've got some CEOs who will talk about working for private equity firms and say,

'They're sharks,' or, 'They're control freaks,' or, 'I'm a tenured 30-year veteran and I'm working with a deal partner who has 15 years of experience and there's a mismatch.' If you are an executive and you don't move beyond those assumptions you're probably going to fail because private equity firms take very different approaches to the way that they engage with their portfolio companies. They all have their own recipe for engaging with executives and they all have varying levels of involvement and engagement depending on their own philosophy and resources and what they can work with. Some CEOs tell us that their private equity firm is barely involved and others say they are very heavily involved, and so when you talk about challenges it really comes down to everyone – ourselves, the CEO and the deal partners really understanding what the playbook is and being very clear and upfront about what the playbook is so that there are no surprises at the end."

Jason Hanold, of Hanold Associates, has his own methods of sizing up just how much the private equity firm is likely to be involved in running the portfolio company's business. "There are easy ways to get at that and it starts with even the interview process," says Mr. Hanold. "Will the PE firm be interviewing finalist candidates? Are they even involved in identifying us as the search partner, or is it the CEO who's reaching out that simply mentions the PE firm? Or maybe the PE firm has nothing to do with the search firm selection or evaluation and they have nothing to do with the candidate who's being hired. Maybe they interview a finalist, almost equivalent to a board in a public company, but that's it. Other times we have PE firms that are coming in and identifying us and then quite frankly they leverage us for all of their portfolio work, as long as we keep doing good work. But they're driving update calls and then it's almost the flip side where then the CEO is meeting

PRODUCT HIGHLIGHT

Human Capital Innovation

First Perform believes there is an overdue opportunity to innovate in the human capital space as an accelerator for the success of organizations.

Through excellence in delivery and innovative thinking, First Perform partners with customers to bring new solutions that will be their differentiators with a shared goal of creating value and building a sustainable foundation. The firm provides end-to-end and modular solutions across the spectrum of human resources.

Products include: talent management and SWOT diagnostics; org design; culture; agile performance; banding & compensation; restructurings; mergers and acquisitions; learning as a differentiator: Interim support or outsourced partner; employee engagement; and best in class reductions in force.

our candidates after they've been vetted by the PE firm, and you have everything in between that."

"But the good news is that for most of those scenarios the two aren't necessarily going in different directions. I've rarely had the scenario where what the executive team wants is different from what the PE firm wants when the PE firm is highly involved. Because they're driving the governance. And usually when we come in to do an HR search they've already had their impact on who is going to be the CEO and maybe concurrently they're figuring out the COO or CFO if it's applicable."

Alice Mann, of Blue Wolf, says her firm strives to keep the relationship with portfolio management teams constructive and collaborative, with both sides working toward the same goals. "We stay very involved because we invest in companies with special situations where there are a lot of opportunities to drive value through business transformation," says Dr. Mann. "So we have operating partners who will often be involved with the executive team. The investment team stays involved. And as the human capital operating partner I'm involved with the executive team and the HR team. But we take a collaborative approach, which is that we're partnering with the team, and we're supporting them to build the capabilities the business needs to succeed – organizational capabilities, human capital capabilities, and leadership capabilities."

That, in turn, plays out in choosing portfolio company leaders. "So one of the factors that you select for is somebody who can thrive in that kind of collaborative environment, who can be a go between their management team and Blue Wolf, who is open to ideas about how to improve the business, how to make things better," she says.

Sometimes, too, the simple truth is that the private equity team has had the experience creating value and knows best how to move forward. Mr. Ferguson, of Perella Weinberg Partners, says that his firm is involved "a great deal" with the business it invests in, usually those with $50 million to $100 million in revenue and $5 million to $10 million in EBITDA.

The firm creates a team around each investment and holds quarterly board meetings, says Mr. Ferguson. "But in between those quarterly board meetings especially in the first year or so, there's a lot of activity around systems identification integration, hiring of people, integrating those people. And so some part of our team could spend a couple of days a month at the portfolio companies, not operating these businesses by any means but by helping them evolve as we're growing the organization and the capabilities of the systems, help them evolve. And then we'll spend a couple of days around the board meetings, and anything after that is episodic."

"If we're going to do an acquisition we'll generally take the point on that because that's not really the

core competency of our portfolio companies," he says. "When we close the deal we have agreement with our partner about how to create value and how to capitalize on that value once that value is created, meaning, how do we exit? Do we want to go public? Do we want to sell to a strategic? What's the best way to capitalize on the value we create? And then we just begin that process and that evolves, that strategy evolves, that view of how to capitalize on the value evolves, but it's a constant dialogue, and sometimes that happens in three years and sometimes that happens in five years, but every one of our conversations is consumed with how does this help create long term equity value. And if it means investing a million dollars we didn't expect because we believe the return on that investment is significant enough to warrant that investment, let's make that investment, because we're going to hold this investment for on average five years. We can all do the math and say, 'Here's what our expectation is with respect to that investment.' Everything is framed with where have we been and where are we going, and what does that mean in terms of creation of equity value?"

Frequently, Mr. Ferguson says, the portfolio companies his firm invests in need to change out their chief financial officer from the start, and the PE firm will see that the portfolio company founder, for example, understands why that must happen. "What they don't realize and what they're blown away by is that if you hire the right person, that person can step into that role, which bridges across finance and into operations, and provide meaningful financial information," says Mr. Ferguson. "They can provide dashboard data that interprets what's going on in a way that these business owners, entrepreneurs, have never thought of. They have never thought of their business that way; they've never seen it presented that way; and for most of these individuals it's really

stimulating to have someone helping them diagnose the business and the issues in their business to help maximize short-term profitability and long-term equity value."

"So we always say, 'Guys, I know you're telling me that you think your controller who you call chief financial officer is fine, but in fact what you have is a controller, and that individual can continue to function in that role as a controller, but what you need is someone who is thinking more strategically, who's thinking more operationally, who is thinking about how to help you make this a better business as opposed to reporting to you what happened in the rearview mirror.' And that's the ah ha moment. When we get these people hired and they've been there for a quarter or two, our chief executive officers all come to us and say, 'Oh my gosh, I had no idea what I was missing.'"

SMART TOOL

Smart Candidate Tool for Private Equity Firms

PrivCo

PrivCo is considered a smart tool for discovering and engaging a new universe of potential candidates. The firm pairs unique financial data sets with comprehensive coverage of the U.S. private company universe. With PrivCo you can quickly hone in on the right companies, identifying executive-level contacts to hone in on talent acquisition targets.

How a private equity firm finds talent for value can differ depending on size. "The large private equity, the megafunds, have an operating group inside the private equity firm, so they've got the deal people and the operating people," says George Davis of Davis Partners Group. "And then they have different segments of operating people within that, so you may have diligence people, you may have operating people who help the CEOs run the companies. Or you can have guys that are talent acquisition as well."

"The mid-tier guys may have just one operating leadership person who is trying to be the general contractor across a wide portfolio of companies but can't. It's like a one armed paper hanger; they're really kind of working like a general contractor but they're not doing the work themselves. The question is, is it high level strategic work or is it low level tactical work? A lot of people like to hire the strategic people but they're asking them to do tactical jobs. So a lot of these firms have gone off to hire ex-recruiters to help get it right. But they're still looking for the magic solution."

Talent Challenges of Mid-Market Players

Ms. Hagen, chief talent officer for Littlejohn & Company, agrees that mid-market firms like hers have special challenges. "One of the things that we face and challenge ourselves to do," she says, "is to find great talent with relevant experience who may have had some training and grooming in larger companies but who have the ability to transition to the smaller environment where they're much more hands-on and may not have the resources that are common in big Fortune 100 companies but have that same quality of strategic thinking, the quality of operational discipline that they could bring to a mid-market company."

As for the smaller firms, oftentimes the companies are in large part left to do it themselves. "The challenge in smaller companies in general is you don't have quite the resources, you need to be more hands on, and some people love doing that," says Mr. Giarman. "I've talked to executives about some of these CEO positions and what I hear is, 'Oh, I can do that because I've done it before.' Well, that's really not the question. The question is do you want to do it here? Are you motivated to do it with this team, change the team, work with this PE firm? Are you going to apply the energy required and effort to get this thing to full liquidity in five years? So I do find some CEOs kind of give it lip service. They say, 'I've been in more complex environments, therefore I can do something that's less complex.' But that theory has been somewhat debunked. It used to be if you're coming in from something big and you put them in something small it's simpler. That's not true. It's harder in different ways. And it's more hands on. And you have to think like an owner and allocate capital differently.

INSIGHT

5 Things CEOs Wished They Knew Before Their First Portfolio Company Role

Understand how private equity works. The fundamentals of how a fund raises money, its inner workings and hierarchy, and its politics all can affect how the firm interacts with your business. Are the partners distracted by other deal activity? Is there another portfolio company in trouble that might change the way the firm works with your business? Also, understand the deal structure and the implications of the structure. How much has the firm already invested in the business? How much capital is left for acquisitions or other capital spending? What's the approval process for gaining access to those funds?

SpencerStuart

Understand how the private equity sponsor will interact with the business. Experienced CEOs said working with private equity is much easier when you know the players in the firm and how they interact with the company: who does the work inside the firm, who's paying attention on conference calls, who to call in advance of a board meeting and who to follow up with after the meeting.

The depth and quality of people is almost always different. Recognize and address gaps in capabilities and processes early on, based on the strategy and exit plan for the business.

Manage expectations. Don't be overly optimistic about the time frame for turning around the business. Expect that not everything will go as planned. As one CEO cautioned, "If you say it's going to take three to five years to turn around the business, and it gets done in three-and-a-half years, you're a hero. If you say it's going to take two or three years, and you get it done in three-and-a-half, you're in trouble."

It's OK to say you don't have all the answers. Most first-time portfolio company CEOs are reluctant to admit that they don't have the solution to every problem, but CEOs who have been through the process say they learned to engage the board on the toughest challenges. Seeking advice and ideas from the board when challenges arise often can result in surprising and successful solutions.

Source: Spencer Stuart

CASE STUDY

Partnering with Clients to Facilitate Transformation

A private equity client was in the midst of executing on an M&A roll-up strategy. Several of the assets were underperforming many years into ownership. The client engaged Korn Ferry to diagnose the organization to them make critical leadership decisions, design the organization, and improve effectiveness of a new leadership team.

Korn Ferry conducted in-depth, multi-method leadership assessments and an organization and culture review. As a result, the client was positioned to make decisions based upon reliable and predictive data and redesign the organization for growth and performance.

Based on results and high sensitivity to organization dynamics, the client engaged Korn Ferry to apply these successful methods across other growth and turnaround situations.

Learn more about Korn Ferry's PE Center of Expertise

Source: Korn Ferry

It's a very difficult job in smaller companies, but there are definitely people that want to move the needle and thrive doing it."

For smaller PE-backed businesses, compensation for top-level talent can be a challenge, especially given their lower cost structure. Candidates for key roles must be educated about the upside opportunity relative to the equity component of the compensation and how it will boost their careers. "This means the recruiting firm, hiring manager and PE firm need to work closely on strategy to educate candidates," says Mr. Giarman. "Before embarking on the search, all should agree on the 'talking points' and materials (beyond a specification) that illustrate the magnitude of the opportunity... It is critical that the search firm qualify early and often and move on if candidates cannot accept cash compensation parameters."

Portfolio companies can further bolster their case by teaching candidates about the PE firm itself. Indeed, many of the mid-market and smaller firms operate, often by design, with a low profile that aligns with their target portfolio companies. "The team working the search must emphasize the value of the firm that will become their partner, both in terms of their successful track record and partnering style working with management," he says.

As Mr. Davis noted, one of the trends coursing through private equity firms these days is the bringing of talent partners on board. "In many ways, that demonstrates their view that talent is an even more meaningful part of the equation," says Kenna Baudin, of Egon Zehnder. "It's not just financial engineering. It's not just buying good businesses. It's thinking about talent more holistically in the portfolio."

Mr. Ferguson, of Perella Weinberg Partners, says he is a big advocate of PE firms like his bringing in a talent officer. During a career that includes more than 13 years in private equity at JPMorgan, he has seen up-close how much human resources can contribute to a firm's portfolio operations. "So many firms have now gotten to that place where they've added a VP of talent within the private equity firms focused on assessing talent and the diligence process, in driving the acquisition of talent once acquired, so kind of overseeing the search, and really focusing on the culture and the health of the organization once you've made the investment," he says. "It's an incredibly valuable position and one that as we get larger we're going to have a person like that. When you think about it, we say we invest in businesses, yes, but we invest in people, and I will tell you that it needs to become more of a focus."

As chief talent officer for Littlejohn & Company, Ms. Hagen, for her part, is largely a one-woman show. She joined the firm a year ago after stints at LVMH, PepsiCo

and Russell Reynolds Associates, among others. Her presence allows for a common point of knowledge on the talent side about the PE firm, its tastes, its portfolio companies and its search firm partners. "One of the benefits of being here and working on a number of searches across the firm with all our different partners is that I'm getting a very strong sense of the kinds of qualities and competencies and kind of leadership capabilities that we look for in our portfolio company leaders," she says. "For me to be able to play that role consistently and to then partner with our search firms to guide the work that they're doing so that we can come to a better answer faster is, that's a big value of this role. I can help us waste less time on candidates who don't have the qualities of ambition and energy and risk appetite that we're looking for."

Making Adjustments

Ms. Hagen is the first talent person that Littlejohn has had in the role. "They had not had a chief talent officer for Littlejohn before and so one of the things I have had to do is to be strategic in our selection of search partners and making sure that we're using the right partner for the right role depending on its industry, the function, the location, as well as the ability of the firm to provide us a level of partnership that we need, which can differ from company to company and from role to role. There are times that we, Littlejohn, are very much in the driver's seat on the search and there are times that our leadership teams at our portfolio companies are much more in the driver's seat. And my role is really to make sure that the search goes smoothly, in much more of an advisory role than a leadership on the search role."

For talent leaders, there are certain adjustments to make coming to work for a private equity firm, whether it be coming from a multinational, as Ms. Hagen did, or a search firm, like Mr. Holzemer, of TPG. "I would say from a nuance point of view, more at a broader

level, one of the things that's very different in being in a private equity environment versus being in a public environment is that we can move very, very quickly," says Ms. Hagen. "And while we don't have the kind of access to the internal pipelines of talent that fuel a lot of big company mobility and searches, we also can be pretty nimble. We try to make decisions quickly about when we need to make a change in one of our companies, or when we meet a fantastic candidate that we think could be right for one of our companies, if we don't have a particular role open at the time we might look for an opportunity to have them as part of the board or as part of some sort of advisory to have them in the orbit at Littlejohn so we can develop that relationship and then find ways to partner with them so they're adding value to the overall portfolio even if we don't have the specific role open at the time. Maybe they're advising us in a due diligence situation or a potential purchase. We may work with them in a board role. But the ability to engage with talent ahead of the need to bring someone in to actually be in an open role, I find we have a bit more flexibility to do that at senior levels in the private equity world than a lot of public companies can do."

Living With the Changes You Drive

Mr. Holzemer, for his part, was until a couple years ago co-head for North America at Spencer Stuart. Although the essence of his work continues to revolve around finding great talent, the private equity world is not quite the same as a search firm. "At the end of the day it's a different industry," he says. "So in my case taking the skills, disciplines and expertise I developed in one industry and applying it in another, it's a change."

These days, of course, recruitment firms offer many more services than search alone, be it governance consulting, assessment, coaching and more. "You work with a principal or an owner of businesses and you get a chance to apply those disciplines," says Mr. Holzemer, "but [in-house], you get to apply them not just as an advisor or consultant that sells services and serves many clients simultaneously, but as a principal. You live with the changes you drive. It requires an ownership mentality, because you're collaborating with the investment partners who did the deal and the operating partners who are working with company management to drive change and create value."

"What's interesting about being in-house is that you're applying disciplines directly; you own the process and see it through," he says. "It offers a unique partnership opportunity and perspective. When you're an outside advisor, good clients share a lot of information to help you give them thoughtful and well-rounded advice on a search, assessment or succession matter. But you're never an insider – you're learning as quickly as you can about the business and the situation. When you're applying these disciplines from the inside you have insight into a company's ecosystem – financial, operational, cultural, etc. It brings new challenges but makes it interesting."

INDUSTRY VIEWPOINTS

VIEWPOINTS

Hunt Scanlon keeps tabs on an ever-expanding executive search and talent management sector that far exceeds where the industry was just a decade ago. Today, Hunt Scanlon tracks some 16,000 executive search consultants at more than 3,600 recruiting firms in North America and another 4,000 overseas, spanning Europe, Asia, Africa and the Middle East, and everywhere else in between. We're also tracking leadership assessment firms, talent solutions providers, consultancies, and those focused on coaching and training. This is an active sector, to say the least.

To round out our study this year, we invited six talent specialists focused on the private equity sector to bring us their market insights. As they will be the first to admit, all of them face a host of challenges. As such, their 'Viewpoints' examine a multitude of topics this year, including: why there's now a premium on great talent; how to select top executives for transformational investments in private equity; why and how to groom the next generation of private equity leaders; CEO assessment and the performance of portfolio companies; the talent challenges facing smaller mid-market PE portfolio companies; and building & activating championship teams.

So, if you're interested in hearing from the industry's most trusted and respected talent leadership advisory professionals, we encourage you to take the time to read this outstanding section of this year's report.

WHY THERE'S NOW A PREMIUM ON GREAT TALENT

Tom Nieman, Co-Founder of Signal Partners

Tom Nieman is a co-founder of Signal Partners. He is also founder & CEO of Signal's predecessor company, Fortis Partners, a full-stack search firm that spanned both executive and non-executive recruiting. For the last 20 he has recruited CEOs and their direct reports for venture- and PE-backed companies nationwide, as well as partners for firms such as Kleiner Perkins and Silver Lake Partners.

Tom has led searches for companies such as: Houzz (VP Finance, VP Global Sales; VP Industry Solutions; VP Partnerships), Wealthfront (CFO; Chief Data Science Officer), Chegg (CEO), LifeLock (CMO), Rival (Head of People; Head of Finance), Telesign (CEO), Tastemade (CFO), RuffaloNoelLevitz (CEO), Acxiom (Board Members), and Invoice Cloud (President), among others.

In the context of private equity, when it comes to talent acquisition, what developments have you noticed?

In general, the biggest development is the increased attention being paid to talent acquisition within portfolio companies. Obviously, talent on the investment platform itself is important, but the focus on how to acquire, assess, and measure talent inside portfolio companies has increased dramatically.

Any thoughts on what's driving this?

In short, numbers. Against the backdrop of tighter public equity markets the private equity markets have become red hot. The big firms are getting bigger, there are lots of new firms, and they're all awash in capital. So now there's more competition. And the way you compete is by creating valuable companies. And it's no secret that the best way to create valuable companies is by attracting and hiring the best people – at all levels. I saw some data recently from a Milken Institute report that highlighted the 10 largest employers in the private sector today. N0. 1 on the list, by a longshot, was Walmart with a little over 2M employees. But the next eight on the list, if you impute the number of employees across their portfolio companies, were all private equity firms. Carlyle and KKR each have ~700K, Blackstone ~600K, Apollo, Warbug, and General Atlantic each have ~300K. So PE firms effectively employ lots of people – and they're the linchpin to success. So the extent to which PE sponsors can improve the quality and caliber of people in their portfolio companies – again, at all levels – they will create more value, drive more exits, and have happier LPs.

Has this affected the recruiting industry in a major way?

Not drastically. At least not yet, other than the lights are now a little brighter. But I can tell you that we took notice a few years ago, re-examined what we were doing and overhauled much of it to address this specifically.

Explain.

In a somewhat oversimplified view, the recruiting universe is filled with lots of retained search firms, on the one hand, and a lot of contingency agencies, on the other. The former are white-glove, value-add, and if you work with the right one, they are very, very good at what they do. But they also come at a price. A retained search simply isn't economically viable for all your hiring needs. It's just too expensive. But at the same time, for every executive position a company fills, there is some order of magnitude of other really important, mission-critical, non-executive positions that need to be filled. Directors, managers, strategic individual contributors, etc. These are the people that make or break plan and drive MOIC and if running a retained search to acquire them is out of the question, what is your next best option? It's contingency. And while that may seem financially attractive with nothing up front, and you pay only when somebody gets hired, it also comes at a price. Junior, often inexperienced, people waving your brand and story in the marketplace, pushing resumes in the hope of "getting a deal done" so they can get a fee. There is little, if any, added value. But, hey, it's economical. This is what struck me as a really poor consideration set for financial sponsors and their CEOs, so we decided to address it.

But aren't there some firms that already play in that middle zone?

Yes, some big firms have "middle management" solutions. But for the most part you have myriad contingency firms trying to up-level or reposition themselves to work on more

senior roles or de-risk their all-or-nothing fee structure. From the bottom up. I looked at this and challenged a lot of my own thinking about the stodgy search industry and how search firms have traditionally operated, and the proverbial light went off over my head. It became clear that there was a very large, under-addressed opportunity to bring the rigor, high service levels and lessons learned from doing high-end retained search and apply it to what I like to call "all the other stuff." Going "full-stack," if you will. From the top down. And priced in a way that makes it a very attractive economic proposition, as well.

"PE firms effectively employ lots of people – and they're the linchpin to success. So the extent to which PE sponsors can improve the quality and caliber of people in their portfolio companies – again, at all levels – they will createmore value, drive more exits, and have happier LPs."

Does technology play a role in this?

For sure. Technology has changed a lot, needless to say. When I started in the search business there was no Internet. Kicking off a search meant diving into a 15-volume publication of Standard Industrial Codes – "SIC Codes". It was a directory of literally every legally recognized company. You would look up your client and if they were classified as 04212, then you would look up all companies that fell under 04212. Then you copy down the entire list of those companies, because that's the best proxy for competitors. Then you look up each of those companies, find the corporate phone number, call the company and see if you could cajole some overworked receptionist into coughing up names. It was wild. Very cloak-and-dagger. Fast forward to today and we've developed an integrated tech stack that allows us to sign off on a new mandate, drive very targeted primary and secondary research, and get a message to a very targeted universe of people within a day. It's amazing.

Changing gears a bit, what is it you and your partners look for when trying to recruit great talent?

I've been doing this for a long time. I was very, very lucky early in my career to work for a guy named Dave Beirne. An amazing guy and a remarkable headhunter. I learned a ton from him and was fortunate to have been one of his associates in the 90s while he did the CEO searches for Netscape and Ebay, the COO search for Microsoft, and recruited Eric Schmidt to run Novell, among others. But I guess my point is that, back then, as the Internet was just beginning to take hold, tech investing was still a bit of a cottage industry. There wasn't a ton of attention paid to who is or isn't a rockstar talent. Mostly, I guess, because there weren't as many success stories as there are today. Information was scarce, exits were smaller and less frequent, and there was a lot of guessing going on. It's very different today, with the industry more mature and so much more capital allocated to the category. I think this inherently puts a premium on great talent.

How do you distinguish the good from the great?

First, you need some of the tenure that gives you perspective. In other words you need context, a little 'inside baseball,' so you can look at somebody's background, recognize companies and have more than a cursory understanding about them. How companies fared, their reputation, their investors, whether they won, or lost, why, etc. It's also critical to dig in and understand transitions. Being able to unearth the real drivers behind somebody's move from Company A to Company B, whether a move was voluntary or not, etc. Grasping the fundamental reasons behind these moves speaks volumes, helps you better hear what's not being said explicitly, as well as what is. For example, an executive who has worked for the same CEO three times in a row, or a CEO who repeatedly had the same set of same financial sponsors. The signals are there. But if you don't have the context or ask the right questions, you'll never see them.

What else, specifically?

There are some personal characteristics that always seem to shine through with great people. Sure, elite education and experience at academy companies are nice. But they

don't always signal the truth. Grit is near the top of the list for me. I love grit. Angela Duckworth explores grit in depth in her recent book. In essence, "talent" is what you're born with while "grit" is the characteristic that pushes somebody to take those innate talents, and hone them to take you to the next level. People with grit have humility, focus and passion. They do the hard things when nobody's looking. They make sacrifices, practice diligently, work hard and persevere. Sure they may "fail" along the way. But that's part of what makes a gritty person great. Gritty people are driven, lead by example, love what they do and don't let anything get in their way. It's not "work" to them. They love it. And it's contagious. Other gritty people follow those with grit. They're the ones you want in your company. Similarly, in the absence of grit, you run the risk of hiring somebody who may have been blessed with a great set of innate skills, and maybe experienced success in life, but never took risks or pushed themselves. For these people, being successful has always trumped the fear of failing so they lack grit. Beware these people!

Back to your new model, are there any distinct benefits that might not be totally obvious to PE sponsors?

Yes, there are. I'm not sure exactly how to articulate it, but it's rooted in quality and message control. To my earlier comments about price, most companies that are growing and serious about talent acquisition are often cornered into using a variety of firms for different levels of hiring. But there is risk inherent in this division of labor. I truly believe a single source provider for recruiting across levels mitigates this risk. And for your non-exec recruiting, in particular, affords you retained service levels with success-based pricing. I guess the point is that recruiting is an incredibly effective and affordable marketing channel when it is considered in this light. Every recruiter you employ, whether directly or indirectly, is somehow or another trading on your brand equity – not an insignificant decision.

THE IMPERFECT STORM: SELECTING TOP EXECUTIVES FOR TRANSFORMATIONAL INVESTMENTS IN PRIVATE EQUITY

Dr. Alice Mann, Human Capital Operating Partner at Blue Wolf Capital Partners LLC

Dr. Alice Mann is an operating partner at Blue Wolf Capital Partners LLC. The Blue Wolf Capital Funds are a family of private funds which focus on transformational investments in middle market companies. For over 20 years, Dr. Mann has advised senior executives to build high-performing leadership teams, develop winning talent strategies, and design organizations that achieve outstanding performance results. As the firm's human capital leader, Dr. Mann drives Blue Wolf's human capital due diligence and works directly with the leadership of Blue Wolf's portfolio companies to develop their talent strategies and capabilities to deliver on their value creation plans.

At many organizations, boards and C-suite executives spend much of their time focusing on protecting their business model from outside influences. In the process, however, they may be overlooking a greater risk that is emerging from within – the impending shortage of C-suite talent that will be vital to drive value creation in the future.

A number of factors, ranging from demographics to increased market competition, are placing the possibility of filling CEO roles, in particular, that become vacant in the next 10 years at risk.

Imagine the following: you're the CEO for a company and you have to tell your board of directors that you've just under-delivered on EBITDA. No matter, next year's forecast looks much better, as you've recently executed a major acquisition that will position your company for growth and transformation. But, that transaction hasn't yet produced all of the cost savings that were forecast. You're confident that next year will.

Sound complicated? Now add in board members who disagree about your commercial strategy and what the business priorities should be for the next 12 months, much less the next quarter.

Successfully navigating this hypothetical board meeting calls for a particular type of CEO: a leader able to weather storms brought about by uncertainty, miscalculation, and misfortune. It's the kind of skillset that often proves invaluable in the context of private equity.

Leading Teams Through Transformational Investments

Private equity seeks opportunities to deliver substantial value in our messy, imperfect and highly complex world that others have either missed or lacked the risk tolerance to pursue. Building financial models and other analytical tools for approximating the uncertain realities of how a business, its people and industry will perform over time is integral to helping identify worthy investments. But beyond the numbers, the value of an investment is often dependent on a company's human capital; people with a particular mindset can make or break the profitability of a portfolio company.

As human capital operating partner at Blue Wolf Capital, a private equity firm in Manhattan, my job is to identify people who can lead teams through "transformational investments." These are investments that require several years of business transformation in order to prepare them for a sale to a strategic buyer at a premium multiple.

For example, a transformational investment could be a company that acquires its closest competitor only to require rapid innovation in its pricing strategy and software platforms to keep up with EBITDA projections. Or maybe it's a family founder-led company based in Texas in a developing industry that has invested handsomely in their facilities, but not at all in their systems, business processes, or talent. The people I look for to lead companies like this can't be faint of heart—they see these uncertain situations as exciting opportunities filled with promise.

But how do you select the successful leaders who will thrive in such an imperfect universe of opportunity? Not only do these leaders need to embrace challenges as opportunities within the companies they lead, but they must partner well with their private equity sponsors, adding another layer of complexity to company-wide relationships. We call people who fit this bill "imperfect leaders." And they're just who we're looking for.

Four Traits of Imperfect Leaders

These imperfect leaders recognize the chaotic world of transformational investments in private equity and can maximize value. I've also found that they tend to share four traits in common:

1) Imperfect leaders are comfortable making decisions and taking action with a sense of urgency and a laser focus on achieving results, because they are energized by uncertainties and complexities in business that others would find paralyzing.

In late 2013, Hologic was a leading manufacturer of diagnostic tools for cervical cancer and breast biopsy tools - but was still not producing strong returns. Former Stryker executive Stephen MacMillan was appointed as the new CEO to lead the company through a major transformation. The medical device industry is highly profitable but also one of the most uncertain. Nonetheless, MacMillan moved decisively. In his first 14 months, he top-graded his executive team, and the team increased the sales of a three-dimensional breast imaging machine made by the company that costs around $350,000. They drove up demand from hospitals for the technology by aggressively marketing three-dimensional scans directly to consumers, who then requested the scans from their doctors for them. MacMillan's urgent action dramatically improved the company's financial performance, with shares more than doubling in value over his first four years.

2) Imperfect leaders accept their own flaws and, by extension, the flaws and mistakes of their team members. As long as everyone can learn quickly from their mistakes and adapt their own behavior to fit the business situation, imperfect leaders press on.

Imperfect leaders have often faced their own limitations, whether through heart-stopping challenges, critical feedback from their co-workers, or company-wide hardships, but they have persevered nonetheless. In his bestselling business book, Principles, Ray Dalio, the founder of one of the largest hedge funds in the world, Bridgewater Associates, shares the origins of his unlikely success. His early years were scattered with failure. Intelligent, but a terrible student; fired from one of his first jobs for scandalous behavior.

To top it off, Dalio publicly predicted in 1982 that the economy was headed for a great depression. As history shows, he was dead wrong. But Dalio learned from this public mistake, understanding that getting it right required more listening and internalizing of the views of other smart people. Changing his behavior by taking the advice of those around him drastically changed his course, leading to the immense success he has achieved today.

"Private equity needs people with the right approach to creating value in imperfect situations. Not only must these leaders embrace business challenges as opportunities, but they need to lead and partner effectively with a whole slew of imperfect people."

3) Imperfect leaders know that getting it right is more important than being right, so they surround themselves with smart team members who think differently than them. And they empower those people to openly disagree with them in pursuit of building a better company.

These CEOs are using essentially the same techniques to extract value from a risky business terrain that fact checkers and superforecasters use to extract facts in our "post-truth" world. In a Stanford experiment, 45 people were asked to evaluate the credibility of information on different websites. 10 were PhD historians, 10 were fact checkers and the rest were college students. The surprising result: PhDs didn't do any better than undergrads – and both did far worse than fact checkers.

The main reason for the fact checkers' higher performance was the practice of "reading laterally." They opened multiple tabs on their browser, evaluating the credibility of every site by going to another site — before even considering the site's content. Just like successful imperfect leaders, they were allergic to certainty and wanted to challenge every assumption.

4) Imperfect leaders are open-minded, transparent and collaborative about their decision-making in real time, leaving no surprises for their teams or their private equity sponsors. These leaders make excellent thought partners, because they are constantly seeking new and improved ways to run the business and lead their teams.

When Tony Hsieh founded Zappos, he created a radically transparent business model. Zappos' organizational chart is available in real-time online, allowing each of the company's 1,500 employees to view the purposes and accountabilities of every other employee. Browsable and updatable governance methods and policy updates are also accessible, allowing every employee to view and contribute to the ever-improving and evolving structure of the company. In his role, Hsieh compares himself to a mayor who doesn't tell his residents what to do or where to live but provides an infrastructure under which growth and innovation are allowed to thrive.

Unconventional Methods for Selecting Imperfect Leaders

So, how do you select for leaders that can navigate imperfect storms under changing conditions, quickly learn and adapt through trial and error, then go on to create high performing companies?

Just as I've discovered these four qualities of successful candidates, I've also found a major problem in the selection process. Despite the fact that Ray Dalio likely would have failed any conventional assessment tools for leadership selection, he is one of the top 100 billionaires in the world today. What gives?

Unfortunately, traditional executive assessment methods are not engineered to find imperfect leaders. Instead the industry seeks "ideal" candidates. What is an "executive scorecard" if not a description of the perfect state? What are "leadership competencies" if not a checklist for the profile of perfection? What is a "behavioral or cognitive assessment," if not a normative tool for quickly establishing whether a candidate's behavior and mental processing fits into an ideal range?

These conventional tools are important for establishing whether the candidate has a track record of high achievement and accomplishments that are relevant to the CEO assignment at hand. Does the candidate check the boxes on the industry knowledge and the technical and functional expertise they would need to excel at a specific leadership role? Are there any red or yellow flags in their leadership style and personality that would clash with the current team and company culture? Can they collaborate well and build a wide range of relationships with their team and their private equity partners?

The conventional talent assessment tools are critical for establishing a baseline of the level of experience, skills and temperament that a candidate must have to succeed in a particular role. All of this information provides important inputs to the selection process. But when it comes to selecting imperfect leaders, you can't stop there.

These tools alone won't give you all the indicators you need ahead of time to know why one founder CEO will successfully make the transition into a professional CEO in a PE-backed company and another won't. Or why one CEO can fill the shoes of his predecessor of forty-years despite having a completely opposite personality, but another with a more similar personality to his predecessor will fail miserably. A stellar candidate may pass all the conventional risk profile tests with flying colors, but still not have a clue about the rules for engaging effectively with diverse teams.

But you can look for other indicators for how a potential candidate will lead to get a glimpse around the corner of what a future partnership with them might be like. These are the indicators that often get missed in conventional assessment methods.

For example, informal reference calls with those in your network who have previously worked with the candidate can go a long way. You can do as many interviews with a candidate's previous customers as possible. You can be relentless about asking for feedback from the entire diligence team about everything from a management team's expertise to how they interact and communicate with external partners as well as the most junior members of the team. You can learn more about how they will treat their employees based on how they interact with your administrative assistant.

Often a potential candidate will tell you before the deal even closes with both their actions and their words what they want from a private equity sponsor. And whether that is to be left alone or have private equity partners set clear goals and expectations can make a huge difference to your alignment with them throughout the investment.

Much of the messiness (and the opportunity!) in private equity investments in transformational opportunities is created by highly imperfect human beings working together to generate large sums of money in a limited amount of time. It's a pressure cooker environment. And even with the most aligned and motivating incentives, such investments can involve many cooks in the kitchen working elbow-to-elbow together, often without a common recipe, and sometimes without all of the requisite techniques and tools. Private equity needs people with the right approach to creating value in imperfect situations. Not only must these leaders embrace business challenges as opportunities, but they need to lead and partner effectively with a whole slew of imperfect people.

THE SUCCESSION IMPERATIVE: WHY AND HOW TO GROOM THE NEXT GENERATION OF PRIVATE EQUITY LEADERS

Steve Potter, CEO of Odgers Berndtson US

Steve Potter is the CEO of Odgers Berndtson US and sits on its global board. Steve spent over two decades as a founder, CEO and senior executive of several financial services executive search firms. In 2002, he co-founded and served as CEO of Sextant Search Partners. In 1999, Steve was appointed CEO of TMP Worldwide Executive Search following TMP's acquisition of Highland Search Group, a boutique executive search firm that he had co-founded in 1995. He was one of five divisional CEOs for TMP, a $7B public company and owner of monster.com. Steve began his recruiting career at Russell Reynolds Associates, and in 1982 he headed the firm's global banking and merchant banking practices. He oversaw Russell Reynolds' Asian operation and served as a member of the executive committee.

Last year, one of Europe's oldest and most successful buyout firms announced its imminent closure. The firm, which I'll call Addison Miller Capital, was founded in 1985 by Neil Addison and Drew Miller (not their real names) and was once one of the biggest players in European private equity. Then, in 2012, midway through its fifth fund, Addison unexpectedly passed away, leaving Miller alone at the helm.

At first, this seemed more of a tragedy than a catastrophe. To compensate for Addison's absence, and to address limited partner concerns about succession, Miller restructured. He did many things right: He introduced a partnership, renaming the firm AF Capital Partners to align the brand with its new structure; he adjusted compensation to more equally distribute incentives within the firm; he refined their investment strategy, refocusing on Northern Europe; and he announced that he would be phasing out of active management, leaving room for the next generation of talent to grow upwards.

But when the firm began trying to raise its sixth fund, investors balked. Asked to invest in what amounted to a new executive team, they demanded that Miller remain fully engaged with the fund for its duration. This was too big of an ask. If the fund ran for 10 years (the industry average is 13), Miller would be in his 70s before he could begin transitioning into retirement. Instead, Miller decided to cancel the planned fund. And with that, 30+ years after it began, Addison Miller's journey ended.

Many lessons can be drawn from the example of Addison Miller, but two stand out. First, succession planning must be preemptive, not responsive. Second, the reward for successfully executing a succession plan is your firm's survival.

Maturing Industry, Maturing Investors

By most metrics, the private equity industry is booming. 2018 saw more than 3,500 buyouts with a total buyout value of $556bn, more than 1/3 of which originated in North America. The industry is collectively sitting on more than a $1 trillion of dry powder. Therefore, competition for investments is fierce. And in their pre-investment due diligence, which has become increasingly thorough, LPs now place significant value on succession structures, firm culture, profit dispersion, and the collective track record of the deal team(s).

Here are three major trends that demonstrate the need for clear and decisive succession planning:

The founders are aging – The private equity industry is effectively four decades old, and its founding titans are aging out of the workforce. This was clearly demonstrated when, over the course of a single year, KKR, Blackstone, Carlyle, and Apollo each elevated a new generation into successional roles. These four firms—the four largest alternative investment firms in the world—have long been industry bellwethers, and the message they sent was clear: Private equity firms need to formalize their process of succession. Why? Because failure to implement a succession plan can lead—as Addison Miller demonstrated—to the destruction of the firm. And as David Rubenstein said about Carlyle's founding team, "It's not clear that people who are sixty-eight, sixty-eight, and seventy-one are the best leaders of the future."

Investors care about succession – The current generation of LPs are increasingly rigorous in their pre-investment due diligence. Drawing on significant data analytic capabilities, LPs can run deep analyses of GP performance and the performance histories of former, current, or proposed portfolio investments. At the same time, they use qualitative models to look beyond track records and strategies for performance predictors like a GP's structure, culture, talent pipeline, and the distribution of economics within its management team—all of which are interrelated and influenced by successional policies and structures.

Investors are formalizing their private equity relationships – Due diligence takes time, energy, and money. To cut down on in-house costs, LPs are consolidating their relationships with GPs. This does not mean that they are investing any less in private equity; they're just investing more money with fewer firms, giving preferential leverage to big firms that, like "one-stop-shops," run multiple funds simultaneously, each with different investment strategies and approaches that can provide a diverse investment base under one umbrella. It also gives leverage to emerging funds, run by young managers, who can promise LPs a multi-decade relationship under the current management team. The result for the GP fundraising market is bifurcation: On the one hand, Apollo can raise a gigantic fund in a very brief period of time; on the other, middle-market GPs are vigorously competing for investor attention, trying to differentiate themselves within a crowded market and prove that their firm—whether old or new—has the capacity to be a long-time, high-performance partner.

All three of these trends points towards the same fact: A private equity firm's ability to raise funds is intrinsically linked to its ability to build an incremental, transparent, and forward-looking system of succession.

What a Good Succession Plan Looks like

The goal of a succession plan is to identify high-potential individuals and invest in their development such that they are eventually able to assume leadership roles. This means that a fully functional succession plan is not simply about a one-time replacement of a CEO or founder. It's about creating a system for assessment, education, and replacement that operates at every level of the organization. In large firms, the infrastructure to do this may already exist at the lower levels, which means that a succession plan is in essence an upward extension of this structure. But in small and mid-sized firms with flatter structures and more shared responsibility, the pipeline to the executive's chair is often less defined and may take years to build.

"Succession planning must be preemptive, not responsive. The reward for successfully executing a succession plan is your firm's survival."

There is no one-size-fits-all solution to succession planning. Each firm will need to tailor general concepts to the shape and composition of their organization. Successful succession plans, however, do tend to share five key similarities:

They are founder led – A succession plan must be voluntary on the part of the founder(s), who should actively socialize the plan with investors, portfolio teams, and GP employees, stressing the fact that the next generation is well-equipped to provide a continuity of performance into the firm's post-founder period.

They account for planned and unplanned retirement contingencies – A preemptive succession plan is, first and foremost, a risk prevention measure that ensures that a leader's departure does not constitute an existential threat to the firm. To accomplish this, the plan formalizes a team of known and competent secondary leadership whose existence can (a) dissuade LPs from invoking key man clauses and forcing the early closure of a fund, and/or (b) persuade LPs to participate in follow-on funds in the absence of a founder. As such, a good succession plan is actually two separate plans.

Plan A covers the ideal scenario: It outlines the gradual departure of the current leader or founder. Plan A looks basically the same whether applied in hierarchal publicly traded firms or smaller middle-market partnerships: As the founders decrease their decision-making involvement, they cede graduated levels of operational and strategic control to their successors.

Plan B, on the other hand, is all about disaster mitigation. It's in place to account for sudden, unplanned departures. This is especially relevant to small or mid-sized firms with just one CEO and no prepared successor. A firm has several options here. Perhaps the chairman of the board steps in and runs day-to-day operations until a new successor can be found. Perhaps the executive committee assumes a joint CEO function for a brief period. When properly communicated, a formalized Plan B can provide real value to the firm even if it's never enacted, helping convince LPs that deal flow will not be hamstrung by the death, illness, or unplanned retirement of a senior member often leadership team.

They are preemptive and incremental – Succession plans should be articulated years before the founders actively plan to retire, giving them time to oversee and advise the next generation in their assumption of leadership duties. The key is to institutionalize paths of growth within the firm, with future leaders gradually assuming more integral roles in strategy, management, and decision-making. Ideally, this would happen over the lifespan of one or more funds, thus avoiding a cold turkey transition; LPs need time to get comfortable with the new leaders. Done correctly, leadership succession will take place largely under the founder's oversight. That way, by the time they are ready to retire, they can truthfully tell investors that the transition has already occurred.

They redistribute wealth – Succession plans should actively consider the ways in which carry is allocated across teams. The allocation should seem fair to all members, reflecting the contribution each person makes to each fund—especially with reference to investment analyses. This means that when founders or other senior executives begin to decrease their active role in investment decisions, their carry allocation should decrease accordingly. Failure to adjust participation systems will lead to employee disgruntlement, or even defection, and can disconcert investors, who want to see that each member of the management team has a personal stake in the performance of the fund. Fair participation systems extend the commitment horizons of employees and help build a culture of ownership, meritocracy, and shared investment, which aids the attraction and retention of top performers. Note: Founders should avoid the temptation to compensate for their decreased percentage of carry by raising larger funds—a move that may endanger their firm and concern LPs.

They are holistic – A good succession plan does more than line up a number two. It also validates investor faith in a firm's essential competency, letting investors appreciate the firm as an institution rather than a single dynamic individual. As senior talent replaces the founders, junior professionals need to be raised into the newly vacated roles. Talented people need growth opportunities; they need formal and clearly articulated paths into greater levels of responsibility, clout, and compensation. Firms that build these pipelines will find themselves able to attract and, more importantly, retain top talent, which will give them the flexibility to adjust team composition according to their investment strategies or market demands. A succession plan is not, therefore, about simply replacing the founder; it's about planning the replacement to the founder's replacement, and thus establishing a system of education, growth, and graduated responsibility that will give employees of all levels the sense that this is a firm in which they can grow.

Final Thoughts

Let's conclude where we began, with Addison Miller. Let's imagine that the firm had gone about its restructuring in 2006, the year prior to the launch of its fifth fund and six years before Addison's untimely death. Let's imagine that both founders, in 2006, had fully committed as co-key men for the duration of the fund and then spent the next few years gradually ceding responsibility to the next generation. Let's imagine that, because they'd restructured the economics, systematized the talent pipeline, and clearly communicated their succession plan, they had no trouble with talent retention and were able to groom new leadership through the full lifespan of the next fund. If these steps had been taken, would Addison's death have set off a chain reaction that led to the closure of the firm? I don't think so. I believe that Miller would have been able to either raise a sixth fund or, if he preferred, retire and let his successors raise it. After all, if any prospective LP balked at his planned departure, Miller could have simply gestured to his successor and said, "It's all right. Juliette has basically been running the show for years."

CEO ASSESSMENT AND THE PERFORMANCE OF PORTFOLIO COMPANIES

Robert Hogan, President & CEO of Hogan Assessment Systems and Rob Kaiser, President of Kaiser Leadership Solutions

Robert Hogan

Rob Kaiser

Dr. Hogan is an international authority on personality assessment, leadership, and organizational effectiveness. His theory-based work in personality measurement has contributed to the development of Socioanalytic Theory, which maintains that the core of personality is based on evolutionary adaptations. He is widely credited with demonstrating how personality factors influence organizational effectiveness in a variety of areas, ranging from organizational climate and leadership to selection and effective team performance.

Rob Kaiser is an advisor, author, and internationally-recognized authority on leadership. He began his career at the Center for Creative Leadership and then joined the executive development firm, Kaplan DeVries Inc., to help shape the practice that came to be known as executive coaching.

In the final analysis, business is about money and people. By definition, successful private equity firms understand finance, but on average they tend to be less sophisticated about people issues. This makes sense: deal partners and analysts are trained in finance and are good at spotting undervalued assets. But savvy private equity players also understand that reviving an underperforming business depends to a large degree on people issues—in particular, it depends on the leadership of the portfolio company and its working relationship with new ownership.

Considerable evidence suggests that PE firms could do a better job evaluating the ability of the leadership team in their acquired companies. A recent survey by Alix Partners found that nearly three-quarters of portfolio company CEOs are removed during the investment life cycle. Over half are replaced in the first two years; but only 15% are replaced at the outset. These data suggest that, for 4 out of the 5 replaced CEOs, the decision takes too long, thereby delaying strategic milestones and prolonging the hold time.

PE firms can more quickly realize returns on their investments if they analyze the leadership of the companies they acquire with the same rigor that they analyze the business fundamentals during the diligence phase. The good news is that there is a science to analyzing people and the same discipline that is used to identify untapped business value can be used to evaluate the leadership potential of CEO candidates.

Barking up the Wrong Tree

In our experience working with PE firms, the conventional wisdom regarding what to look for in portfolio company CEOs can be misleading. People assume that brains and experience are crucial. But it turns out that IQ and prior industry and CEO experience do not predict the ability to lead through a profitable exit. For instance, a recent survey of managing partners at 32 PE firms (including Blackstone, KKR, and Carlyle) revealed that experience as a CEO in a publicly traded firm does not prepare people for success in the intense PE environment. The data also showed prior industry experience predicts the tendency to run the same playbook rather than driving radical change typically required.

The experience factors associated with successful leadership of a portfolio company include having worked in a PE environment and having previously performed a similar transformation. This doesn't necessarily mean having been a portfolio company CEO before; having held a big job in a PE environment is enough to appreciate the pace, the sense of urgency, and the need to be in close communication with ownership about everything from strategic direction to performance details. And a track record of having performed the same task successfully—whether that be cutting costs, growing revenues, managing debt, raising capital, going digital, expanding channels, or what have you—bodes well for doing it again and quickly.

Soft Skills Make the Difference

Beyond PE experience and task experience, the factors that best predict the ability of CEOs to lead to a successful exit are found more on the soft side than the hard side. And this is where it can be challenging for financial experts: understanding people is different from understanding balance sheets. However, people differ in certain regular

and quantifiable ways and research has shown which differences make a difference when leading a portfolio company. They fall into two general categories.

The first category contains the personal factors common to most successful PE CEOs. They include:

- The ability to build and lead a high-performing team with complementary strengths
- A tough-minded temperament with a sense of urgency
- Resilience—the ability to recover from the inevitable setbacks
- The willingness to admit problems and face difficult realities without spinning or sugarcoating them

PE environments usually have limited resources, which points to the need for versatile chiefs with a broad range of expertise and skills. But versatility is a rare commodity. Less than 10 percent of senior leaders are able to consult with their staff in decision making while still being able to act acting decisively, or pay attention to the big picture while also attending to the day-to-day details. Successful portfolio CEOs need to be able to recognize their limitations and staff accordingly; they also need humility in order to turn their staff loose. It's a complex set of capabilities, which accounts for the staggering number of CEOs who are replaced.

The second category of differences concerns the chemistry between the CEO and PE ownership. The big issue concerns compatibility: can the CEO and primary deal partner agree on performance expectations, communication cadence and content, and other, often unspoken, rules of engagement? This is about far more than "liking" each other; it more about mutual respect and trust. Establishing a short-hand vocabulary, sharing values, and minimizing surprises is very important in a fast-paced, pressure-cooker environment.

The Science of Personality

Many people tend to think that personality tests are on-line questionnaires or magazine quizzes designed to tell them about their "type," "color," or the house at the Hogwarts School of Witchcraft and Wizardry into which they would best fit. However, there is a science of personality assessment based on research going back over 100 years. It isn't rocket science, it's behavioral science—and it leads to solid, dependable results.

"PE firms can more quickly realize returns on their investments if they analyze the leadership of the companies they acquire with the same rigor that they analyze the business fundamentals during the diligence phase."

The evidence is clear that personality assessment powerfully predicts real life behavior; hundreds of studies with hundreds of thousands of working adults show that competently constructed personality measures predict performance with surprising accuracy. Properly validated personality measures predict job performance, career success, and leadership better than any known alternative, including IQ. Personality is stronger than Viagra: the correlation between personality and leadership is stronger than the correlation between Viagra use and improved sexual functioning.

Moreover, well-designed personality assessments can forecast an individual's ability to build a team, make tough calls, handle pressure, and be candid, flexible, and humble. Being able to penetrate the veil of self-presentation is important because sitting CEOs are likely to be on their best behavior during the courtship phase of an acquisition. There is a big difference between people at their best—what we call "the bright side" of personality —and people under sustained pressure when you see their "dark side"—the behavioral tendencies that derail teams and careers. For example, over time confidence can turn into arrogance, collaboration morphs into appeasement, and passion and a sense of urgency turn into erratic tantrums. Personality testing is especially useful when evaluating possible replacement candidates, because you will often have little direct exposure to the person yourself and smart people can conceal their dark sides for short periods of time.

Personality testing is also effective at determining the compatibility between people. It's the basic theory and measurement system behind successful online dating platforms, and it can also be applied effectively to working relationships. In addition to predicting how well two peoples' interpersonal, thinking, and communication styles will mesh, personality assessment can also predict how people are likely to rub each other the wrong way and push each other's hot buttons. Perhaps most importantly, a comprehensive personality assessment that includes core values can identify whether people are aligned in what they really want—versus likely to be working at cross purposes. In a PE context, for example, it is vital that the CEO and the primary deal partner agree about core values—i.e., about the relative importance of money, status, fame, relationships, and pleasure.

Managing Risk on the People Side

Assessing the personalities of CEOs and their leadership teams should be a routine part of doing diligence on a potential acquisition company. On the one hand, evaluations of the leaders' work histories can indicate whether they understand the pressures of PE environments and if they know how to execute the sorts of changes needed to realize value. This tells you whether people can do the job on paper. Similarly, personality assessment will provide a sense of what it would be like to work with them—how they will do the job once in office, what it will be like to have them in your life.

It is interesting to note that most failures of leadership are less about a deficiency in what they know and more about how they prioritize time, focus attention, and interact with key people. And the most important interaction of all is between the CEO and the primary deal partner; with so much at stake, it's best to understand how this relationship will work at the start, including how it could go wrong and how to manage it when things get tense.

TALENT CHALLENGES FACING SMALLER MID-MARKET PE PORTFOLIO COMPANIES

Keith Giarman, Managing Partner Private Equity at DHR International

Keith Giarman serves as managing partner of the private equity practice at DHR International. He is based in the firm's San Francisco and New York offices. He is also part of the firm's advanced technology, financial services, board & CEO, and financial officer practice groups. For more than 10 years, Keith has been overseeing board, C-suite and senior level search assignments working with management teams and investors where the mantra is rapid and long-term enterprise value creation. He has also been instrumental in the build-out of principal investing teams. Prior to DHR, Keith built the CEO practice for one of the premiere boutique executive recruiting firms in Silicon Valley serving the venture capital community.

Driving differentiated returns in a crowded private equity environment was never easy and has become significantly more difficult over time. Firms are paying top dollar to source and acquire companies in a market flooded with capital. Fewer deals are "locked up" in a proprietary manner. The areas where firms have true leverage to create value are short and long-term operating improvements.

Research from consulting firms like Bain & Company and others confirm that early "activism" on the part of the PE firm and a more systematic approach working with management yields better returns than more passive strategies. Everyone agrees that it is critical to have a well-defined value creation plan before executing a transaction and monitoring portfolio companies carefully and consistently throughout the lifecycle of the investment.

The Issue:

Businesses with ambitious plans often face a wide range of talent and organization issues.

WHAT CAN GO WRONG

Clarity & Alignment	■ Leadership doesn't set clear **priorities** or **communicate** vision and value creation initiatives throughout entire organization ■ Leadership team is **not aligned** on priorities—where to go and how to get there
Roles & Structure	■ **Accountabilities** are not clarified for the most critical decisions ■ Critical **interfaces** don't work together effectively ■ **Structure** gets in the way of delivering an effective value creation plan
Processes & Information	■ Key growth initiatives are **not resourced** to succeed—bench depth issue ■ **Bureacracy** gets in the way of growth
People & Performance	■ Value creation plan lacks the right talent or **leaders** (skill or will) ■ Insufficient **talent pipeline/capabilities** to sustain growth ambition ■ **Incentives** don't reinforce value drivers in most critical initiatives
Leadership & Culture	■ Inability to transition the top team to a **PE mindset,** required to balance big-picture thinking with hands-on style ■ The organization is not sold or **not excited** by the value creation plan
Results Delivery®/ Ability to Make Things Happen	■ Management **dashboards** don't provide visibility into key value creation drivers to **push and follow through** results achieved ■ Incomplete appreciation of company's **inability to manage the change**

"Results Delivery®" is a registered trademark of Bain & Company, Inc.

With the above in mind, PE firms that specialize in lower mid-market transactions (sub-$100 million in revenue) have an added challenge. Attracting top talent that can function effectively in these smaller environments is not a trivial exercise. Smaller companies do not have the cost structure to support an army of staff and they have often been starved in one or more areas in terms of professionalized functions like finance, HR and sales. A decade ago, some thought executives coming from larger and more complex environments might naturally be able to manage smaller and supposedly not-so-complex environments. It seems safe to say that the latter has been disproved over time. It is impossible to ensure a new CEO or CFO will be successful unless one carefully considers their functional, technical and leadership competencies with a focus on their management/communication style and what behavior they exhibit that may or may not be suitable for a given culture in a smaller company.

Key Issues to Consider

Dearth of PE-Proven Talent – One way to minimize risk is to recruit executives with direct and successful experience working in a relevant PE funded environment. Unfortunately, there are only so many in the market at any given time and the pool of talent suitable for smaller companies may even be smaller and harder to access. It is critical to create a big enough pool to ensure the candidates can align with the culture and critical success factors facing the business. Entertaining executives who might commute is one way to open up the pool, but the decision to allow that is situational – highly dependent on the state of affairs at the company, the make-up and quality of the team and the extent of effort required tied to investment phase.

Source the Right Candidates – In order to broaden the pool of talent, it is important to find executives with AND without PE experience. Certain companies tend to cultivate P&L leaders that often are much better prepared to step into P&L as well as CFO roles. These companies are often decentralized where unit executives really own the P&L. A classic example of this is Danaher which, importantly, uses their own proven system of value creation – the so-called Danaher "business system. Executives coming from highly matrixed environments like GE, UTC and many others can struggle in smaller environments unless they have stepped out and already proven themselves in a smaller environment (or overseas or more entrepreneurial venture in some cases).

Geographic Considerations – When sourcing in tough-to-recruit areas, it is critical to have a clear search strategy on where to hunt for talent. A top executive from a company in Manhattan is unlikely to be the best fit for a company in Wichita, KS (and vice a versa) from a cultural standpoint. That said, there are executives who have grown up in or attended college in the Midwest, as an example. Perhaps they grew up on a farm in Michigan, went to school at Ohio State, and are now running a smaller company in New York. There is a much better chance someone like this will be more suitable to the culture of a Midwest company and can be recruited into a geography that once was home. Search firm partners and their staff must have experience running searches with these challenges in mind and qualify candidates early and often to be sure they are truly engaged.

Competitive Compensation – Irrespective of geography, smaller PE funded companies have a lower cost structure and that translates to reduced overall cash compensation at an executive level. Candidates for key roles must be convinced there is a compelling upside opportunity relative to the equity component of the compensation and a good career path. This means the recruiting firm, hiring manager and PE firm need to work closely on strategy to educate candidates. Before embarking on the search, all should agree on the "talking points" and materials (beyond a specification) that illustrate the magnitude of the opportunity. No matter how compelling the upside is, there is no reason to waste time on candidates that will not embrace the opportunity given certain cash requirements. Again, it is critical that the search firm qualify early and often and move on if candidates cannot accept cash compensation parameters.

"A decade ago, some thought executives coming from larger and more complex environments might naturally be able to manage smaller and supposedly not-so-complex environments. It seems safe to say that the latter has been disproved over time."

PE Firm Brand Awareness – Sometimes, it is not enough to educate the candidates on the business opportunity ahead; they need to learn more about the PE firm itself. Most executives have heard of Blackstone, but the same cannot be said of many smaller funds in the mid-market space that often, by design, operate with a low profile that aligns with their target portfolio companies. The team working the search must emphasize the value of the firm that will become their partner, both in terms of their successful track record and partnering style working with management.

Fly High and Fly Low – Executives stepping into smaller environments need to "fly high and fly low" AND be excited about this aspect of their role. With a well-crafted value creation plan in hand, laser-focused execution and a metric-oriented culture of accountability are critical. When something breaks, C-level executives need to problem solve with their team until course corrections are determined. They need to relish the opportunity to walk the factory floor, know every employee's name and work hand-in-glove with field personnel as they interact with customers. A CFO of a small company who has no interest in running his own numbers on a spreadsheet from time-to-time or writing some query code for the ERP to extract data may not be suitable. The

right executives think like an owner of the business, are "hands-on" and value building a lean operation.

The Founder Led Small Business – Related to the above, it is often the case that PE firms are acquiring companies led by a founder that may be great at conserving cash but not versed in surgical capital allocation with a new capital structure focused on growth and transformation. Smaller companies typically need to be professionalized quickly – systems, processes and people. Small companies cannot just "save their way to success." They must transform with better execution focused on current products in current markets, new products in current products, new products in new markets, M&A, etc. Not every executive, no matter how good they look on paper, is wired for this type of role.

All PE funded companies are struggling to find the right talent, but the challenge is particularly pronounced in smaller mid-market entities. Several things can be done to reel in the right talent. Develop a search strategy where a broader pool is part of the process. Make sure all parties are clear on how best to educate candidates on the value of the opportunity and working style of the PE firm. A strong equity upside position to get candidates to engage is a must. And, most importantly, be sure you are working with a firm that has a proven process to assess this talent carefully for a hands-on working style that will match the culture. Thoughtful collaboration amongst the PE firm, management team and the search firm is the key to a successful outcome.

BUILDING AND ACTIVATING CHAMPIONSHIP TEAMS

Jill Hill, Ph.D., Head of Private Equity (Americas) and Isabella Roger, Ph.D., Senior Consultant, Private Equity at YSC Consulting

Jill Hill

Isabella Roger

Jill Hill, Ph.D. leads YSC Consulting's Private Equity Practice for the Americas, advising many of the world's leading global PE firms on their toughest leadership and talent challenges. Jill is a strategic partner who specializes in providing management due diligence, senior executive assessment, coaching, board effectiveness, and high-performance team development to investors, Boards, CEOs, and portfolio company management teams.

Isabella Roger, Ph.D. specializes in helping Private Equity firms and portfolio management teams achieve results by aligning and developing the leadership, talent and organizational variables required to deliver the investment thesis. Isabella brings expertise in Executive Leadership Assessment, Leadership Development, CEO Succession Planning, High-Potential Development, High Performing Team Development, 360 Feedback Surveys, Organizational Design, and Organizational Culture.

Closing a new deal is an exhilarating moment, one marked by excitement and anticipation. It is also the best time to start investing in the leaders and talent who will play a pivotal role in the overall success of the investment. In our experience, the number one priority post-close is supporting and activating the management team. While it can be tempting to dive straight into operational opportunities, we argue that the larger opportunity for improving organizational effectiveness and accelerating performance in the long run is ensuring that the top team operates as a championship team.

While there is no scarcity of motivated management teams, there are several key factors that distinguish championship teams from other groups of talented leaders. Most importantly, championship teams are fully aligned and deeply aware of the mix of skills and capabilities across the team. These teams play to their strengths and mitigate their risk areas. They also regularly monitor and re-evaluate their team principles and group dynamics to ensure that trust, communication and focus remain strong.

With these pillars in place, management teams generate exponential impact in terms of leading their organizations and rallying employees around a clear strategic vision. They are also better positioned to maintain a strong read on the true state of the organization because they are not spending their time putting out fires at the top.

Clear Benefits

The benefits of activating championship teams are plentiful and clear. How exactly to evaluate teams and accomplish this, however, is an area where many savvy investors rightly seek some additional external support. Working in partnership with PE firms, CEOs and management teams, YSC's PE consultants help answer the most pressing and challenging talent questions:

- Is this group of leaders functioning as a high performing team?
- Are they aligned on the strategy?
- Will they relentlessly drive to deliver excellence?
- How will each leader contribute to the company's new chapter of change and growth?
- What support does the team need to accelerate optimal performance?

Our rigorous, data-driven approach integrates techniques and best practices from organizational behavior, clinical psychology, and management studies. We begin by focusing on the strategic context. To know where the company is going, we spend time with deal partners and

portfolio executives to understand the current state and the features of the desired future state in terms of leadership, team and cultural characteristics.

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Driving Performance

Building and supporting a championship management team that can deliver the anticipated results begins with a thorough evaluation of the company's existing strategic goals as well as the PE firm's investment thesis. From here, the key strengths and leadership skills required to drive these strategic goals are identified, and a structured approach to enhancing these skills at the top of the organization can be launched.

In our view, activating the team starts with gaining in-depth insight into each of the team members as individuals and as leaders. To attain this goal, we incorporate advanced psychometrics and behavioral interviewing to gain a deep understanding of each leader in a short period of time. Layering on team effectiveness analyses, we develop a clear view of the team's dynamics and opportunity areas. These insights provide the foundation that allows us to recommend targeted, high impact individual and team development actions proven to drive successful performance.

As relationship-oriented leadership experts, our genuine developmental lens significantly differentiates our approach in the marketplace. We work exceptionally hard to support and partner with management teams; our processes reflect a done with approach rather than one that is done to. Trust, open communication and a transparent partnership are keys to unlocking the insights that will actually move the needle.