Dispelling Common CEO Myths: **Six Lessons for Private Equity Leaders and Portfolio Company CEOs**

Table of Contents

- **Methodology and Acknowledgements** p 3
- **Framing the Issue** p 4
- **Six Flawed Assumptions and the Lessons They Reveal** p 4
  - Once you've seen one PE firm, you've seen them all p 5
  - A win is a win p 6
  - Active investor involvement = I'm failing p 7
  - Existing team = acceptable team p 7
  - It's essential to get a few quick wins to prove your worth, then you can focus on the long term p 8
  - Don't challenge your investors until you've built a solid relationship with them p 9
- **Conclusion: Build the Relationship Before You Build the Business** p 9
- **About Russell Reynolds Associates and Green Peak Partners** p 10

Origin of the Study

In our work with clients, Russell Reynolds Associates and Green Peak Partners have each devoted significant attention to identifying the qualities that differentiate the strongest portfolio company CEOs from ordinary ones. Over the years, we have observed the towering importance of the strength of the relationship between CEOs and their PE sponsor(s) – yet we also noted the lack of published guidance on how to handle this critical dynamic. While our firms compete in some areas, we have great respect for each other – and realized that we might better address this gap by tackling the topic together.

What you see is the product of a close partnership between Green Peak and Russell Reynolds. We hope that you find the content insightful and applicable.

Methodology and Acknowledgements

To develop our six recommendations, Green Peak and Russell Reynolds Associates went directly to the investors and CEOs who are engaged in the operations of private equity portfolio companies on a daily basis. Our consultants conducted in-depth interviews with 25 leaders at premier private equity firms in Europe and the US, as well as with 15 current or former portfolio company CEOs, gathering both qualitative and quantitative data. We augmented this firsthand perspective with secondary research on the topic, emphasizing the identification of proven tactics that would be applicable across a range of organizations.

This project would not have been possible without the remarkable generosity of these 40 executives, and we are grateful for their time and insights. Their incisive observations about both successes and failure offer a unique window into a world that is often largely inaccessible to outsiders.

A special thanks to the following private equity leaders, who were among those we interviewed.

Graham Weaver
Founder and CEO
Alpine Investors

Steven Dyson
Partner
Apax Partners

Andrew Sillitoe
Partner and Co-CEO
Apax Partners

Geoffrey Rehnert
Co-CEO
Audax Group

Josh Klinefelter
Managing Partner
Aurora Capital Partners

John Connaughton
Co-Managing Partner
Bain Capital

Ross Jones
Managing Director
Berkshire Partners

Steve Moore
Partner
Brentwood Associates

Brooke Coburn
Deputy CIO and COO, Real Assets
The Carlyle Group

Maxim Crewe
Partner
Cinven

Dipanjan (DJ) Deb
Co-Founder and CEO
Francisco Partners

Jon Ralph
President, Chief Operating Officer and Partner
Freeman Spogli

Bill Ford
CEO
General Atlantic

John Bernstein
Partner
Generation Investment Management

Philip Hammarskjold
Co-CEO
Hellman & Friedman

Tim Franks
Member, Private Equity & Head of Consumer & Retail, EMEA
KKR

Timothy Flynn
Partner
Leonard Green & Partners

Matt Wilson
Managing Director and Co-Portfolio Manager
Oaktree Capital

Paul Salem
Senior Managing Director Emeritus
Providence Equity Partners

Mark Gillett
Managing Director and Head of Value Creation
Silver Lake Partners

Brian Conway
Chairman and Managing Partner
TA Associates

Daniel Zilberman
Managing Director and Head of Europe
Warburg Pincus

Anthony de Nicola
President and Managing Partner
WCAS

Aside from those specifically quoted in the study, CEO interviewees have been kept anonymous in order to ensure that they would feel comfortable in openly sharing lessons learned from their work with PE sponsors.

Framing the Issue

Many executives think they've made it once they are hired to be CEO for a private equity–owned company. About half of them, it turns out, are wrong. An analysis of portfolio company leadership by consulting firm Bain & Company found that just under 50 percent of CEOs were ultimately replaced by the PE firm—an outcome that the majority of those owners hadn't anticipated when the relationship began.[1]

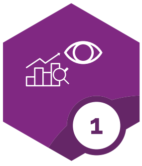
Succeeding as a portfolio company CEO means more than bringing traditional general management experience and skills or producing impressive statistics around sales growth or expense reductions. Instead, it means fully understanding and embracing the perspective of the PE investors—but then forging your own path to success.

To help CEOs understand how to start and stay strong in a PE-backed company, Green Peak Partners and Russell Reynolds Associates recently interviewed 25 leaders at premier private equity firms as well as 15 current or former portfolio company CEOs whom those investors identified as being among their most successful. As a group, these CEOs have been associated with close to $7 billion in disclosed PE investments, according to PitchBook, and more than $5.2 billion in transaction values for those who have seen their companies through exits.

From these interviews, we have distilled what top-performing CEOs do to both engage effectively with their PE sponsors and succeed in the market. And since the avoidance of pain is often a stronger motivation than the pursuit of pleasure, we offer a what-not-to-do list in the form of six common yet flawed assumptions that often blindside incoming CEOs.

Six Common Myths About Working with a Private Equity Firm

[1] http://www.bain.com/Images/Bain_report_Global_Private_equity_report_2015.pdf, 56.



Flawed Assumption #1: Once you've seen one PE firm, you've seen them all

Many of us start with cartoonish stereotypes of PE investors: They're sharks, they have sharp elbows, they're control freaks. But unless you move beyond these assumptions, you're destined to fail. In reality, once the deal is sealed, PE firms take extremely different approaches to their portfolio companies.

Every PE firm has its preferred recipe for engaging with portfolio company executives, with the level of involvement varying based on a firm's investment philosophy and available resources. In some cases, CEOs told us their PE firm was fairly hands-off or would get involved in just one aspect of the company. In others, the firm was heavily involved in everything from sales strategy to employee benefits offerings. In the middle of all this, depending upon the sponsor, the PE firm's playbook may be considered either as a religious text or simply a compendium of suggestions.

Then there's the need to decode standard PE vocabulary words that carry anything but standard definitions. All firms, for example, will ask their CEOs to operate with a sense of urgency, provide detailed updates and communicate frequently—but what that means in actual terms can range widely. One PE investor we spoke with defines frequent communication as speaking with his CEOs three or four times a week, another is satisfied with once-a-week calls. Operating with urgency means the CEO is up and running within three months for a managing director at one firm; his peer at a different firm allows for a year or even 18 months.

The variations across PE firms are substantial, but with the right mindset and careful attention, new CEOs should ultimately be able to unearth them. What's surprisingly more important and even trickier to discern, however, is the variance *within* firms. As many CEOs have told us, the personal motivations of the people on the deal team—where they are in their careers, how their financial incentives are structured and how their other portfolio companies are doing—can deeply influence the decisions they make about your company. "I used to think I was running the business exclusively to generate enterprise value, but that is not always the case," one successful PE portfolio company CEO told us. Investors "have agendas, careers and livelihoods at stake, with a massive amount of money involved. Understanding this is important for the CEO to be successful." A deal team professional who needs a win to secure a promotion may be motivated to sell your company sooner, for example, while one without this urgency may be open to a longer holding time.

And while conventional wisdom says senior partners are easier for CEOs to work with, it's not always that simple. Junior members may be more cautious under the pressure to deliver consistent results—or they may be more willing to take risks for larger rewards. Senior members with more political capital may offer a CEO more latitude—or they may become more risk-averse as they near retirement.

The upshot is that the specific people in the room can often matter more than the firm that employs you. This is a lesson that Randy Dobbs discovered early in his stint as CEO of US Investigations Services while it was owned by PE firm Welsh, Carson, Anderson & Stowe. After four months on the job, he told his investors that USIS needed to increase its wages, hire more people and invest in better logistics to make the firm competitive—moves which would subtract an alarming $14 million from profits in the short term. His board initially pushed back and asked for more details, wanting to engage on the underlying assessment of the issues as well as the recommended (costly) solutions. The third time through his pitch, however, one of the PE firm's leaders was listening. This immediately changed the conversation. The PE leader said, "We spent six months hiring this guy. He told us the three things he needs to do to drive results. If we say no, we might as well let him go," Dobbs recalled. "It was a great reaction" from a partner with significant power. The firm leader was able to pull out of the details, reorient the board around the higher-level questions and provide Dobbs the runway to make changes to the company, which ultimately repositioned the company for success.

Portfolio company CEOs will not always have the luxury of a leading partner on their boards, but one step they can take in any circumstance is to drill deeply into the unique styles and motivations of each individual member of the team to understand how best to work with them. Among the information we advise CEOs to glean from their deal and/or operating team: Where is the firm in the fund lifecycle? Who will be involved in the day to day? Where does decision-making authority

lie? Is the firm's playbook gospel or guidance? How are team members compensated? Where is each person in the pecking order, and how many deals and exits have they had? What other external pressures are team members facing that might affect their work on your company? Armed with that information, CEOs must then manage those motivations.

Flawed Assumption #2: A win is a win

CEOs who fail often have crisp definitions of success in their minds—they just don't happen to be the same definitions used by their investors. The best CEOs quickly discern exactly what a prize-winning exit looks like in their investors' eyes, in effect defining the terms of the divorce—or exit/sale—at the very outset of the relationship. But they also get a full understanding of the past: what's gone wrong at the company, where the PE firm sees value and what drew them to the deal in the first place.

Managing directors at several top PE firms told us that it's all too common for CEOs to charge ahead without gathering all the facts. "You'd be amazed by the number of CEOs who don't ask for our work on the deal. It would be the first thing I would ask for," said John Connaughton, co-managing partner of Bain Capital. "If I think about failure modes, one of the biggest for any senior executive is not understanding or not having shared understanding around the plan that is being delivered," said Mark Gillett, managing director and head of value creation at Silver Lake Partners. "There are lots of examples of executives thinking they are doing a great job, but it isn't the plan the sponsor underwrote."

This was readily apparent to investors at The Carlyle Group when they bought a company that had previously been owned by three other PE firms. "The way we worked and our objectives were very different from the previous owners," recalled Brooke Coburn, deputy CIO and COO, real assets, for Carlyle. Unlike past investors, who aimed to cut costs in order to boost profits, Carlyle saw the company as a promising platform with international growth potential that was suffering from underinvestment. Instead of trimming spending, Coburn's team wanted to launch new products and triple the sales growth rate. "That was a really big change and hard for our CEO, who had been living in an austere environment," said Coburn.

In some cases, the PE firm has a process to establish a shared view of success, such as a strategy off-site scheduled soon after the transaction closes. "We are extremely focused on partnership with incumbent management. We have a teach-in with every new CEO and we take them through our investment thesis, risks, growth levers and how to build the business," said Josh Klinefelter, a managing partner at Aurora Capital. That often includes bringing in outside consultants who have analyzed the company for a fuller perspective. "We give them everything we know. Our most successful CEOs eat it up and challenge us." Klinefelter credits these upfront sessions and the firm's partnership orientation with minimizing the number of CEOs replaced for underperformance.

At other firms, the emphasis is on creating a detailed picture of an ideal exit. In 2016, founder Mark Friedman saw his PE-backed company, real estate and facilities management firm Accruent LLC, through a successful sale to Genstar Capital. Part of what made it go smoothly was that he and his investors created a mock banker book for the exit immediately after the initial PE investors, Vista Equity Partners, took on additional investment from a second PE firm, TA Associates, in 2013. "Right after we closed the TA deal, we created the banker book for what the company was going to look like when we sold it the next time," said Friedman. The goal was to "sit down as a team and, in high definition, envision what the company is going to look like in a few years, in terms of leadership, metrics, products, customers, geographies." Getting to that level of clarity and shared understanding informed the operating plan for next three years and later led to Genstar's interest in buying the company. (Accruent was recently acquired by publicly-traded Fortive Corp. for approximately $2 billion.)

Some firms not only lay out the history and the PE firm's hopes in early meetings but also force alignment with the CEO on key growth strategies. Within the first 100 days of his investments, Alpine Investors founder and CEO Graham Weaver has new CEOs brainstorm with their boards to write the hypothetical front-page *Wall Street Journal* article they hope to see about their company within three years. A substantial return is assumed; the question the group must tackle in a short space is: How? Which client wins, product innovations, acquisitions or market expansions led to that success? And what does that future story mean for the company's strategy over the life of the

investment? Surprisingly, as important as the visioning is the distillation of the key priorities to only three or four from most companies' starting list of ten or twelve.

Whatever the process, CEOs need to ensure they have a granular understanding of (1) what investors think went wrong at the company originally, (2) what drew the PE firm to this investment, (3) what they expect to achieve and (4) how they plan to make it happen. If your firm doesn't proactively offer a high-definition picture of success, make sure you ask for it and push to clarify it. "The best first-time CEOs will have done their homework in advance," said Coburn, surfacing past problems, which metrics matter most now and what the firm expects to happen at the one-, two- and three-year marks.

Flawed Assumption #3: Active investor involvement = I'm failing

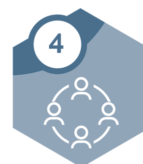
One of the biggest surprises to first-time PE-backed CEOs is how often their investors want to communicate with them and how hands-on they will be in daily operations. For senior executives coming from just about any other environment, this level of involvement may be unnerving. "A new CEO may misperceive active involvement as a vote of low confidence, but we see it as a positive opportunity to support the leader's growth plan by applying our organizational capabilities and leveraging our experiences in similar situations," said Bill Ford, CEO of growth equity firm General Atlantic. And while it is natural to resist asking for outside help, this is not what investors want from you. Ford says one of his pet peeves is CEOs not sharing bad news quickly enough because "if we don't know about a problem then we can't help, and often we do have resources and ideas that actually can help – and we want to."

In situations where CEOs fail, it's often the case that "if there are any speed bumps, the CEO becomes closed and defensive," and the sponsor then becomes "prosecutorial," said Silver Lake's Gillett. In an ideal world, "a great CEO is open to listening to the perspective of 10 smart PE investors, and a great deal team is open to encouraging a candid partnership, recognizing operational reality." Then, when problems occur, "the CEO shares them and the sponsor leans in as a partner to help find solutions."

While this is a difficult dynamic to achieve, successful CEOs almost unanimously echo the sentiments of PE investors, often speaking of their PE firms with great admiration. When Accruent founder and then-CEO Friedman accepted investment from Vista, for example, he knew it would be an extremely hands-on partnership. The Vista team expected faithful execution of its playbook and was deeply involved in nearly every aspect of the business, down to when specific deals would close and how to structure commissions for sales reps. "They were just on top of every detail of how the company was running—people, products, processes. They were everywhere," said Friedman.

While Friedman admits that the level of involvement could have been oppressive with the wrong PE sponsor, he believes Vista's involvement made him a better CEO. When PE investors "are giving the right advice and your ego doesn't get in the way, it is awesome. You have teaching, direction and coaching," said Friedman. He soon came to realize that "the playbook wasn't just based on the ideas of some PE guys who went to fancy schools and had never run a company; it was a collection of best practices over 15 years from their CEOs who were really successful." As a result, he said, he learned more in his first two years with Vista than in his previous 19 years as a CEO.

The primary challenge for a CEO is to ensure the firm you sign on with is one you can learn from and partner with effectively. From there, it's opening yourself up to outside help without letting it erode self-confidence—even when it means sharing bad or embarrassing news before you have a solution in hand. What not to do is to make it your mission to prove you don't need help from your investors or to hide until you have things all figured out.



Flawed Assumption #4: Existing team = acceptable team

In hindsight, nearly all new CEOs wish they had made changes to their senior teams sooner. While PE-backed CEOs have a certain advantage over public company CEOs in that their team moves don't have stock price repercussions, they also face the time pressure that comes with a fixed investment horizon. "Our goal is to support a company's growth and we believe it's best to get in front of potential issues or changes sooner rather than later," said Ford of General Atlantic. "If we address management gaps early, we can often change the trajectory of a business to the positive. If we wait two and a half years, we are in trouble."

Not surprisingly, when we asked investors and CEOs about the most important actions for new CEOs to take within their first six months, assessing and upgrading the executive team was by far the most popular answer. A full 97 percent of respondents cited it as a priority, putting it ahead of operationalizing the strategy and communicating the vision, among others.

Some caution is advisable, of course. Making changes simply to check boxes will not win any points with PE investors, and a CEO can quickly lose credibility if the replacements turn out to be B players. But, in nearly all cases, replacing the necessary direct reports sooner rather than later typically yields better results. And by sooner, we mean assessing the team and initiating the relevant searches within just three months (versus the typical twelve to eighteen months).

One motivation to move quickly is to capitalize on the fresh perspective a new CEO brings, as familiarity often clouds the picture. One talented CEO we worked with considered difficult people decisions one of his strengths and replaced the vast majority of the senior team soon after joining a PE-backed firm. But when Green Peak conducted a review three years later, he realized he wasn't holding the new members of his team to high enough standards. As he had gotten to know people better, he had developed blind spots about their weaknesses. Ultimately, he let go an additional two people as a result of this external feedback.

In other cases, the argument for replacing people is as simple as the need for new people to match a new culture. "It is all about the impact and speed of change," said Bain Capital's Connaughton. With his firm's standard (and ambitious) goals to accelerate revenue growth by up to 10 percent and double profits, his belief is that existing management teams are often unlikely to be able to quicken their pace fast enough. "You often need new executives and capabilities to create discontinuous change and achieve the vision and strategy of new ownership."

As with so many other issues, your PE firm may or may not have a strong point of view on how quickly and how fully you should replace your team and whether or not it will be involved (many firms will assist in the hiring process for key roles, particularly the CFO). It's important to clarify perspectives early on, but keep in mind that even if the firm would allow a slower pace, you will be better off making quicker decisions.

Flawed Assumption #5: It's essential to get a few quick wins to prove your worth, then you can focus on the long term

CEOs can be forgiven for orienting themselves toward quick wins, especially those who come from public company environments where investors expect to see meaningful progress every quarter. PE investors still hold out the 100-day mark as an important milestone, and even without external pressures, many CEOs feel the need to gain credibility with tangible early results.

However, despite popular business literature to the contrary, an obsession with quick wins is a good impulse to squelch, particularly in PE. Private equity investors tend to look at progress in much longer chunks of time and won't appreciate short-term gains that come at the expense of their total return. "People will want to develop 100 days of rapid action—'new sheriff in town' stuff. Close that office, discontinue that product line," said Silver Lake's Gillett. "But over the course of the whole investment or a CEO's tenure, they probably aren't the most material ... and can get in the way of getting the big things right." In fact, when we asked investors and CEOs about the most important actions for a CEO to take within the first six months, identifying and accomplishing quick wins came in ninth on a list of 10 potential priorities, with only 38 percent of people agreeing that it was a priority at all.

The nuance of time horizons was one of the most surprising elements of becoming a PE-backed CEO, USIS's Dobbs recalled. As a former public company executive, when the company missed its numbers in his first quarter, he went to the board meeting armed for battle. "I went in focused on where we were, why we were missing and what we were going to do," he said. Afterward, the lead managing director from Welsh Carson gave him high marks for effort, but also a key lesson. "He said, 'Understand one thing: Quarter to quarter, this isn't a big public company.'" While the PE firm wanted to see continued progress toward long-term goals, they told him "we are not going to beat you up about not making a quarter—our objective is the return on the business in three to four years," Dobbs recounted.

The 100-day milestone is real, there's no question. But CEOs can improve their odds of impressing PE investors if they realize that they're not being measured

on what they've done in that time; they're being measured on how well they're choosing what to do over the next three to five years and setting a clear path of actions and results. Many of the investors we spoke with noted how important it was for the CEO to focus on a short list of meaningful goals, even when it meant slow progress initially. "Pick two or three things that we are going to crush and do really well and get rid of everything else," said Weaver of Alpine Investors. "The magic is picking the right two or three because that is how you really build the confidence of the team. If you pick too many, you have the opposite effect."

Quick wins are not bad in and of themselves. The problem is when they distract from more meaningful goals. While human nature is drawn to the dopamine rush of box checking, CEOs in a PE environment particularly must avoid this temptation. As one person we spoke with said, "If you're tripping over $100 bills, pick a few up—but don't get distracted by nickels."

Flawed Assumption #6: Don't challenge your investors until you've built a solid relationship with them

Go slow, go fast; follow our playbook, be vulnerable: With the deluge of advice PE investors have for new CEOs, it's easy for new executives to default to becoming order takers. But above all else, for all the listening and nodding a good PE CEO does, he or she must also recognize that PE investors expect their CEOs to bring unique and valuable perspectives to a company.

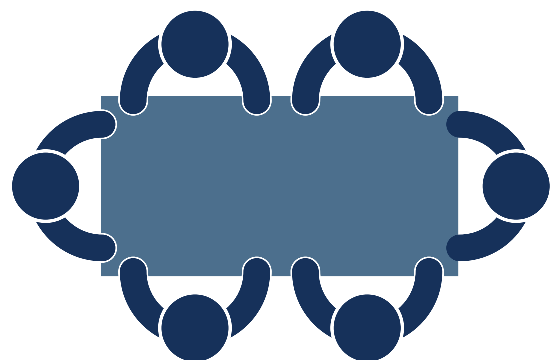
Investors are quick to discount CEOs who fail to challenge their views and contribute independent ideas. "Someone who hasn't been a CEO before, who is looking to paint by numbers and follow directions, saying, 'Tell me what to do and I'll do it' – that's a potential recipe for failure," said Brian Conway, chairman and managing partner for TA Associates. More bluntly, "One of my CEOs takes my advice only 25 percent of the time, and he is doing great," said a managing director at another well-known PE firm. Likewise, in describing one outstanding portfolio company CEO, Hellman & Friedman co-CEO Philip Hammarskjold noted that he had "a real vision of where he wanted to go, a strong roadmap for how to get there and a cadre of people from his network to join the company and get the job done. It was breathtaking to watch."

A number of successful CEOs noted that their role was often one of mitigating the allure of groupthink. "PE guys move in a herd mentality, and you sometimes need to stand up to that mentality," said Todd Davis, founder and former CEO of identity theft protection firm LifeLock. For example, when his investors threw down an edict to cut 10 percent of his employees, "I said, 'If you want me to take out 10 percent of my workforce as a blanket statement for your portfolio, then you have the wrong guy running this. I am not going to do it,'" Davis recalled. At the same time, he was willing to run with the bold idea of publicizing his own Social Security number in 2008—first on national television and then on billboards—to express his confidence in his company. He credits that move with significantly raising LifeLock's profile, contributing to its $141 million IPO in 2012 and subsequent $2.3 billion sale to Symantec in 2017.

A constructive challenger is a complex role to play, but the best CEOs are neither lapdogs nor lone wolves. They know when to acquiesce and when to trust their instincts.

Conclusion: Build the relationship before you build the business

Succeeding as a PE-backed CEO is a daunting task. In some ways, though, all of the advice we heard from PE investors and portfolio company CEOs can boil down to a simple message: Build the relationship before you build the business. Like learning the language in a foreign country, it's a foundational step that can make you or break you. Without that relationship, you're stuck pointing and gesturing, hoping your message gets through. With it, you've got exponentially more freedom to understand and explore and to build a winning business along the way.



AUTHORS

CAMILLE DELAITE, a former partner at Green Peak, is operating partner, talent, at Charlesbank Capital Partners, a private equity firm and Green Peak client. She is based in Boston.

JP FLAUM is the founder and CEO of Green Peak. He is a globally recognized author, speaker, and CEO coach. He is based in Denver.

GEORGIA RANKIN co-leads Russell Reynolds Associates' Financial Services practice in the UK and is a member of the Global Private Equity Group. She is based in London.

JEFF WARREN is a leader in Russell Reynolds Associates' Global Private Equity and Private Markets Group as well as the Financial Services Sector. He is based in Los Angeles and New York.

About Green Peak

Green Peak is a premiere leadership acceleration firm committed to 'eradicating average' at the leader, team, and organizational levels. With consultants in seven U.S. cities, we help CEOs and investors maximize their financial results and valuations throughout diligence and the deal cycle. Green Peak helps our clients optimize organizational structure and culture, assess talent for key roles, integrate acquisitions, and coach executives and teams to maximize leadership potential. Our differentiating advantage is the interconnectedness of our offerings – by maximizing structure, culture, talent, and team, we have an outsized impact on our client's ambitious trajectories, especially in demanding and fast-growing environments. Find out more at **www.greenpeakpartners.com** or contact us at **info@greenpeakpartners.com.**

About Russell Reynolds Associates

Russell Reynolds Associates is a global search and leadership advisory firm. Our 425+ consultants in 46 offices work with public, private and nonprofit organizations across all industries and regions. We help our clients build teams of transformational leaders who can meet today's challenges and anticipate the digital, economic and political trends that are reshaping the global business environment. From helping boards with their structure, culture and effectiveness to identifying, assessing and defining the best leadership for organizations, our teams bring their decades of expertise to help clients solve their most complex leadership issues.
Find out more at **www.russellreynolds.com**
Follow us on Twitter: **@RRAonLeadership**

© Copyright 2018, Russell Reynolds Associates and Green Peak Partners. All rights reserved.