

LEADING FOR EXECUTION

Execution is the Key to Improving Profitability

The Role of Private Equity Funds



LEADING FOR EXECUTION

This is an important time to focus on executing plans to improve the performance of your businesses.

Private Equity has a key leadership role

The Real Economy is now caught firmly in the financial crisis. Your businesses are facing the twin difficulties of deteriorating economic conditions and leveraged balance sheets.

Leaders should take initiatives now to assist their people in driving improvements in the operational and financial performance of their businesses. Don't be accused of not acting quickly enough!

The professionals in Private Equity funds that control companies are part of the leadership group alongside the CEO. The people in those businesses will respond positively to appeals to help improve profit and cash flow, provided there is clear direction, communication and commitment from management throughout. The execution of significant operational change is difficult but it is achievable if you follow certain guidelines. This paper focuses on how, and your role.

Introduction

Formulating strategy has always been popular with Private Equity funds but it is the execution of strategy, rather than its design, that is the leading concern of CEOs. Execution turns plans into increased profits and cash. It is the focus of much more attention by CEOs than strategy, and should be more of a focus for Private Equity fund professionals.

Dr Peter Goode, former Group CEO of Private Equity owned Vetco International says: *“Execution is the current, agenda-topping issue for CEOs, on top of concerns about the credit crunch. Strategies are almost two a penny. Coming up with ideas, some of them great, is not that difficult for many CEOs. But execution – that’s different. You need to pay close attention to it, or the strategy will fail.”*

Percy Barnevik, former Chairman of ABB Group, says: *“Thinking – the strategies and design part – only gets you 10% of the way to realizing value. 90% is in the execution.”*

Alexander Proudfoot believes that Private Equity funds should be focusing now on ensuring operational plans are implemented successfully and taking an active role to optimize success.

“I am shocked at the number of people who were just looking at the train coming down the tracks and were still worrying about whether they had the strategic plan for 2009.”

Jamie Dimon, CEO of JP Morgan Chase.

“The downside news from the real economy has increased the risks of a bigger and more sustained down turn.”

Andrew Sentence, member of the Bank of England’s Monetary Policy Committee.

That will mean that they should also focus more on ensuring the CEOs of their companies have execution experience or the ability to call upon extra external resource to help make execution succeed. It is very rare that companies have spare good people, with operational change experience, who can be taken out of their day jobs and committed full time to an initiative. Hiring additional resources can be key to success. Some Private Equity funds have now realized this and are playing an important role as part of the leadership team in the execution of strategy. In the current economic climate they need absolute certainty that the sense of urgency in the board room is communicated effectively throughout the organization and that execution of plans takes place with the greatest certainty of success and in an accelerated timetable. The funds we talk to say that over 50% of their companies are in breach of their banking covenants. Taking positive actions to improve performance and cash is an imperative.

Successful execution is not easy. It requires a comprehensive understanding of the business, its people and culture (*“how we do things around here”*); above all, it requires great communication and firm

leadership. Those are not traditional skills of Private Equity professionals.

However, the Private Equity funds cannot afford to shy away from what execution is really about, and their role as part of the leadership team - factors that can determine the success or failure of the successful execution of a vital operational change project.

Many Private Equity funds acknowledge that. However, because they have not traditionally hired people with the experience or skills, they are putting in place teams of operating partners to work alongside their management teams. This ensures the management teams focus on the need to deliver the investment plan - and requires a new relationship between the CEO, senior management team, and the Private Equity professionals. They all need to understand the operational issues of the business, its people and who has responsibility for what and the provision to the business of leadership.

Resources

That is a good approach but it does not provide the CEO with the resources to deliver substantial change at every level of the organization. It requires the full time commitment of teams of good, experienced people to work at every level. However, such people can be in short supply.

This paper includes excerpts from an exclusive conversation with Dr Goode, who left his post with Vetco International in May 2008 following the successful sale of the Group. Vetco is a leading provider of upstream oil and gas production facilities, process systems, technology, services and products. Dr Goode is now exclusive advisor to Candover in the oil and gas sector. He was Proudfoot's principal client when it completed a number of significant operational improvement projects with Vetco, after Candover introduced Proudfoot to the management team.

Dr Goode gives his views on

- The relationship between the CEO and the Private Equity funds who owned Vetco
- Why execution is so much more important to CEOs than strategy
- How to succeed in execution
- The role of the fund professional

Highlights of the conversation with Dr Goode:

- Execution is the top issue of the moment, heightened by concerns caused by the downturn.
- Thinking up a new strategy is easy. So why get obsessed with strategy reports?
- Execution is the difficult bit! It is successful execution that boosts performance and as a consequence improves profit, so it should be the priority.
- Execution requires an understanding of the operations of the business and the issues of its people.
- Surprise at how little many Private Equity professionals want to know about execution. Their attitude impacts the relationship between the fund and the management team.
- At the core of every successful execution is strong direction from the "leadership group", and clear communication with staff at every level of the organization. These have to be maintained throughout a project.
- The leadership group in a Private Equity owned business can include the CEO and the Private Equity owners. The group has an important role to play in ensuring commitment to the changes is maintained at all levels to guarantee successful execution.
- A key to successful execution, where the CEO and his or her team are not experienced at implementing major change, or where they do not have sufficient good people available to commit full time to the project, may be the involvement of external help. That should ideally happen from the outset, where the CEO believes extra specialist resources would ensure success and speed up the process.



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Dr Peter Goode, former Group CEO
of Private Equity owned Vetco International



Proudfoot has also included in this paper excerpts from interviews with CEO supercoach John Foppe, on how gossip (“*discussions around the watercooler*”) can fill the void left by poor leadership and communication, and with Priscilla Standifer, at Proudfoot, on the role leadership and communication play in successful execution. The interviews and the full conversation with Dr Goode are available on the Proudfoot website www.alexanderproudfoot.com

High Failure rate of execution. Why?

Pentacle reports that 56% of strategic initiatives fail during execution, with 73% of respondents blaming poor communication. The most expensive book shelves in the world are those in CEOs offices, laden with strategic reports, many of them unopened.

Dr Goode says that obstacles to executing change initiatives are in the mind, the vagaries of the markets, the politics of the boardroom and at every level down to the shopfloor. But they can be overcome, starting with clear leadership and communication, followed by project management and availability of people with experience. When they are overcome there will be a boost to business performance.

In his interview for this paper, John Foppe lays the blame for failures on poor leadership from the top. The Private Equity funds are often seen by employees to be part of the leadership group. The funds should contribute to communication and be committed throughout.

Read the conversation with Dr Goode on www.alexanderproudfoot.com

Private Equity firms showing greater interest in execution and achieving value creation through leadership

Private Equity funds are incentivised by their own investors to create value and some are now successfully engaging with their senior management teams to help ensure execution succeeds.

These companies are beating listed companies at creating value. In 2007, the enterprise value (EV) growth of Private Equity-owned businesses outperformed that of the public companies for the third consecutive year, according to Ernst & Young’s global study of the 100 largest Private Equity exits in 2007.

Source: <http://www.altassets.com/knowledgebanksurveys/2008/nz13828.php>

In fact, in 2007 EV growth was double that of equivalent size listed companies.

Source: <http://www.newswire.ca/en/releases/archive/July2008/09/c3002.html>

Ernst & Young has urged business to “*manage the basics and focus on execution.*” A survey by the firm found that a full 66% of corporate strategy is never executed, adding to those expensive book shelves.

With the recession now here the value of existing portfolio companies is being adversely affected; performance is down against plan, impacting bank financial covenants. There are also fewer opportunities to make acquisitions or to benefit from valuation arbitrage gains.

As a result, Private Equity firms are now committing more time to understanding the performances of their existing investments and to working with their management teams to ensure plans are executed and the most value and cash are realized.

Dr Goode believes this may also be because these firms now realize they have a very positive role to play in ensuring the success of execution.

The relationship between the Private Equity fund and the CEO is important. A fund normally backs management; however, most CEOs welcome a

positive involvement by the fund professionals. It is key to establish that relationship from the outset and for the professionals to be sufficiently experienced in business to fit in and contribute.

Ownership

However, it is always important for the CEO to retain ownership of the need to manage the business and deliver the agreed business plan. That ownership must not become the Private Equity fund’s responsibility. The people at every level of the company must accept the need to change.

The CEO and his/her leadership team need to ensure they show commitment to the execution of an operational improvement project throughout its life. A major cause of failure is the CEO losing interest once execution gets under way; the employees pick up on that and also lose interest.

It is important that, once the Private Equity fund becomes involved on the board and part of the leadership team, its representatives also show

The CEO supercoach advice to CEOs

- Views like these are reflected in what CEO supercoaches Paul Gibbons and Paul Taffinder observe. Says Gibbons: “The CEO’s role is critical in communication – and there are things only CEOs can communicate. Only they can communicate with shareholders and analysts and manage how the change is viewed by the capital markets. In addition, the CEO can help the people affected by the change make sense of how it fits with the overall vision and strategy, which the CEO principally owns.

“Most complex programmes require much more than just CEO backing, ground rules and expectations. A programme with a large payoff and risk profile will likely touch many of the top hundred in the company, and even a few recalcitrant members of that group can torpedo a programme.

“Furthermore, executive teams are not usually straightforward places politically. Depending on the CEO and the culture, the CEO’s direct power can be

circumscribed. Real alignment, including willingness to endure hardship and make difficult decisions, produces considerable effort.”

- Taffinder, like Gibbons, has gained the confidence of CEOs, and has mentored CEOs in the US and UK. “Among the perennial issues that concern CEOs, first and foremost is execution,” he says. “Strategy comes a distant second and, in some industries, like reinsurance and investment banking, it doesn’t feature much at all.

“Execution is a concern for the CEO because (i) it involves getting very senior executives to act together in concert – and that can be a problem (ii) if it fails in some way, that could reflect badly on the share price and the CEO.”

- You can see now why execution, and getting it right, is such a focus for CEOs.



commitment to the execution of operational strategies and are prepared to be visible.

The general consensus out there is clear; execution is difficult but vital, and requires business understanding, leadership and communication from the top, and dedicated resources.

Successful execution

To the old adage that some 70% of all internal projects fail to deliver to plan, can be added a new one: there is little to stop a project from succeeding if the CEO backs it, enforces common ground rules throughout, has a detailed project plan, expects execution to succeed to a plan and commits appropriate people and resources with the necessary experience.

A new operational initiative is like a new product; it is so much more likely to succeed and create value if it is launched and completed on time and on budget.

It enables the company to be more competitive in the market and move ahead of the competition.

Typically, successful companies do not have people who are good at what they do, experienced at execution *and* have time to be taken full time out of their normal job to spend on execution initiatives. That can be remedied through project management and the commitment to engage the right help, and to have the confidence

in the organization to see this not as a help but as an investment to ensure its people succeed.

Strategies can be bought off the shelf. Successful execution can't

There is a view among CEOs that strategy is the easy part; it can even be “bought” from specialist consultancies, which may already have “off the shelf” strategies they have developed for other clients. In reality, it's the execution of strategy that creates the value in profit and loss, and that is the difficult part.

So why do Private Equity funds spend so much time discussing strategy with CEOs? Strategy is recognized as being an important contributor to the business, but as Dr Goode points out, it should come second to execution.

Emphasizing strategy almost to the exclusion of so much else gives the impression that the funds are missing what could be a key part of their role. Dr Goode says: “*There is a fundamental gap between the best-laid plans and their realization, which only execution can fill.*”

If the Private Equity funds miss this emphasis they will reduce their credibility with management and fail to support the CEO in a key area.

Examples The Proudfoot and CEO perspective on execution

Seven Elements of Execution

Clear leadership throughout the execution, from the leadership team and from the immediate managers of every individual.

Clear communication about the need for execution to succeed for the company and for the individual, with progress reported at all levels throughout.

Agreement on the redesigned structures, systems and processes with the people at all levels of the organization positively and not through compliance.

Changing attitudes, behaviors and skills as people align themselves with the new needs of the business during execution.

Accelerating the pace of change through project management and execution to ensure there is momentum and drive without internal compromises.

Measurement and control, to give management the tools on a daily/weekly/monthly basis to measure and control what is going on and ensure the execution programme stays on track.

Resources, to make sure there are sufficient full time experienced people committed to the success of the project and with ownership of achieving its financial objectives to plan.

The watercooler philosophy; how gossip and “everyday conversations” can disrupt execution

In his interview, John Foppe says the watercooler is like an open forum for gossip and rumor. Foppe adds that unless communication and leadership from the top are clear and strong, gossip at all levels will dilute the message and the execution.

He spent more than 15 years travelling the world as a CEO supercoach. He started to hear the same complaint from leaders and managers – *“it’s really hard to make things happen.”*

A former high ranking executive of a US soft drinks giant confided in him, *“We were great at developing strategy, and we were great at creating innovative products. We were also great at marketing - but there was always some excuse why the people couldn’t hit their numbers.”*

Foppe says that executive *“exemplifies the sentiment of countless organizations in the general marketplace. Great vision. Poor execution. No outcome. Why?”*

“Many companies have unacknowledged factions within them,” he says. *“There is a real ‘us and them’ attitude. Another common problem is that many companies operate from crisis to crisis: ‘We can’t do anything about our problems because we don’t have time, and we don’t have time because of our problems,’ they say. It’s a trap. The watercooler has much to answer for.”*

Without clear communication from the top whenever things are happening in an organization, rumor will take hold and establish ways of behavior that can be disruptive and, consequently, destructive.

“Employees take on a way of being that encodes itself into the fibre of an organization’s culture, either blocking the vision from becoming an outcome or from bridging the gap between the vision and the day-to-day reality,” says Foppe. *Just like their gossip-prone staff, CEOs too can hinder execution. “Most CEOs I interact with are at one or the other end of a spectrum. Either he or she is in complete denial [about the current state of affairs in the business] or is too confrontational about what needs to be done.”*

Recipe for disaster?

Where communication from the top down is inadequate, rumor becomes rife and obstruction by staff sets in. It’s a recipe more suited to failure than success.

Foppe - *“Essentially, people are sitting around the watercooler and moaning. That translates into potentially dangerous gossip and embedded behavior, as they wait for something positive and constructive to be communicated from higher up the organization.*

“It’s not only gossip that is to blame for staff resisting execution. Gossip implies rumors, secrets, etc, whereas the watercooler philosophy also includes everyday conversations which filter, distort, and garble the organization’s vision.”

Foppe advises: *“The most critical thing for CEOs is awareness – they cannot be in denial but they also must have empathy for the people they work with.”* And he quotes his former boss, motivational speaker and teacher Zig Ziglar: *“People don’t care how much you know until they know how much you care.”*



The solution to the watercooler problem:

The only viable response to the watercooler “problem” is for the leaders of a businesses to be very clear and proactive in their communication with employees. In her interview, Proudfoot’s Priscilla Standifer is very firm about this, to the extent that anything up to 50% of the execution of a change programme can be spent on activities to involve staff at every level of the organization in the change and ensure they are positively engaged and aligned.

For the full interview, visit www.alexanderproudfoot.com

Loss of interest is a threat

Priscilla Standifer also emphasizes that a loss of interest in the project by the CEO or the leadership team is a threat to execution and is inextricably linked to communication.

“CEOs and senior executives often don’t realize the extent of the influence they have over an execution – that what they say, or don’t say, and how they behave, has a huge effect on staff, including lower level managers,” says Standifer. *“Our response to that is to engage them in the execution process and be active in it throughout. CEOs may think*

initiating the change process is the end of it for them, whereas it’s only the beginning.

“Good communication gains results more quickly and much more powerfully, and sustainably, than by simply ordering staff to comply with instructions or not communicating clearly and appropriately through different mediums. The impact goes way beyond loss of short-medium term profits.”

Standifer concludes: *“Failure in execution can be foreseen and planned against. Excellence in communications will reduce the risk, especially in Private Equity situations where there may be a shortage of experience in executing the sort of material changes required to achieve challenging business plans and in accelerated time tables.”*

Conclusion

Execution is the hot topic among senior executives in all types of company. Strategy and planning are seen by many CEOs as the easy part that can be bought in for “two a penny” off the shelf from many consultants. The difficult part is execution. That requires an understanding of the business and its people, leadership, communication and commitment.

CEOs worry about execution, and rightly so from their personal perspective and the perspective of their business and its people. Their concerns have been intensified by the current economic conditions and performance against plan and bank covenants. Do not get caught comatose, looking at the train coming down the track, worrying about the strategic plan for next year.

Now is the time for leaders to show and communicate their sense of urgency, and to communicate - to the people in their organization - plans to drive the operational and financial performance of the business.

The execution of those plans, in an accelerated time table and achieving the financial results with the greatest certainty, is more crucial now than it has ever been.

Peter Goode, directing his arguments to CEOs, says *“... ‘leading for execution’ is about active involvement; it is key to be seen to be leading and getting involved and ensuring that senior managers are on board. That is the route to gaining broad buy-in and helping the project to be a success.”*

CEOs need execution because strategy on its own is simply not enough.



Private Equity funds are now realizing that they have traditionally not been involved in execution, one of the key drivers to creating shareholder value. They are now far more interested and involved in execution, but the relationship with the CEOs of the business must be established in this way as early as possible. They must not take responsibility from the CEO for achieving the results.

About Alexander Proudfoot

Proudfoot is the world's leading operational consultancy which specializes in the design and execution of projects achieve material changes in operational performance and, as a consequence, financial performance. We are extremely experienced at executing change successfully across the world and across all business sectors, having completed 10,000 projects over 60 years. Some 30% of the projects we complete are for the management teams of companies owned by Private Equity funds. We know how to work for teams to ensure execution of challenging business plans succeeds.



About John Foppe.

John Foppe was born without arms but that has not stopped him from becoming a leading speaker, CEO supercoach and trainer on how to maintain momentum when executing initiatives. John is CEO of Visionary Velocity Worldwide, of St. Louis, MO. For further information visit www.visionaryvelocity.com, call (+1) 618.526.5500 or email john@visionaryvelocity.com.

About Paul Gibbons.

Paul Gibbons is Chairman of Future Considerations, one of Europe's top leadership consulting firms. He is a psychologist, neuroscientist and philosopher by education, and a banker and consulting thought-leader by trade. He recently moved to from London to Madison, Wisconsin with his family and can be found on www.paulgibbons.net or www.futureconsiderations.com.

About Paul Taffinder.

Paul Taffinder is an author, CEO supercoach and founder of Taffinder Consulting - and a Visiting Professor at University of London. His written works include Big Change and The New Leaders. He has also written The Leadership Crash Course. More at www.taffinderconsulting.com Previously Paul was a partner at Accenture. Contact: pt@taffinderconsulting.com

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