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The CEO's Perspective: What Public Companies and Private Equity Can Learn from Each Other

The elements of success for a CEO can vary when comparing the contexts of private equity-owned and public companies. CEOs who have led in both public and PE-backed environments tell us that private equity is more focused on fast value creation and a successful exit, which often stands in sharp contrast to public companies, where navigating board dynamics, public shareholders and quarterly guidance is often seen as key to success when managing perception over longer durations.

However, considering today's market realities, it's not surprising that companies are looking past these differences, with private equity portfolio companies increasingly tapping public company talent pools to find new leaders — and vice versa. There are close to 23,000 private equity portfolio companies in the United States today, and according to a report by the National Bureau of Economic Research, 71 percent of portfolio companies install a new CEO at the time of purchase. Meanwhile, the overall pool of CEO candidates is shrinking, as the Baby Boomer generation retires, and as new, lucrative non-CEO opportunities open up for experienced candidates, including board positions and PE operating partner positions. All told, a shrinking talent pool under increasing demand creates an environment where companies don't have the luxury of restricting their options.

However, as we have learned in our work on hundreds of CEO searches and succession plans annually for both PE-backed and public companies, there is plenty companies can do to find and evaluate candidates who can thrive even without explicit experience in one environment or another. Our research has shown how past playbooks are less useful when facing novel, unforeseen challenges. Recognizing the differences in how to succeed in private and public settings, companies in both environments can better understand how to find leaders with the capacity to adapt and succeed.

Interviewees

- **Chris DiSantis**
  Managing Director, American Securities; former CEO, Verso Corporation, H-D Advanced Manufacturing and Latrobe Specialty Metals
- **Ann Fandozzi**
  CEO, Convergint; former CEO RB Global, Abra Auto Body & Glass and vRide
- **Eric Foss**
  Former CEO, Aramark, Pepsi Beverages Company, The Pepsi Bottling Group
- **Jacque Hinman**
  CEO, Atlas Technical Consultants; former Chair and CEO, CH2M
- **Ron Keating**
  CEO, Excelitas; former CEO, Evoqua Water Technologies and Contech
- **Larry Kingsley**
  Advisory Director, Berkshire Partners; former CEO, Pall and IDEX
- **Andy Silvernail**
  CEO, International Paper; former CEO, Madison Industries and IDEX
- **John Stroup**
  Partner, Clayton, Dubilier & Rice; former CEO, Belden Inc.

With this in mind, it's critical for both public and PE-backed companies to understand how they can assess potential CEOs with experience in a different environment. How do PE and public realms differ? What skills are transferrable? And, most importantly, what can public and PE companies learn from each other? In this piece, based on our own experience advising companies on their CEO transitions, and on several interviews we had with CEOs who had successfully led companies in both public and private environments, we look at the answers to these questions, to understand how to find a CEO who can lead and thrive.

How PE and public companies differ: "Sprint vs. marathon"

There's no doubt that the CEO experience and how success is defined differ between PE and public. Private equity firms are famously devoted to value creation and to a profitable exit over (most commonly) a five-year duration, whether by IPO, sale to a public buyer or sale to another private equity sponsor. Further, the very nature of the private equity ownership model means that PE firms are quite literally invested in their company's success, and as a result generally much more involved in strategy and operations than a public board would be.

Meanwhile, public company CEOs in general must face a greater deal of short-term scrutiny than their private equity counterparts. Quarterly statements are typically the primary focus, with boards and public shareholders demanding immediate results balanced with a long-term vision for holding their investments for longer durations. Public company CEOs find more of their time consumed with managing board director and investor relationships, and often note their operational leadership is delegated more to other C-suite leaders.

Our conversations for this article, along with our experience as leadership advisers to both private equity–sponsored and publicly owned companies, demonstrate how each model could learn lessons from the other. Following is a look at some of these lessons.

What public companies can learn from PE

Hyper-focus on value

Private equity firms are known for their laser-like focus on making moves that add value to the company in the context of the exit, whether by sale or public offering and on making that impact within a certain predetermined timeframe. This allows private equity to operate in near-to-medium-term timetables without worrying as much about quarterly setbacks. Public companies can lack that same focus on value, especially as they face pressure from boards and investors to meet quarterly results and address issues that may not directly impact the bottom line or may shift focus to more distant future trends. Public boards should find ways to help management teams spend more time in the business and to defend management teams when quarterly setbacks are needed to drive longer-term objectives.

Avoid "short-termism" that comes from quarterly results

As noted, PE firms are generally less beholden to short-term metrics, and in particular quarterly results, compared with public companies. "In a privately owned company," one former CEO told us, "you have the permission to take a longer approach to value creation, and more air cover to sequence your choices." In public companies, boards and investors often make that hard for CEOs to do.

Day-to-day investor management and addressing board concerns are often the top priorities for public company CEOs. While these are important elements, public company CEOs spend much of their time managing issues that leave them with less time to personally impact operating performance. In some cases, this can create a big skill gap between what's needed in a public company CEO versus a PE company, with setting direction and influencing skills being more critical than actually doing (or the other way around).

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Compensate based on results

While CEOs in both contexts have performance hurdles and compensation tied to results, PE-backed CEOs in general operate with more extremes. This means that the CEO could earn far less if performance goals are not achieved, but may also earn much greater compensation comparatively when goals are met. While some claim this dynamic creates greater risk appetite or requires a greater comfort with risk-taking behaviors, others claim this alignment creates maniacal focus and 24/7 work ethic from PE-backed executives.

What PE can learn from public companies

Open the pathway for more independent (outside) points of view

PE firms are often active participants in their portfolio companies' operations. On one hand, this gives CEOs a much more active and invested partner in decision making. On the other hand, this relationship increases the risk that the CEO is being micromanaged. "What I missed the most in private equity is extra space from the board," one CEO told us. "Decisions that make an impact are at a higher level in public markets. It allows you to think at a higher level, and the board advises and supports you on this."

In particular, the way that privately owned companies are set up, with invested parties serving as the primary advisers, often leads to situations where leaders could find value in having more independent and diverse opinions on strategy and execution.

Indeed, private companies often lack the wide range of capabilities that most large public company boards have. While a public board with less "skin in the game" than the PE owners brings its own challenges, many of the leaders we spoke with said they valued the opportunity to have people they can tap for unbiased, outside-in insights on a variety of issues. "A select and strategic addition of outside directors can bring perspective that you might not find otherwise," one CEO told us.

Maintain a steady pace

The streamlined PE timeline and consolidated stakeholder base are often called out for their positive attributes. But many of the CEOs we spoke with pointed out that the typical PE ownership structures can create their own stressors in certain situations. For example, the pace of change and 24/7 focus from PE sponsors can leave CEOs burned out. It is increasingly common for a PE firm to cycle through more than one CEO over the duration of its holding period. The relentless focus on increasing value quickly can also limit CEOs' options for growth, especially if value cannot be proven in a short period. And, exit strategy timelines that rarely extend beyond seven years can in fact deter longer-term thinking compared to public counterparts.

The world of public companies, on the other hand, is steadier and more predictable. "It's driven by disclosure, analysts, and no sudden moves," one CEO told us. "Overall, the trajectory over a five-year period is somewhat predictable, which in turn informs behavior." For privately owned companies, opening the door to more long-horizon thinking can give CEOs valuable breathing room for driving value in unexpected ways.

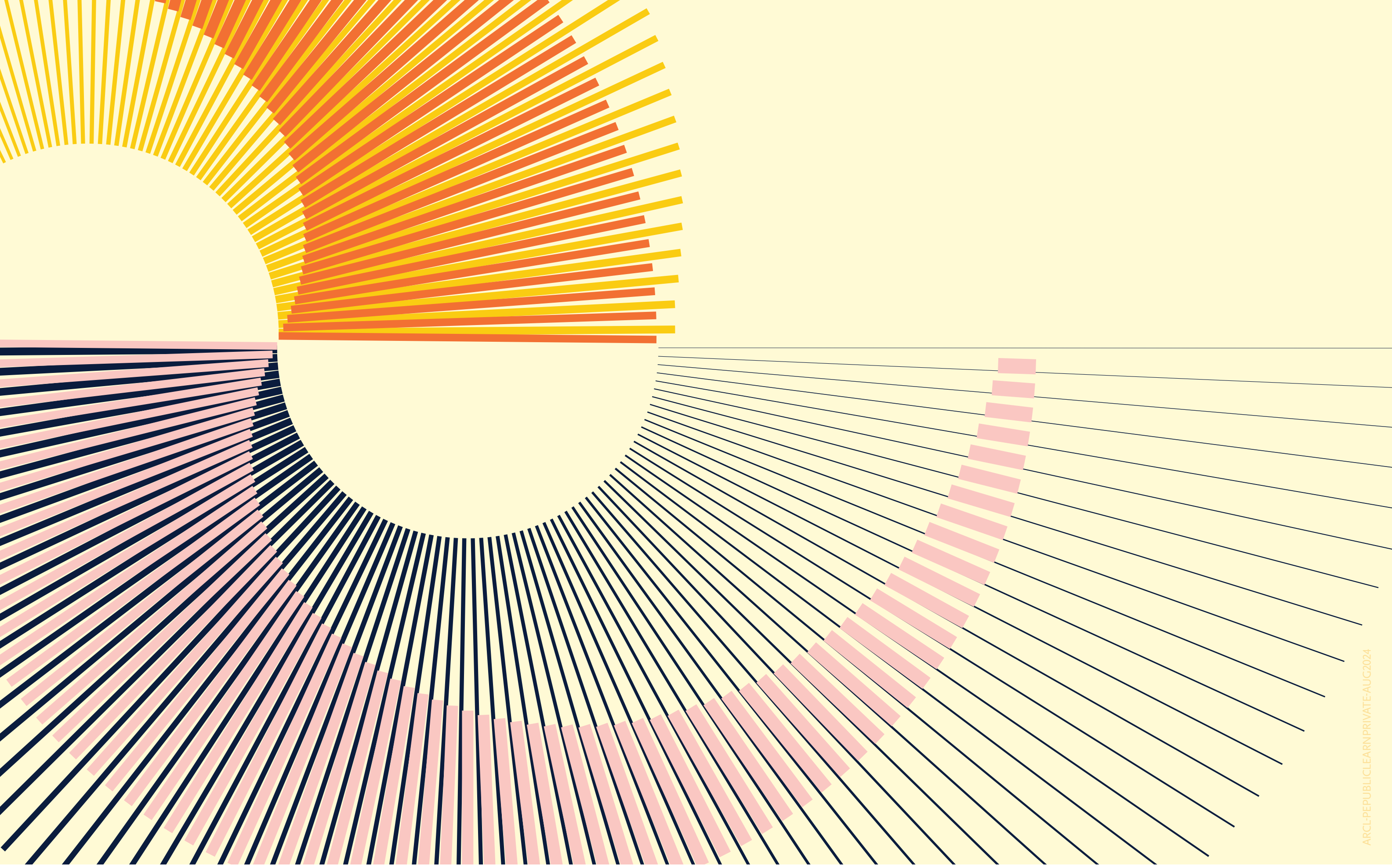
Test the edges on value-adding strategies

While immediate value creation and exit strategies receive the primary focus in private equity settings, they can come at the expense of strategies that can be beneficial but in a longer-term context. For example, one CEO noted that PE owners may be less inclined to invest in learning and development opportunities that don't link to immediate changes. This isn't to say PE sponsors care less about L&D than public companies, but tradeoffs get made. The reverse can also be true if something lies central to the investment thesis. For example, if sustainability initiatives will bring about a greater ROI during a hold period or increase the multiple of an investment on exit, one may swiftly find sustainability initiatives take priority over other crucial elements.

The best of both worlds

The leaders we spoke with align with what we've learned in our client work: Great leaders can be successful in both the public and private models. For executives considering transitioning between the two environments, it's important to be mindful of the differences, and to understand how and if you can adjust your management style to adapt. And for public boards and sponsors looking for CEOs, while familiarity with the ownership environment is helpful, it's important to understand how to assess for whether a leader may be able to transition between the two, and if you may be able to coach for it.

By understanding each environment and what matters in each, public and private companies can operate better to get the most from their leaders and drive value for all stakeholders.



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Privately held since 1956, we focus on delivering knowledge, insight and results through the collaborative efforts of a team of experts — now spanning more than 70 offices, over 30 countries and more than 50 practice specialties. Boards and leaders consistently turn to Spencer Stuart to help address their evolving leadership needs in areas such as senior-level executive search, board recruitment, board effectiveness, succession planning, in-depth senior management assessment, employee engagement and many other facets of culture and organizational effectiveness, particularly in the context of the changing stakeholder expectations of business today. For more information on Spencer Stuart, please visit **www.spencerstuart.com**.

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