Leadership Capital Report 2024

Quantifying the impact of Leadership in private equity-backed businesses

About LCap Group

We are a leadership consultancy that supports investors, high growth businesses and their leadership teams through the entire investment lifecycle.

We unlock people value and maximise value creation through our expertise in insights, change and development.

The three phases of the 'leadership lifecycle'

Our services span the three phases of the 'leadership lifecycle' and cater to the spectrum of private equity, from private capital, to mid-cap and large-cap businesses.

Analytics

Our objective, data-led insights on leadership competencies and behaviours enable more proactive, evidence-based leadership decisions, and better outcomes.

Change

Powered by insight, our executive change brands - DRAX and DRAX Affinity - support leadership optimisation to build an executive team with the right balance of competencies and behaviours to deliver growth.

Development

Our behavioural evaluation, PACE, enables clients to maximise the impact and effectiveness of their leadership capital, by providing the tools to engineer their culture.

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1. Leadership Capital 2024

How private-equity backed businesses are leveraging leadership in shifting markets and challenging times for value creation

Market adversity drives leadership innovation

Private equity-backed businesses exiting in the last 12 months have come through a period of significant change and adversity. For those achieving top quartile returns, Leadership Capital has been a critical differentiator in maximising performance, growth, and securing a successful exit.

Welcome to the sixth LCap Group Leadership Capital report, a study of every private equity backed company that exited in the last 12 months, to assess how Leadership Capital correlates with financial performance on exit.

Throughout this report, we aim to understand how the best performing companies have optimised leadership to meet the needs of a changing market and shifting value creation levers. Leadership Capital isn't static; what worked in previous years is different to what has worked for this cohort of businesses. By shining a light on evolving strategies and trends, we empower investors and businesses to become even more targeted and responsive going forward.

A testing time for investors

This cohort of exiting businesses and their investors haven't had an easy ride, having felt the full force of the economic rollercoaster that has defined the 2020s so far. Acquired at the tail-end of the 2010s, these businesses were rapidly swept into a period of rapid change and huge uncertainty, including first the pandemic, followed by the war in Ukraine, and then the inflation crisis and faltering economy of the post-pandemic period.

This unusual and complex sequence of events has tested leadership and investors to the full, and the impact can be seen throughout this year's report findings. It is testament to the strength and maturity of the private equity sector that, despite these challenges, it has still delivered outsized growth, remaining the top performing asset class.

Leadership innovation

But innovation is often born from adversity and this report highlights how Leadership Capital can help businesses **respond to changing markets** and continue to deliver value.

As in previous reports, we see that the best performing businesses prioritise **building a high performing leadership team that evolves with the business**, particularly where the presence of a strong founder demands a watertight succession plan.

For top performers, it isn't just about getting the right heads around the boardroom table, it's also about how leadership **behaviours and competencies** align with the market and value creation. This year, we find that domain experience has been at a premium as uncertain times have demanded deep sector and customer knowledge.

Finally, **emerging and evolving leadership roles have come to the fore** to spearhead new business objectives and priorities. Offering a critical edge and new perspectives, we anticipate these roles will become increasingly commonplace in PE-backed businesses and the wider business landscape.

Better leadership for better companies

Private equity is vital to a healthy economy, putting capital to work to build stronger companies, create jobs and deliver value to shareholders. As the economy gradually recovers from an unprecedented few years, investors are more important than ever to help build future market leaders, support turnaround stories, and drive the next wave of innovation and growth.

Leadership Capital is central to doing that effectively, and those businesses that innovate and evolve how they optimise leadership will be at an advantage. This report aims to arm investors and portfolio management teams with quantitative insights to facilitate objective leadership discussions and proactive decision-making, so they can continue to optiomise their Leadership Capital, for whatever the future brings.

Executive summary

Adversity can be a powerful catalyst for innovation, and private equity-backed businesses exiting in 2023/24 have faced their fair share of both. A rapidly changing market and economy have forced businesses and investors to push the boundaries in how they leverage leadership to create value.

This has driven four overarching trends amongst top performing businesses: the need to adapt leadership strategy to market shifts; to intentionally build top performing leadership teams; dig deep into leadership behaviours and competencies to drive performance; and maximise emerging leadership roles to spearhead change.

Within these four trends, ten key insights stand out as critical to maximising leadership now and in the years ahead:

1 Value creation and leadership demands shift

Value creation levers are shifting in response to market challenges.

Between 2008 and 2019, leverage and multiple expansion accounted for over 50% of value creation. Post-Covid, that has fallen to 39%, while the role of margin improvement has more than doubled to 22%. New priorities mean investors and management teams are rethinking their leadership strategies to adapt and enhance growth potential. Businesses exiting in the last 12 months made twice as much leadership change as those the previous year (9.7 vs. 3.7 changes amongst top quartile performers), and a wave of new leadership roles and responsibilities are emerging.

Pre-Covid (2008–2019), leverage and multiple expansion made up over

50%

of value

2 Market and customer focused leaders at a premium

This year's top performing leadership teams were defined by strong domain expertise, combined with robust situational experience, suggesting the pandemic period put a premium on deep market understanding and customer-centricity.

Operating in unprecedented and unpredictable times, domain specialist leaders were at an advantage, with the ability to respond rapidly to customer behaviour through optimising operations, and exploiting market opportunities effectively. The result: higher equity value at exit.

Top-performing leadership teams this year, defined by strong domain expertise and situational experience, drove higher equity value at exit

> "In navigating changing markets, we see the best businesses proactively adapting their leadership strategies to drive value creation. Innovative leadership solutions are now essential, with top-performing companies making intentional decisions to build teams that can respond to these shifts and spearhead growth. The ability to evolve leadership roles and competencies is becoming a critical factor for success in this environment."

Samuel Robberts, Chief Strategy Officer

3 Proactive leadership strategy linked to top returns

Across all criteria, the best performing businesses were more proactive and strategic about leadership change and optimisation.

Businesses delivering top quartile returns made more leadership change (9.7 changes vs. 8.1 for the bottom quartile) and made change faster, introducing core C-suite hires within the first 18 to 24 months of the hold period. These top performers also had significantly larger leadership teams, averaging almost seven members, compared to just 4.4 in the third quartile businesses. Having a wider breadth of roles and specialisms, optimised for value creation, set them apart from the competition.

Top performing businesses make

21%

more leadership change throughout the hold period than lower performers

4 Top founder-led businesses prioritise strategic succession plan

Founders are a significant asset to PE-backed businesses; 25% of top quartile businesses still had a founder in place at the time of exit, compared to just 14% of those in the lowest quartile.

But, for founder-led businesses looking to scale, building a balanced, high performing leadership team around the founder is vital. Top performing founder-led businesses do this highly effectively, with an average of 7.5 leaders in place, suggesting a less formal and hierarchical structure and a breadth of functional roles. Over a third had a founder succession plan in place, compared to none in the bottom quartile.

38%

of top performing founder-led businesses plan for succession

5 Rise of high impact chair

Investors are increasingly looking for chairs who can actively influence the value creation journey throughout the hold period, as opposed to taking a hands-off, purely governance role.

Whereas historically, chairs have predominantly joined post-deal, this year's exiting businesses made a quarter of chair appointments in year three and a fifth in year six, suggesting they're looking to maximise the impact of the role. Executive Chairs are also emerging as a valuable differentiator to help manage periods of turbulence; 16% of upper and second quartile businesses had one, compared to just 7% of those in the bottom two quartiles. In contrast, lower performers were more likely to introduce an interim CEO to perform a similar function.

58%
of businesses exit with a Chair

6 Emerging M&A Directors key to maximising bolt-on acquisitions

M&A Directors are rapidly emerging as key players in top performing leadership teams for their role in orchestrating bolt-on acquisitions.

Two thirds of top quartile businesses (68%) made a bolt-on during the hold period, and 25% brought an M&A Director to ensure maximum value for the business. As a fledgling role, these M&A specialists tend to be more junior than others in the leadership team, but their deep sector knowledge combined with a skill for execution makes them well suited to the position.

68%
of top quartile businesses made a bolt-on acquisition during the hold period

7 More than a CTO: Multifaceted technology leadership drives top returns

Board-level technology leadership is now commonplace for both software and non-software PE-backed businesses, with 30% of top quartile performers having a CTO, or other technology leaders upon exit.

Furthermore, the growing complexity and diversity of technology requirements has now created at least seven distinct job titles, many of which are converging and or changing, as seen with the rise of the Chief Technology and Product Officer (CTPO) in recent years. For many businesses, one "technical leader" is not enough, with top performers boasting an average of three functional, technology specialists on the executive team, with responsibilities spanning full-stack technology, IT functions, data, security, and product management.

30%
of top quartile performers have a CTO or other tech leader at exit

8 CHROs prove their value in the boardroom

CHROs are the new rising stars of PE-backed businesses, as employee engagement becomes a key priority at a board level.

Now appointed by a third of top quartile companies (30%), compared to just 5% of the poorest performers, CHROs are also being brought in early, with 28% of top and second quartile companies hiring a CHRO in the first two years. Forward thinking companies increasingly value the CHRO's expertise on engagement and talent management strategies, which are pivotal to delivering business change and organic growth. But equally, CHROs are becoming integral to optimising the leadership team for ever-evolving business needs.
This dual role is why they are proving their value more than ever.

28% of top and second quartile companies hire a CHRO within the first two years

9 Interims power business turnarounds and specialist impact

In a year when bankruptcies have reached a 30-year high, interim leaders perform a valuable role powering turnarounds in poorer performing businesses.

Third and fourth quartile businesses are twice as likely to use interims than those in the top quartile and do so across a wider range of C-suite roles. In contrast the best performing businesses leaned on interim leaders only sparingly, and solely in the CFO position, with many instead opting for an executive chair to bring fresh energy and insight.

62% of all the interims used throughout the hold period were CFOs

10 Gender diversity: A tale of action and inaction

Gender diversity within PE-backed organisations is a tale of progress and stagnation.

Figures show that women make up fewer than one in five PE-backed leaders at the time of exit (17%) - compared to 23% across the general business landscape - a trend perhaps aggravated by less willingness to look beyond 'tried and tested' talent pools during turbulent times. However, a sub-set of businesses are bucking the trend. Among companies with at least one female C-suite member, 45% had two or more, representing 30% of the C-suite team. Nonetheless, a more concerted effort is needed across the sector to provide opportunities to female leaders and unlock the potential of diverse leadership teams.

Female representation is down 25% on PE backed boards compared to the average board

Leadership Capital

What is Leadership Capital?

Leadership Capital refers to the collective value and effectiveness of an organisation's leadership team, encompassing their skills, experience, vision, and the trust they command within the company. It includes the capacity of leaders to drive strategic initiatives, inspire employees, foster innovation, and navigate through complex business landscapes. Leadership capital is not a static asset; it can grow, or it can lose value when the leadership team does not have the right experiences, functional blend, or behavioural complementarity.

How does Leadership Capital impact value creation?

Leadership Capital is critical in any business, but even more so in private equity-backed businesses, which have a defined timeframe within which to create significant value. Achieving a high level of leadership capital is pivotal in several key areas:

- **Strategic vision and execution:** Helping set a clear vision and strategy, aligned with market opportunities, and ensuring that the company stays on course during its growth trajectory.
- **Talent attraction and retention:** Skilled and visionary leaders create an environment where employees feel valued and inspired, reducing turnover rates and fostering a culture of loyalty and productivity.
- **Innovation and adaptability:** Leaders with high capital encourage a culture of continuous improvement and are better equipped to pivot in response to market changes or disruptions.
- **Stakeholder confidence:** High leadership capital instills trust and confidence that the business can manage growth effectively and deliver returns on investment.
- **Operational efficiency:** Experienced leaders streamline operations, eliminate inefficiencies, and implement best practices.
- **Crisis management:** Leaders who can effectively manage stress, make decisions, and communicate transparently are invaluable in navigating challenges without derailing the company's progress.

Building resilience through Leadership Capital

Optimising Leadership Capital equips businesses with the skills to manage and embrace today's challenging and unpredictable business environment. For example:

- **Enhanced decision-making:** The ability to make informed and timely decisions, balancing short-term needs with long-term objectives.
- **Strategic partnerships and networking:** Effective leaders can forge strategic partnerships and build networks that provide additional resources, knowledge, and market access, accelerating growth.
- **Cultural cohesion:** Fostering a strong, cohesive corporate culture puts an organisation in a stronger position to overcome challenges.
- **Sustainable growth:** By prioritising sustainable practices and ethical governance, leaders ensure that growth is not only rapid but also sustainable.
- **Succession planning:** Prioritising leadership ensures that the organisation always has a ready pool of capable leaders to drive its growth and innovation efforts.
- **Enhanced reputation:** Companies known for strong leadership attract not only top talent but also potential partners, customers, and investors; a significant competitive advantage in the marketplace.

Framework

The LCap Group has developed a framework for measuring Leadership Capital, supported by research carried out with leading academics, Adrian Furnham and Simmy Grover, at UCL and Birkbeck University.

The study has analysed every private equity deal across the UK and Europe since 2010 and is an ongoing study, incorporating new deals as they happen. Each company is analysed based on the profile of its management team throughout the hold period and its financial performance upon exit. Through this work, we have identified four key factors that determine leadership success:

Functional competence: Does the team contain the right representation and depth within each of the key functional areas (i.e., finance, operations, technology etc), for its growth stage and value creation plan? Does this balance also suit the market that the business operates in?

Situational competence: What situational challenges have leaders faced in the past and how well does that experience match the current challenges they face and their value creation journey?

Domain competence: Does the leadership team have knowledge of the industry, market, the customer base, and business model?

Behavioural competence: Is the team compatible at a behavioural level, based on the key behaviours of Pragmatism, Agility, Curiosity and Execution? Does the team have cognitive diversity; a wide range of perspectives and behaviours? Will they bring out the best in each other?

This report applies this framework to the UK private equity marketplace in the 2023/24 financial year, revealing fascinating insights about the power of leadership for value creation.

About Leadership Dynamics

Leadership Dynamics is the first digital insight product designed for individual leaders and leadership teams of high-growth founder-led or private capital invested companies.

Leadership Dynamics is designed specifically to optimise the potential of an individual or leadership team whilst maximising their performance within high-growth businesses. It provides leadership foresight on the performance and potential of individual leaders and leadership teams with objective data-driven analysis.

About PACE

PACE stands for Pragmatism, Agility, Curiosity and Execution: and is the No.1 private equity behavioural evaluation, that allows high-performing leaders to understand their strengths, weaknesses, and the key to developing their performance levels.

It is the only behavioural evaluation benchmarked against private equity executives, designed by leading psychologists, and purpose built for the unique leadership demands of venture, private and growth capital.

Methodology

Throughout this report company performance is based on Compound Annual Growth Rate (CAGR) weighted average, which comprises three financial components: EBITDA, revenue and total assets. This allows for easy comparison across all exiting companies which have been segmented into quartiles, referred to as 'upper quartile' (Q1), 'second quartile' (Q2), 'third quartile' (Q3) and 'lower quartile' (Q4) throughout this report.

A mature UK market

Mapping company CAGR components together demonstrates the overall maturity and success of the private equity asset class in the UK, with 92% of companies reporting positive CAGRs on at least one measure. However, the landscape in 2023/24 reveals a greater variance in value creation, with both extreme gains and losses being reported with a slight increase in the number of companies reporting negative CAGRs compared to 2022/23, reflecting heightened volatility within the marketplace.

Macroeconomic effects

Several macroeconomic factors have compounded to create this variance. Interest rate spikes have increased borrowing costs, impacting companies' ability to finance expansion and operational improvements. Higher interest rates also discourage new investment, contributing to slower growth rates across sectors. Concurrently, cost of living increases have squeezed consumer budgets, leading to reduced consumer spending. This reduction in demand affects revenue growth for many companies, particularly those reliant on consumer markets.

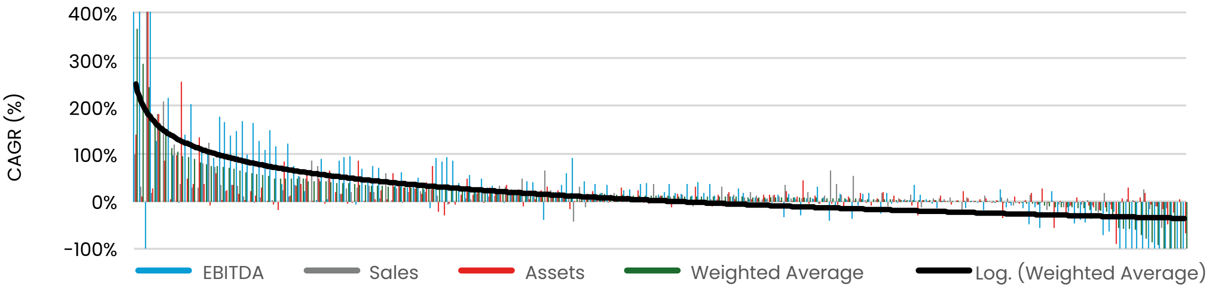
Inflation fluctuations have further complicated the landscape. Elevated inflation rates drive up the costs of goods and services, squeezing profit margins for businesses that struggle to pass on these costs to consumers. The resultant pressure on profitability is reflected in the significant EBITDA growth among the best-performing companies, as these companies have managed to sustain or enhance their operational efficiencies and cost structures despite inflationary pressures.

Energy price increases have added another layer of complexity. Rising energy costs have led to higher operating expenses for companies, particularly those in energy-intensive industries. These increased costs are challenging for businesses to absorb and can significantly impact bottom-line profitability if not managed effectively.

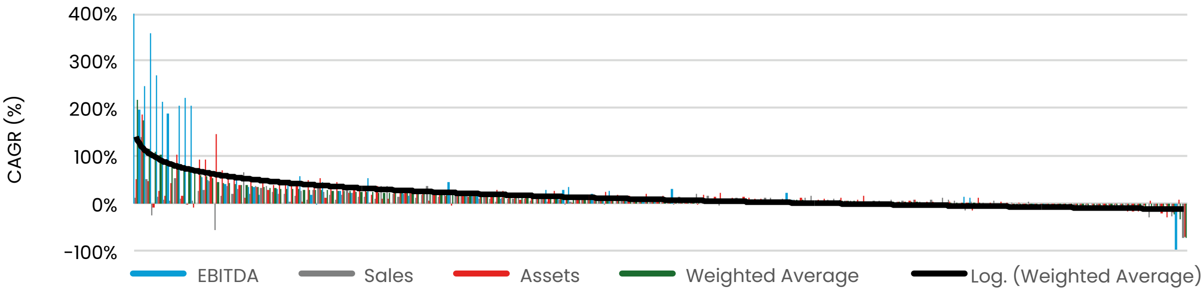
The UK economy's technical recession and the highest bankruptcy rates in 30 years also weigh heavily on company performance. Recessionary conditions often lead to reduced investment activity and heightened caution among consumers and businesses alike, stalling growth initiatives. The surge in bankruptcies highlights the vulnerability of businesses to these challenging economic conditions. Notably, 50% of the companies reporting negative CAGRs were affected by bankruptcy of some description, underscoring the severe impact of the current economic climate on private equity backed businesses.

Overall, the increased variance in CAGRs within the private equity asset class in 2023/24 can be attributed to the compounded effects of interest rate spikes, cost of living increases, inflation fluctuations, energy price increases, reduced consumer spending, technical recession, and historically high bankruptcy rates. These factors have created a challenging environment for value creation, contributing to both the notable successes and significant setbacks observed within the sector.

83% of all PE backed exits in 23/24 delivered growth across the hold period



85% of all PE backed exits in 22/23 delivered growth across the hold period



2. Value creation and leadership shifts

A challenging market sparks new value creation priorities and a new approach to leadership

Value creation and leadership shifts

No. of Active PE Investors	Dry Powder Available (£B)	Assets Under Management (£B)
2,446	£159.4	£18,093
143 PE funds closed	£128 Trillion capital raised	The average size of fund was £713 M, which represented an increase of 13% in the capital available compared to 2022/23.
6,754 Investments	19,218 Inflight	1,424 Exits

- **European deal activity, exits and new funds all down on the previous year**
- **Dry powder continues to increase**
- **Value creation shifts from multiple expansion to margin improvement**

Businesses exiting in the last 12 months have wrestled with a turbulent market, spanning first the pandemic and then the post-pandemic recovery period defined by inflation, high interest rates, and rising energy costs. With impacts on borrowing, consumer spending and economic growth, investors have had to think on their feet to maintain growth and maximise value creation. For those at the lower end of the market, the fear of bankruptcy has loomed large, with business failures reaching a 30-year high in January 2024*.

Deal activity, exits and new funds down on last year

High interest rates meant it was a slower year for new deals across Europe, which declined 10% on 2022/23 (6,754 vs 7,479). Cautious investors were more reluctant to part with portfolio companies, with European exits also down by 10% (1,424 vs. 2,589), and fundraising was also hit, with 20% fewer new funds closed.

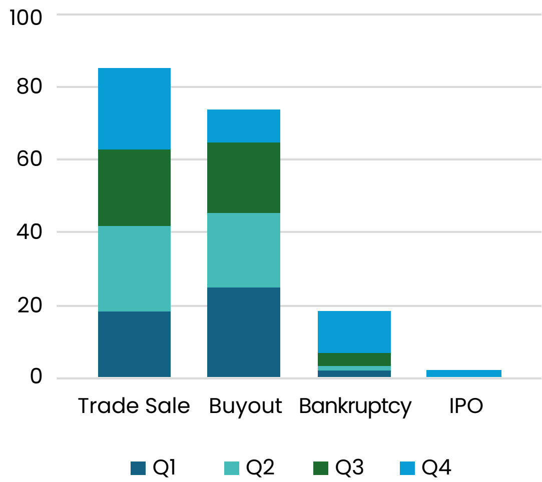
Fund sizes hold steady and plenty of dry powder to deploy

Yet despite fundraising and exit challenges, overall capital raised increased to £128 trillion, up from £118 trillion the previous year. The average fund size increased by 13% to £713 million, suggesting many LPs remain confident in the sector. Private equity still has record levels of dry powder to deploy, indicating continued optimism about long-term value creation opportunities.

Buyouts and trade sales most lucrative

Trade sales emerged as the most popular exit route and two-thirds of this cohort's top-quartile businesses (68%) made bolt-on acquisitions, indicating significant activity from strategic buyers and consolidation by bigger players. Buyouts were also popular and marginally more successful than trade sales for returns achieved (34% of buyouts achieved Q1 exits vs 22% of trade sales). In contrast, unfavourable market conditions meant IPOs were the least popular and least successful exit route.

Trade sales were the most popular exit route although they showed mixed returns



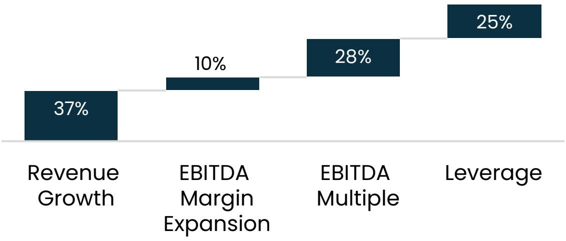
* The Insolvency Service

Value creation levers shift from multiple expansion to margin improvement

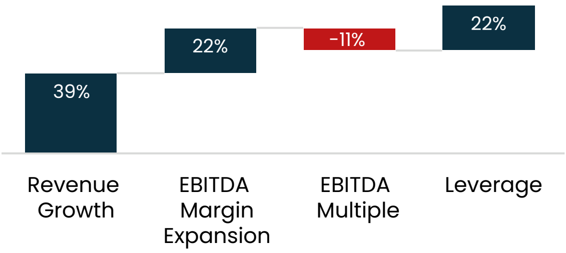
This combination of market factors meant that value creation levers that worked for the prior 10+ years ceased to be as effective for this cohort of businesses. Between 2008 and 2019, leverage and multiple expansion accounted for over 50% of value creation, but post-Covid, that has fallen to 39%. Meanwhile, the role of margin improvement has more than doubled to 22% over the same period and is expected to reach 30% in the next couple of years.

The bottom line is that investors and leadership teams are having to work much harder to extract value from their portfolio companies through approaches spanning operational efficiency, digital transformation, go-to-market strategy, M&A, and international expansion.

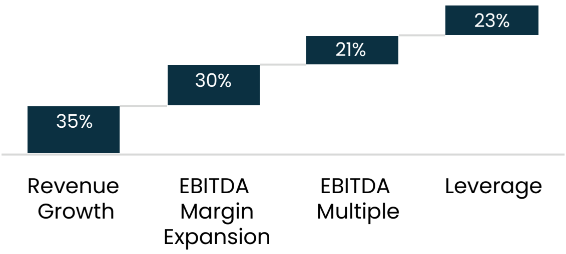
2008-2019 value creation focused on multiple expansion & revenue growth



Post covid value creation shifted to margin improvement & revenue growth



That focus on operational effectiveness is expected to continue into 2024-25



Value creation and leadership shifts

- **Volume of leadership change more than doubled amongst exiting businesses in 2023/24**
- **Spike in domain experience demonstrates need for customer-centricity and market understanding**
- **Emerging C-suite roles differentiate top performers**

As market challenges and value creation levers have shifted, private-equity backed businesses have had to rethink their leadership strategy to adapt to a changing market. This plays out in three key trends:

Volume of leadership change doubles

The volume of leadership change more than doubled amongst this cohort of exiting businesses. Throughout the hold period, top quartile businesses made an average of 9.7 changes, compared to 3.7 amongst last year's cohort. Those in the bottom quartile made 8.1 changes compared to just 3.4 last year.

Partly driven by the unusual market, which required businesses to rapidly adapt to changing circumstances, this rise also demonstrates the increasing role of leadership in value creation, as organic growth levers, such as operational efficiency and innovation have come to the fore.

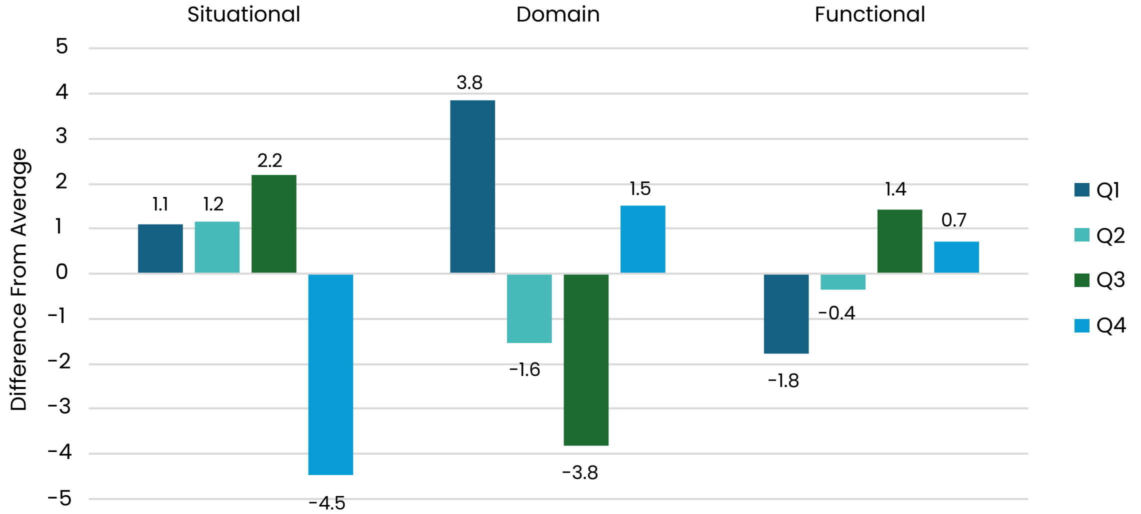
Spike in domain experience

Leadership profiles have also shifted to suit an evolving market. This year's cohort of exiting leaders boast a significantly higher level of domain experience than those in previous years, when situational experience was more sought after. This suggests the pandemic and post-pandemic periods have put a premium on deep market understanding, customer-centricity, and squeezing margins; all vital for delivering organic growth.

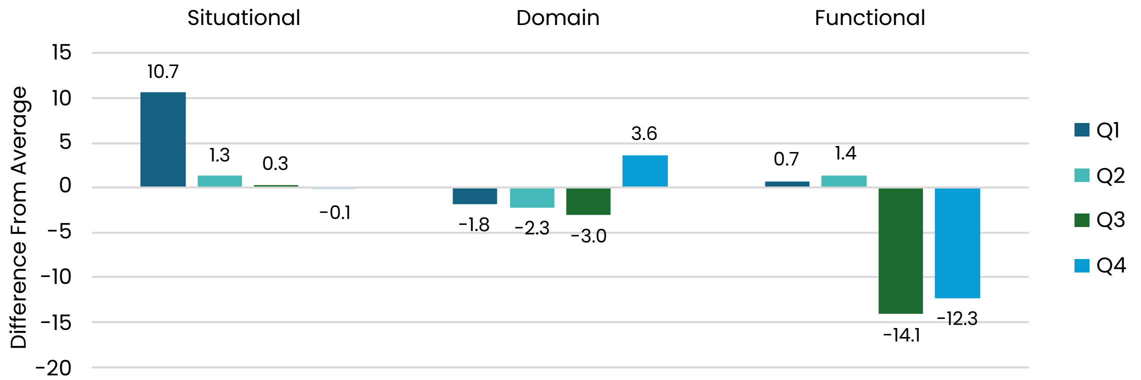
Emerging C-suite roles

A wave of emerging leadership roles also highlights how the best performing businesses are thinking laterally about the impact executives can have on value creation priorities in the current economic climate. Amongst business exiting in the last 12 months, we see a growing focus on roles outside the standard C-suite 'template', including M&A Directors, CHROs, Executive Chairs, and specialist technology leaders. As with other areas of business, leadership roles and responsibilities are constantly evolving, and those who innovate are at an advantage.

Difference in experience profile by quartile in FY23/24



Difference in Experience Profile by Quartile from FY22/23



3. Building a top quartile leadership team

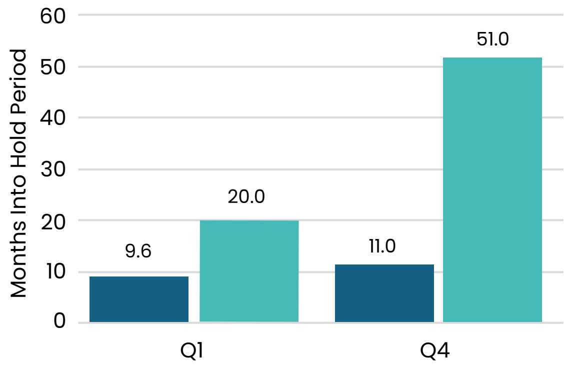
We know that top quartile businesses prioritise Leadership Capital to achieve growth. But how do factors such as leadership change, board composition, founder succession, and interim talent contribute to exit performance?

How do top performing businesses optimise their board?

- **Top quartile businesses made an average of 9.7 changes throughout the hold period, 21% more than the poorest performers**
- **Volume of leadership change doubled since last year's report**

Building a well-balanced leadership team that is aligned with the value creation plan is a key growth lever for private equity investors, particularly when faced with an uncertain market. Our findings reveal that top performing businesses have been even more proactive in optimising their leadership team in recent years, making more change, making change faster, and prioritising roles that will drive growth.

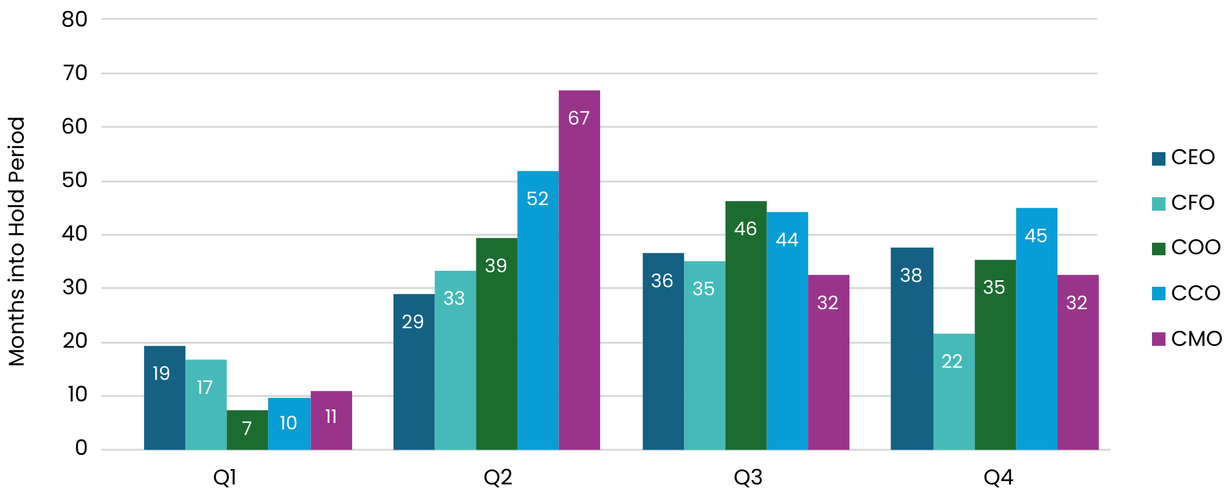
Year on year comparison of leadership change timings



Top performers made the most leadership changes
Of those businesses that exited in the last 12 months, top quartile performers made an average of 9.7 changes to their C-suite during the investment period, in contrast to 8 changes seen in less successful counterparts.

Once again, we see that making more leadership change is positively correlated with performance, indicating a greater agility and willingness to adapt to new challenges and opportunities. Making more change enables companies to bring in functional leaders that will aid the growth of the business, as well as change leadership that is underperforming.

Average of core leadership timings by quartile



- Early leadership change linked to best exit returns
- Top performing businesses change core C-suite roles within the first 18 - 24 months

Top performers make changes faster
Not only do top performers make more change they also make changes faster, within 9.6 months, as opposed to 11 months for those in the lower quartile. This trend is even more pronounced when looking at the core C-suite roles, CEO, CFO, COO and CCO, with top performing businesses making all these hires within the first 18 - 24 months of the hold period.

This suggests that top performers strategically plan their leadership transitions to ensure alignment with their growth objectives, and a faster response time provides a critical advantage, allowing these businesses to swiftly realign their strategies and drive performance. It also gives new leaders, and the combined team, more time to have a greater impact on the company and its growth objectives.

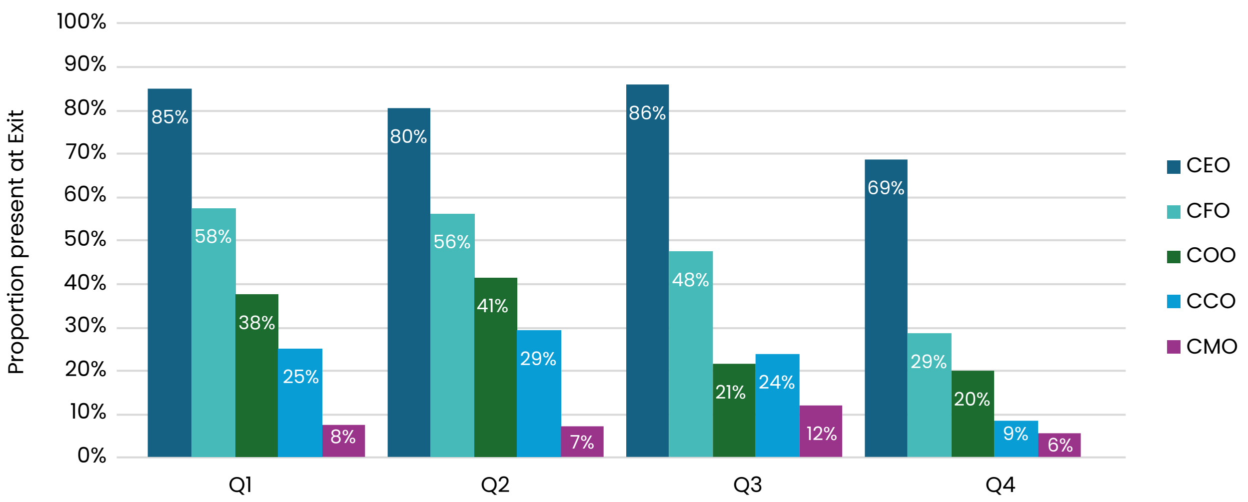
Frequent adjustments help maintain momentum
Top quartile businesses also show a trend of making frequent leadership adjustments into the second and third years, allowing them to stay agile and adapt to new challenges and opportunities as they arise.

Lower performers suffer impact of delayed change

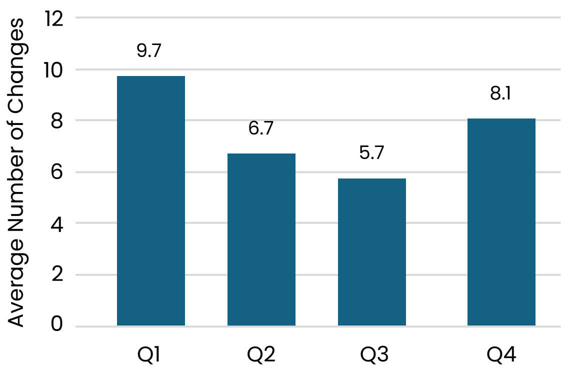
In contrast, lower-performing companies (Q4) tend to make a lower proportion of changes to core C-suite roles, and often later within the hold period.

This reactive approach suggests a reluctance or inability to proactively align leadership with evolving business needs, impacting their overall performance.

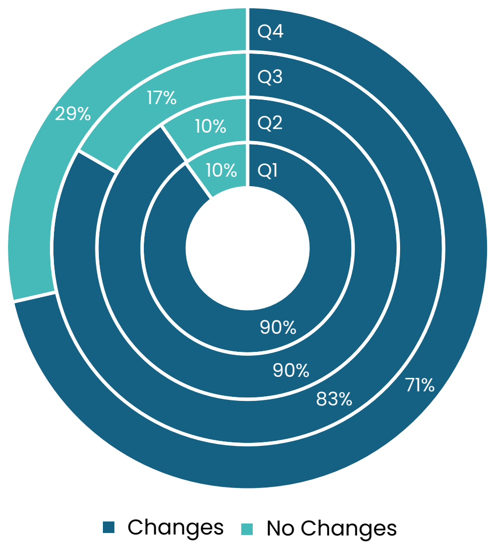
Proportion of core leadership roles present at exit by quartile



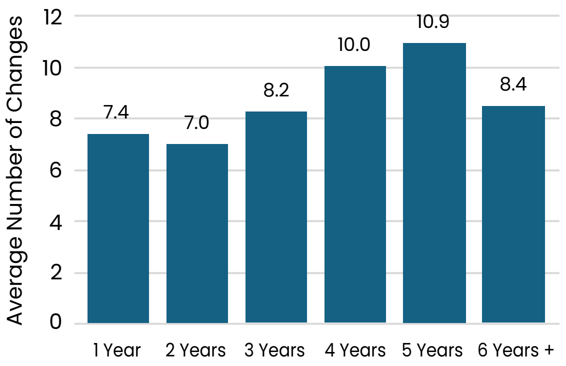
Q1 Companies make more changes to C-Suite



Better performing businesses are more likely to make leadership changes



A high proportion of Leadership change occurred later into the hold period on average

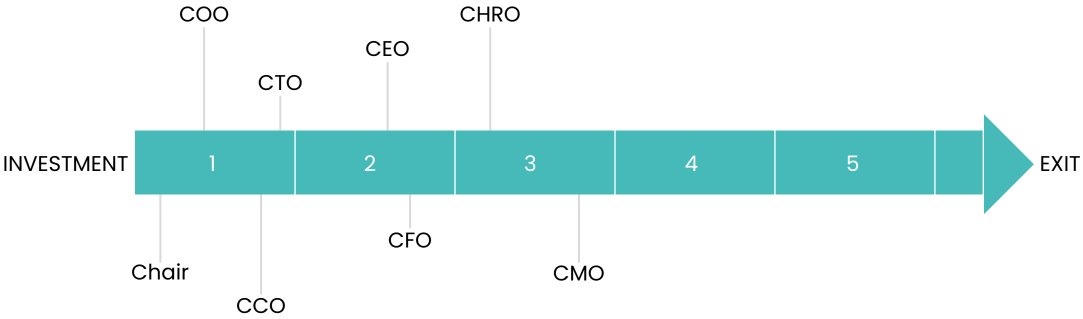


Leadership team evolution

Top quartile vs. bottom quartile businesses

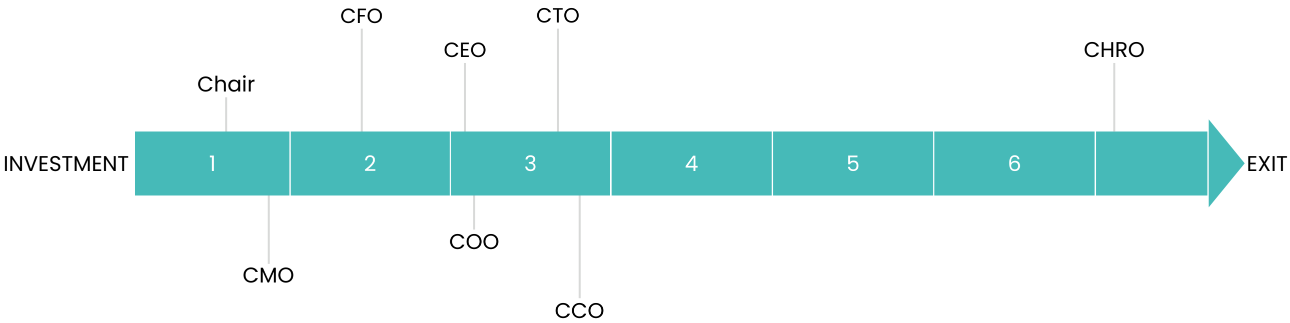
Stronger performing leadership change through the investment period

Average investment time = 5.3 years



Lower performing leadership change through the investment period

Average investment time = 6.7 years



The leadership change sequence in higher-performing businesses highlights several ways that they are optimising leadership more effectively than lower performing businesses.

Firstly, the investment hold period for higher-performing businesses is significantly shorter, averaging 5.3 years, compared to 6.7 years for lower-performing businesses. This shorter period indicates a more efficient path to achieving investment goals and preparing for a successful exit, highlighting the importance of having the right leadership team in place as early as possible.

Here we can see that the best performers...

Made change earlier, reflecting a proactive approach to leadership transitions.

Made early CEO change, so new leadership could drive the company's vision and strategic initiatives effectively, setting the tone and direction for the entire organisation. In contrast, a delay can indicate a prolonged period of ineffective leadership, contributing to subpar performance.

Made early COO change to optimise operational efficiency from the start, indicating a focus on achieving quick wins in productivity and efficiency. In lower performing businesses, COO changes happen later and frequently followed CEO changes, reflecting deeper challenges within the operational framework.

Switched CFO sooner to optimise financial management, ensuring robust financial health, and better resource allocation. Better performing businesses also frequently followed CEO changes with CFO appointments, indicating a focus on financial stability and oversight during transitions.

Made CMO change later once operational and commercial roles were settled. Early CMO change in lower-performing businesses indicates an initial attempt to boost market performance and customer engagement, without putting the right foundations in place first.

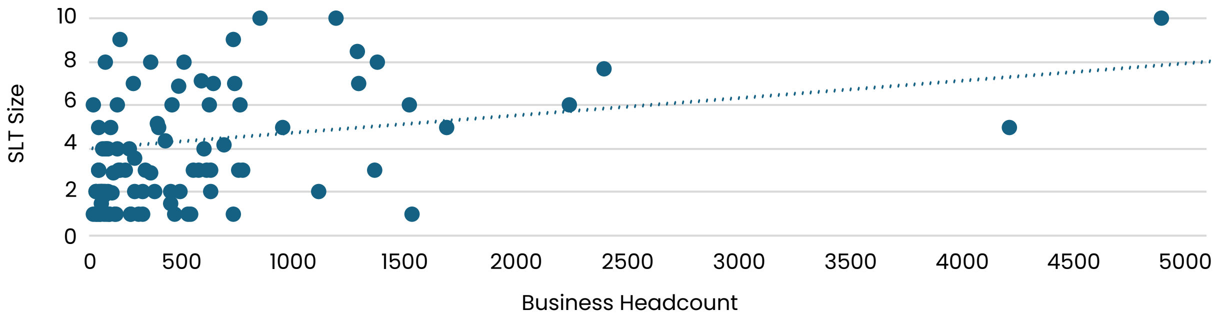
Optimised the CCO earlier to enhance commercial strategies and strengthen client relationships, which are essential for driving early revenue growth. A later CCO change, as we see in lower performing businesses, suggests a need to address earlier operational and strategic misalignments.

Give the CHRO time to make an impact by introducing them mid-way through the hold period. Notably, in lower performing businesses, the CHRO change occured near the end of the investment period, perhaps to address cultural and talent management issues that have hindered performance.

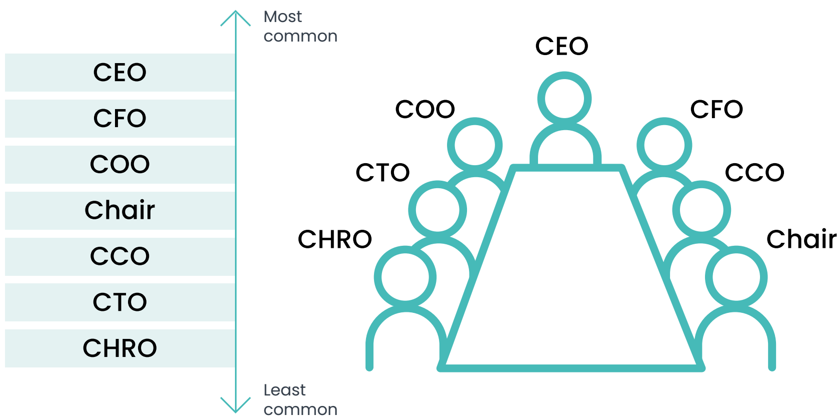
Around the boardroom table

While every PE-backed leadership team is unique, our analysis highlights some interesting patterns in the size and composition of teams across different quartiles. Here we visualise the modal structure (i.e. the structure that occurs most frequently) of leadership teams within each quartile, to demonstrate where the top performers may be gaining an edge. However, it's worth bearing in mind there will be numerous variations on these, depending on the business size, sector and priorities.

The SLT size positively relates to the organisation's scale



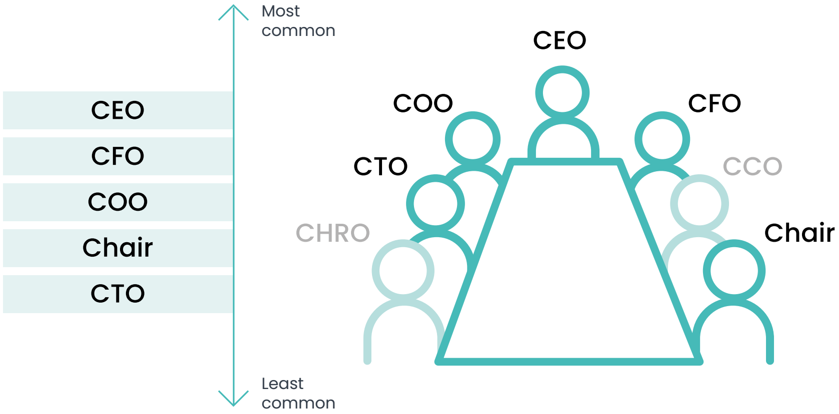
Q1



Average size of SLT at exit = 6.8

- The best-performing businesses are characterised by a larger and more dynamic C-suite, suggesting a more robust leadership structure contributes to business success.
- Top performing businesses are also more likely to have core C-suite roles filled at the time of exit.
- Where is the CMO? In fact, CMO was the eighth most common role, just outside the model top-quartile leadership team.

Q2

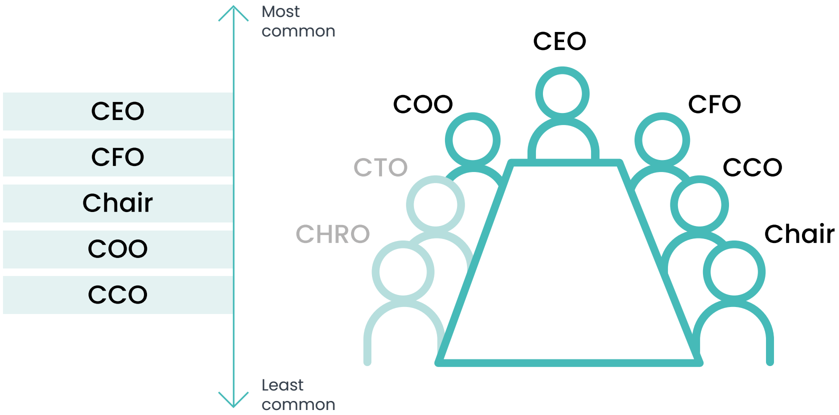


Average size of SLT at exit = 4.9

- More than half of upper and second quartile businesses (58% and 56%) have a CFO at exit, compared to just 29% of lower quartile businesses.
- Around a quarter of top-performing companies (Q1 & Q2) have a CCO at exit (25% and 29%) compared to only 9% of the lowest-performing companies (Q4). CCO sits just outside the average second quartile team.

Modal SLT composition

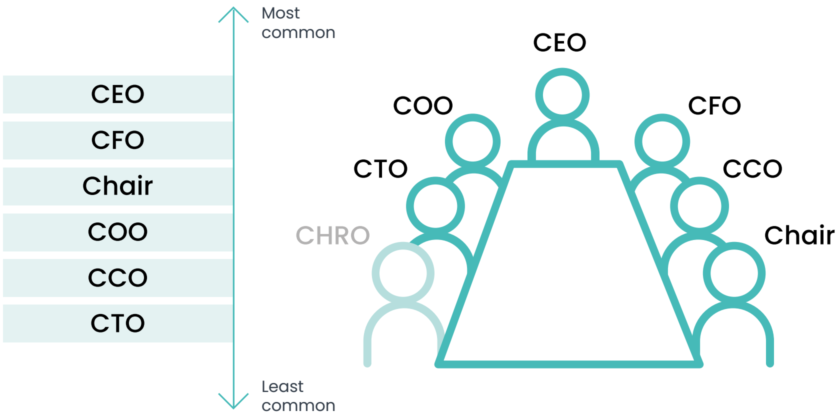
Q3



Average size of SLT at exit = 4.4

- Companies in the top and second quartile (Q2) are almost twice as likely to exit with a COO; 37% of top quartile and 41% of second quartile companies, compared to only 21% of third and 20% of bottom quartile companies.

Q4



Average size of SLT at exit = 6.0

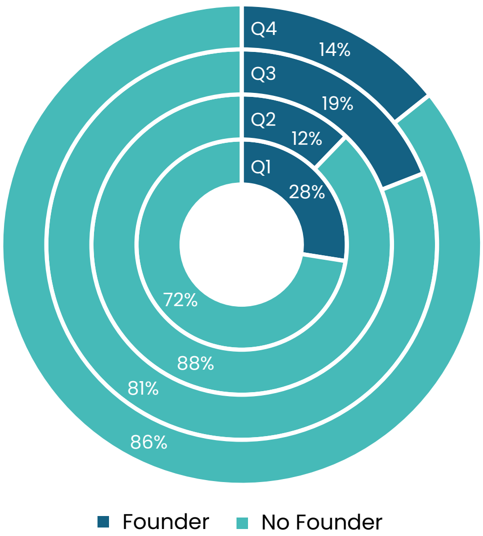
- The lowest performers have the second largest leadership teams on average. In this instance, performance could, in fact, be compromised by the size of the leadership team, if the CEO lacks the capability to manage a large team, or the composition or competencies of the team are misaligned, making it more challenging to manage.

Founder succession: supporting a visionary leader

- **Top performing founder-led businesses have large leadership teams, with an average of 7.5 leaders**
- **Upper quartile founder-led businesses make more leadership change, and make change faster**
- **Best performers prioritise situational and domain expertise over C-suite experience**

Founder-led businesses bring a combination of benefits and challenges for private equity investors. On the one-hand, founders invariably provide unrivalled vision and leadership for a fast-growing business, along with deep understanding of the market. Their value is demonstrated by the fact that top quartile businesses are twice as likely to exit with a founder in place than those in the bottom quartile (28% vs. 14%).

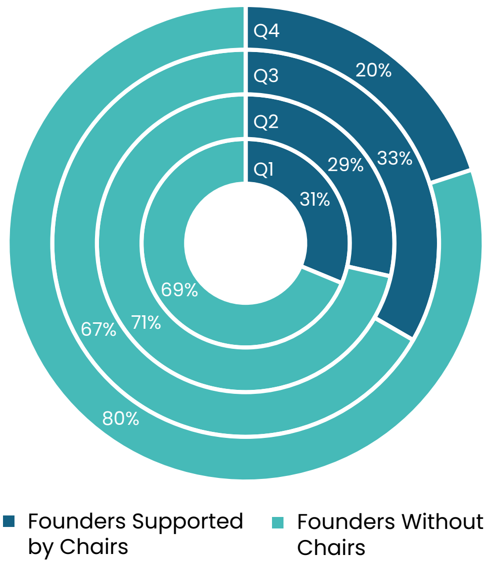
Q1 businesses were twice as likely to exit with a founder than Q4



However, overreliance on a charismatic leader can present risks to business continuity, and performance, when they inevitably want to take a step back. It is rare for a founder to have the skills needed to lead a business as it scales, which means careful planning to build a well-balanced, cognitively diverse team around them, which also complements and gels with the founder on a behavioural level.

Founder-led businesses that perform well are often supported by Chairs who play a crucial, yet complementary role. Acting as a strategic sounding board for the founder, Chairs provide valuable experience that helps navigate market complexities and ensure alignment with long-term value creation objectives. In high-performing companies, this relationship fosters more robust decision-making, particularly around leadership, as Chairs offer a stabilising influence during periods of uncertainty. By leveraging their expertise, Chairs enable founders to remain visionary while grounding them with the governance and strategic ballast needed to successfully scale the business.

Founder-led businesses supported by Chairs experienced stronger exits



How do the best performing founder-led businesses approach leadership change and succession planning?

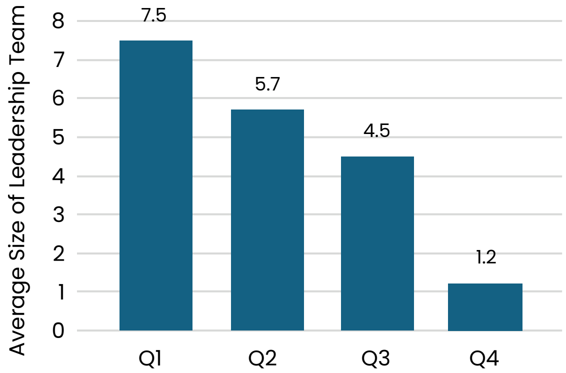
Best founders make more leadership change, make change sooner, and build larger leadership teams

For founder-led businesses looking to scale, building a balanced, high performing leadership team around the founder is vital. We can see that the best performing businesses do this in three ways:

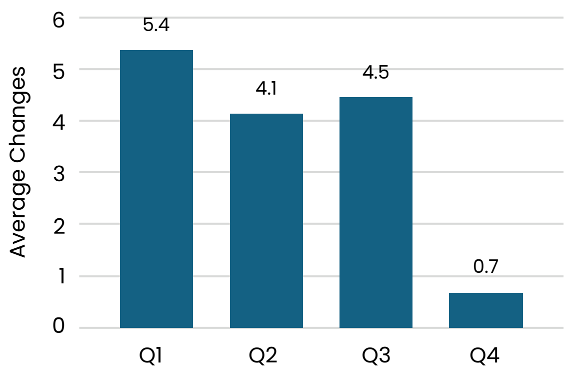
- They have larger leadership teams, with an average of 7.5 executives, compared to just 1.2 for the poorest performing founder-led businesses. This suggests a focus on a flatter, less hierarchical structure, incorporating a wider variety of functional roles.
- They make more leadership change throughout the hold period, averaging 5.4 compared to just 0.7 in the poorest performers.
- They make change faster, waiting just over six months to make their initial leadership change, compared to nearly a year for bottom quartile businesses.

This indicates that the best founder-led businesses aren't only bringing in leaders at the right time but thinking ahead by hiring required competencies ahead of time. This ensures the team has time to test what competencies work alongside the founder, while affording them the capacity and experience to address specific challenges and opportunities as they arise, rather than hiring in a more reactive way that could slow growth.

Better performing founder-led businesses have larger leadership teams



Better performing founder-led businesses make more changes



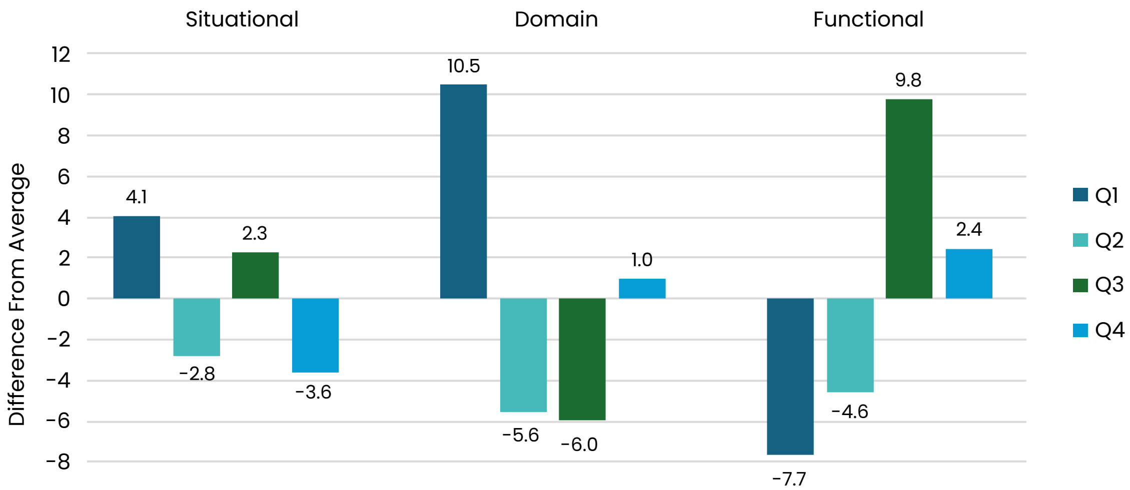
It's worth noting that business scale also plays a role in the breadth of the leadership team, with size of business positively correlated with the size of the SLT.

In contrast, lower quartile performers are on average focused on a limited range of expertise, while just 20% lower quartile founders are supported by a chair, which could be hindering their ability to adapt.

Best founders prioritise situational and market expertise over C-suite experience

Alongside filling functional gaps, founders must ensure new leaders have complementary skills and competencies and align with where the business is in its growth journey. Founder-led businesses are unlikely to be ready for corporate-level experience, instead requiring leaders who can combine strategic competencies with the ability to be hands on when necessary.

Better performing founder-led businesses prioritise situational and domain experience when they develop their teams

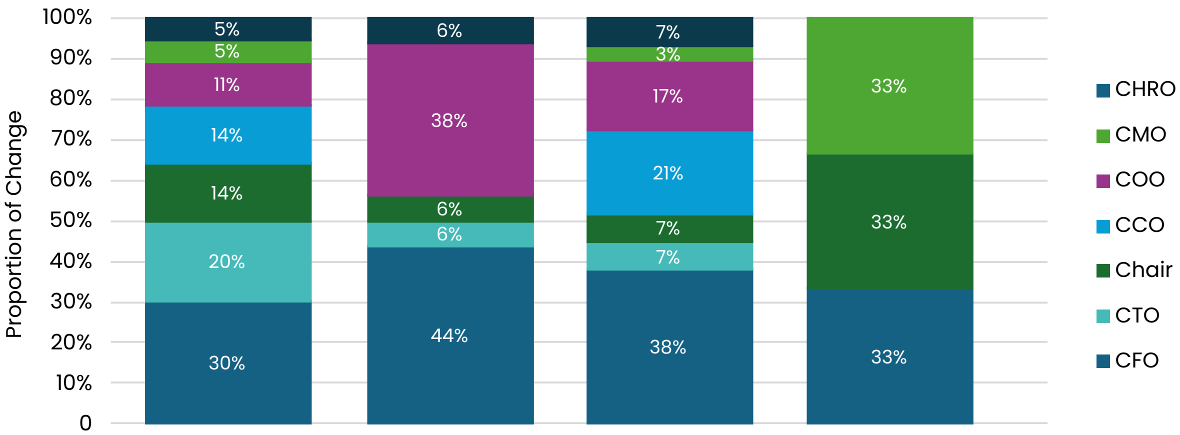


We see this play out in the competencies that top performing founders prioritise, which focus on a combination of situational experience and domain expertise, as opposed to functional C-suite experience. This trade-off is often considered worthwhile, as market and journey experience enables the company to stay agile and responsive to market dynamics, even if it means foregoing some of the broader experience traditional C-suite executives might offer.

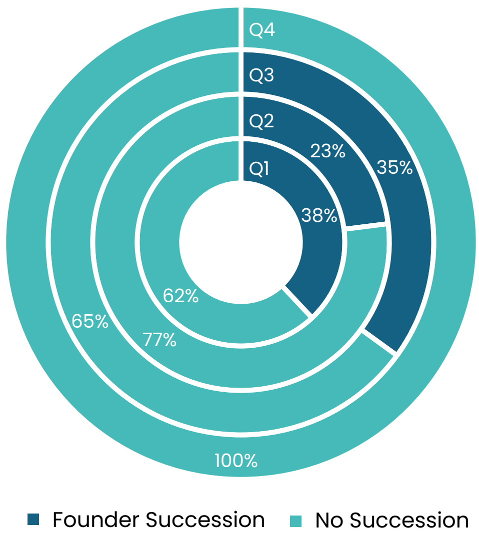
What does it take to replace a founder?

Top performing founders consider broader functional needs
Founders often wear many hats, so for them to take a step back, or plan to leave the business, several functional heads will usually be needed to fill the gaps they leave behind. Hiring patterns show that the most successful founders have this in mind when expanding their team, with hires in the top quartile spanning six C-suite roles, and a third of top quartile founders (31%) introducing a chair to ease this transition.

Better performing founder-led businesses make changes according to the business needs



Better performing businesses are more likely to have accounted for founder succession



- **Worst performers neglect founder succession planning**
- **Founder successors have strong situational and functional competencies, but less domain experience**

Founder succession vital to performance
Given the valuable role that founders play in business success, planning for their succession is vital to ensure their growth trajectory can be sustained going forward.

Founders in PE-backed businesses typically undergo a transition through multiple rounds of investment, with a high proportion remaining in place from primary to tertiary stages. However, by the fourth round, founders have commonly exited the operational leadership and may transition into Non-Executive Director or Chair roles. When this happens, the right CEO must be ready to take over.

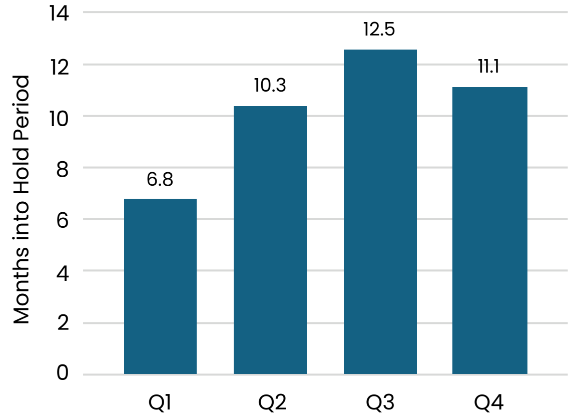
We can see that top-performing businesses exhibit a more proactive approach to founder succession planning, with 38% having a succession plan in place, compared to none in the lowest quartile. However, given the high proportion of all businesses lacking a plan for founder succession, there is a significant opportunity to improve business resilience across even the best performing businesses.

Top performers prioritise situational and functional experience in successors
Replacing a founder isn't easy, so what competencies are the best performers looking for when they choose a new CEO to take over?

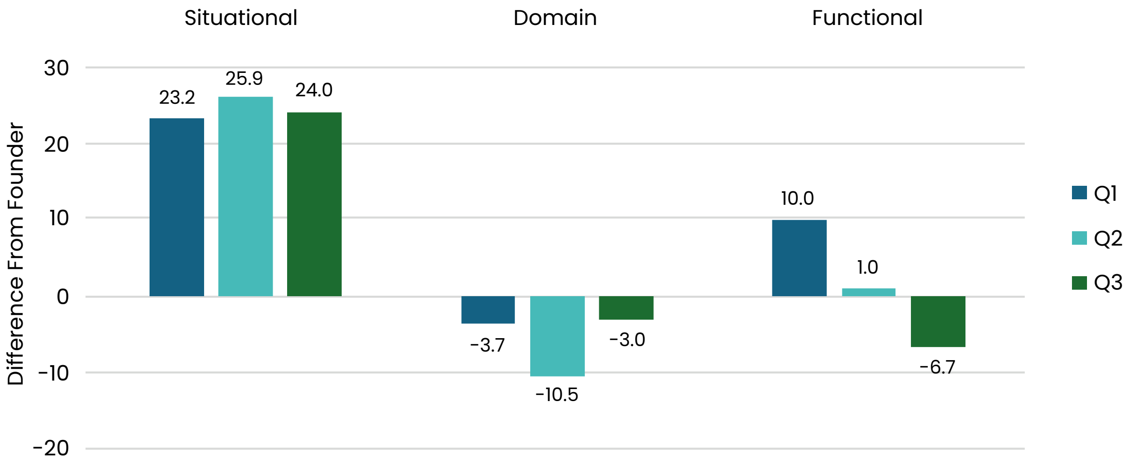
We can see through our analysis that successful successors to founders typically possess extremely strong situational experience, along with robust functional experience, although they may have less domain expertise compared to the founder.

The lower domain expertise of successors compared to founders is not surprising, given the founder's intimate familiarity with the business environment and industry nuances, which has enabled them to establish a strong market presence. Successful founder successors leverage this foundation while bringing strong experience of the growth strategy that aligns with the company's evolving needs and growth objectives.

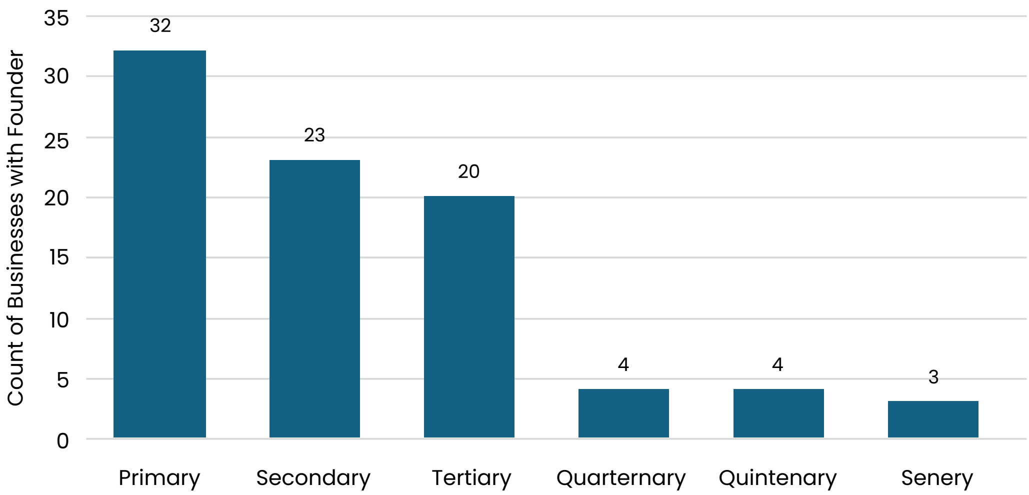
Average Time into hold before initial change to leadership team



Founders are succeeded by individuals with strong situational experience



Founders are likely to have exited the business after their third round of investment



Interim leaders: powering business turnarounds and specialist impact

- **Lower performing businesses more reliant on interim leaders for course correction**
- **Top performing businesses primarily use interims in the CFO position**
- **Interims can also be a catalyst for short-term impact within specific business functions**

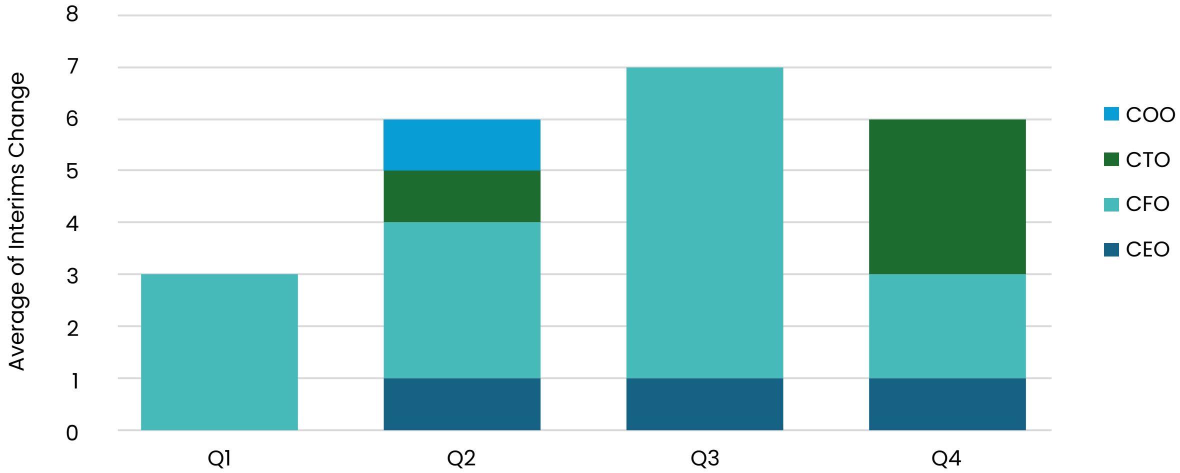
PE-backed businesses are operating within a defined timeframe, which means the majority of executive roles could arguably be described as 'interim.' Nonetheless, specialist interim executives fulfil a valuable role within investors' leadership toolkit. When leveraged effectively, they ensure businesses avoid gaps in key functional positions, provide stability, a specialist expertise, and can help turnaround struggling businesses.

Bankruptcies hit a 30-year high this year in the UK, meaning more businesses were struggling to come back from the brink. In many cases, interim leaders were pivotal to helping them do so.

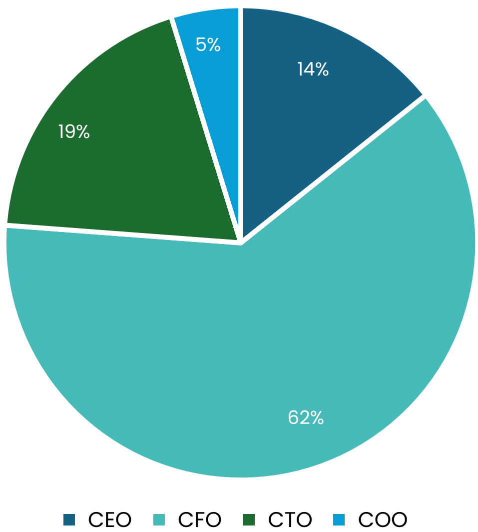
Lower performers rely more on interims – across a wider range of roles

Third and fourth quartile businesses were twice as likely to hire interim leaders as top performers, demonstrating the key role they can play in sustaining these businesses throughout turbulent periods and getting them back on track. As well as using more interims, these businesses (Q4) were also more likely to appoint them across a range of C-suite roles, including CEOs, CTOs, and CFOs.

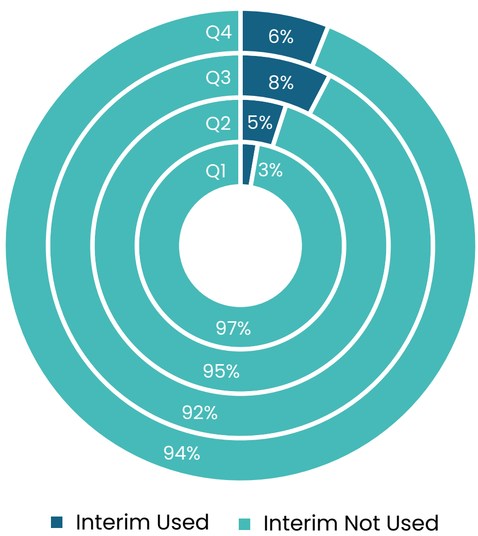
Lower performing businesses more likely to bring in interim leaders



CFO is the most common type of interim used



Lower performing businesses are more likely to use interim leaders during the hold period



CFOs are the most common interim

Amongst all businesses, CFOs were the most common type of interim, representing two thirds (62%) of appointments, highlighting the critical role of financial management in business continuity and investor confidence. CTO was the second most common interim hire, particularly amongst the poorest performing businesses, indicating challenges in digital transformation and technological change, which needed a fresh perspective.

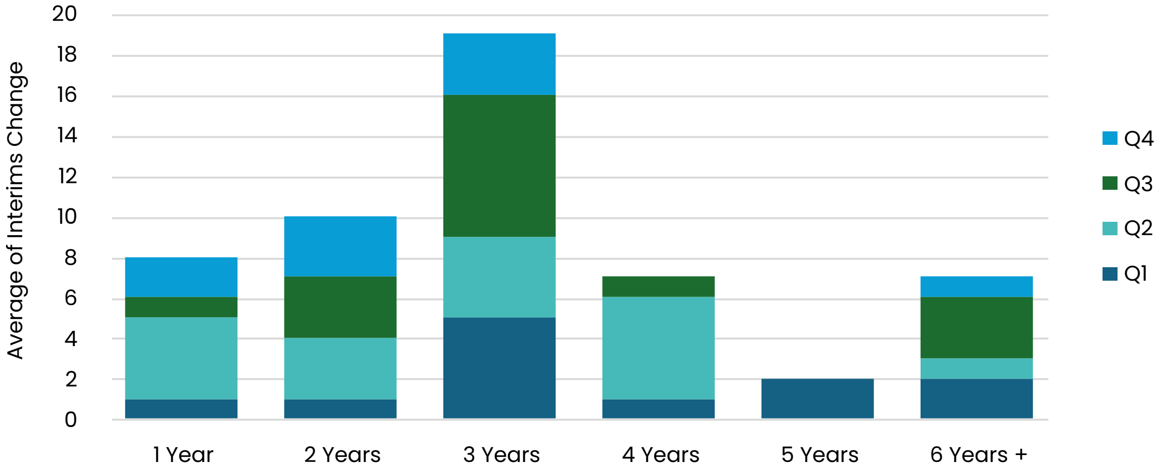
Lower performers rely on interims late in hold period

Overall, interims are mostly introduced in the middle of the hold period (three years in) to manage periods of change; an intervention that can be crucial for stabilising the business and addressing immediate challenges. However, lower-performing businesses (Q3 and Q4) show a higher likelihood of using interims in the latter years, again highlighting the 'firefighting' nature of the role, and its importance for securing a buyer for these companies, despite poorer performance.

Interim impact

While the most common use-case for interims is to orchestrate business turnarounds in struggling businesses, the breadth of interim hires deployed within second quartile businesses suggests they also have a role in unlocking growth and transformation, often earlier in the hold period. In this case, an interim would usually be appointed due to their specialist capability - operational, commercial, technological, or people - and the role is akin to an in-house consultant tasked with unlocking growth and performance in a specific business area.

Majority of interims are brought in mid cycle to manage periods of change

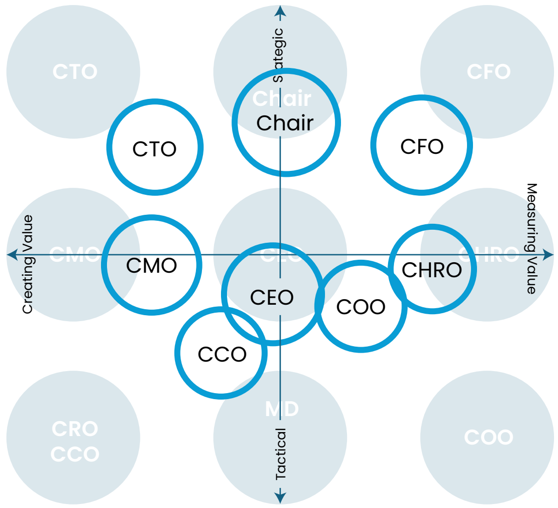


4. Optimising leadership performance through insights

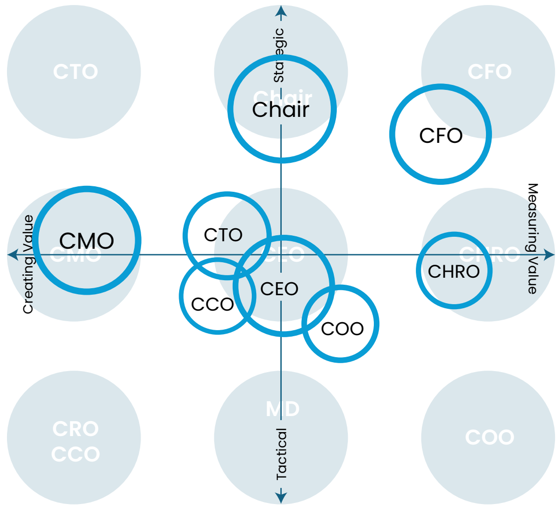
The right balance of competencies, behaviours and cognitive diversity is vital for a high performing leadership team. What characteristics differentiate top quartile businesses?

Functional balance

Typical upper quartile team functional balance



Typical lower quartile team functional balance



- **Balance and role clarity marks out upper quartile businesses**
- **Commercial CEOs supported by strong functional leaders**
- **Best performers have a strong functional CTO**

Leadership structure can be assessed by looking at the functional balance of leadership teams and how this correlates with performance. The leadership balance chart visualises a team based on depth of experience within key functional roles, and how it aligns with the value creation plan and the team's ability to deliver it.

The location of an individual on the chart represents whether they create or measure value, and whether they are more strategic or tactical. Each position is designed to reflect the archetype of the specific role, based on real leadership team data. The bubble size represents how much experience that individual has within their function.

Balance and role clarity marks out upper quartile businesses
Overall, upper quartile companies exhibit a greater balance across their leadership teams, with clearer delineation of roles, highlighting a more strategic and comprehensive approach to executive responsibilities and decision-making.

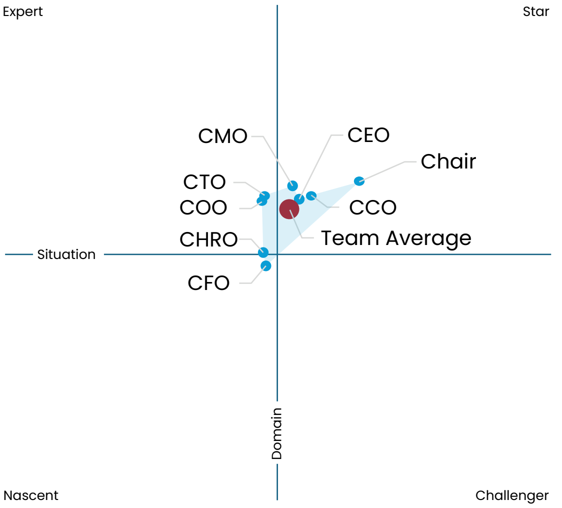
Commercial CEOs supported by strong functional leaders
CEOs in these top-performing firms often come from commercial backgrounds, bringing market-oriented thinking that drives growth and innovation. These CEOs are supported by robust strategic leaders with functional depth across various roles, creating a well-rounded executive team. They are also supported by a more tactical CCO with greater commercial focus.

Strong functional CTO
CTOs in the upper quartile significantly contribute to technological innovation and strategic initiatives, with a strong functional depth. These leaders are instrumental in leveraging technology to drive business transformation and competitive positioning. In lower quartile companies, CTOs are displaced from their archetypical location with a greater impetus on tactical objectives, indicating a reduced functional depth and therefore lessened impact on technological advancements.

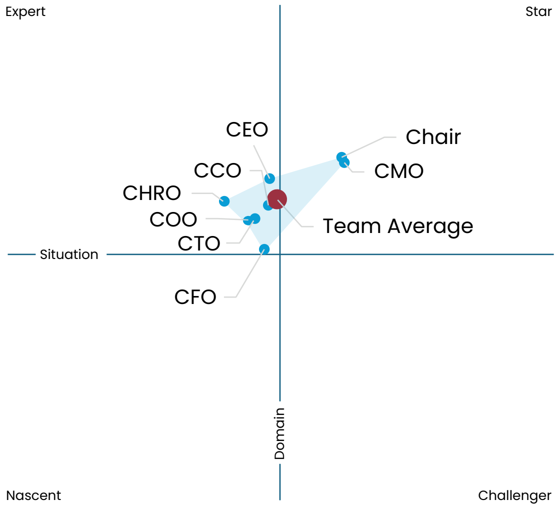
Poorer performers lack breadth of experience
In contrast, lower quartile companies show more nascent leadership structures, with a tightly clustered executive team centered around the CEO, who typically has a stronger operational background. This operational focus indicates a narrower scope of expertise and potential for less value creation and innovation. The leadership in these firms tends to lack the breadth of experience seen in their upper quartile counterparts, limiting their strategic capabilities. Interestingly, lower quartile performers have a strong functional CMO, again suggesting an outsized external focus, without the necessary foundations to back it up.

Balancing domain and situational competencies

Typical upper quartile experience profile



Typical lower quartile experience profile



- **Upper quartile teams boast several 'star' leaders, providing value creation expertise**
- **Lower quartile teams over-reliant on 'star' Chair**

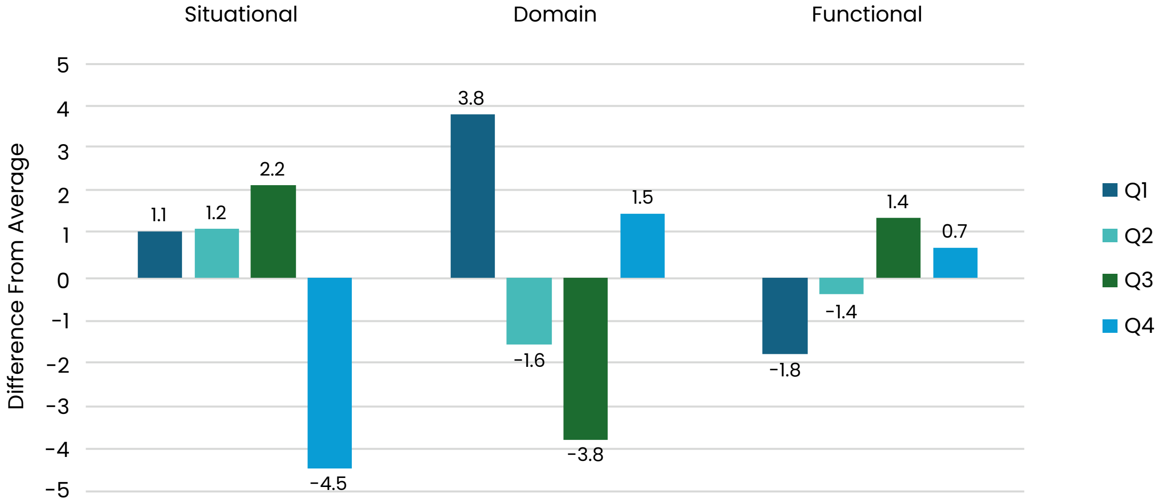
The leadership positioning chart is where we can evaluate the domain (market) and situational experience of each leader, and the team, against the business's value creation strategy. This enables us to see how a leadership team can deliver against the investment hypothesis.

Ideally, a team should have a good balance of expertise across the Challenger, Expert and Star quadrants to provide a range of perspectives and capabilities.

While at first glance the upper and lower quartile charts look similar, some key differences set apart top performers:

- Upper quartile leadership teams are positioned more to the right of the chart in the star quadrant, indicating several leaders with a strong combination of domain and situational experience.
- They are joined by experts and challengers in key roles such as COO and CTO, providing valuable diversity across the team.
- Amongst the strongest performers, we see a strong Chair reinforced with a strong CEO, both of whom bring deep knowledge in how to deliver on growth objectives. The CEO is also positioned in the middle of the other team members, suggesting they can effectively bring all the experience together.
- In contrast, lower performers are positioned closer together in the centre and left side of the chart, indicating a narrower range of perspectives and competencies.
- Lower performers demonstrate an over-reliance on a strong Chair for experience of the value creation plan, rather than a depth of expertise on how best to deliver growth. These teams are also dominated by market over situational knowledge.

Difference in experience profile by quartile



- **Upper quartile businesses prioritise domain and situational expertise**
- **Rise in upper quartile domain experience could be driven by demands of pandemic**
- **Lower quartile leadership teams lack value creation experience**

Upper quartile businesses prioritise domain and situational expertise

Higher-performing businesses tend to bring in leaders with strong domain experience and robust situational experience. These leaders are typically better equipped to align their teams with the company's vision, optimise operations, and exploit market opportunities, all of which contribute to higher equity value at exit.

Importance of domain experience could be driven by pandemic demands

This year's cohort of top performing businesses have leadership teams with particularly strong domain experience, suggesting the pandemic period may have put a premium on deep market understanding and squeezing margins at a difficult time.

Poorest performing businesses neglect situational experience

Leadership in lower-performing businesses typically has significantly less situational experience compared to higher-performing teams. This suggests that investors in these businesses are more focused on hiring junior talent moving through the ranks, rather than looking externally for the ideal mix of competencies. As a result, they are at a disadvantage in understanding how to execute an ambitious growth plan and could see the performance of the team and business compromised as a result.

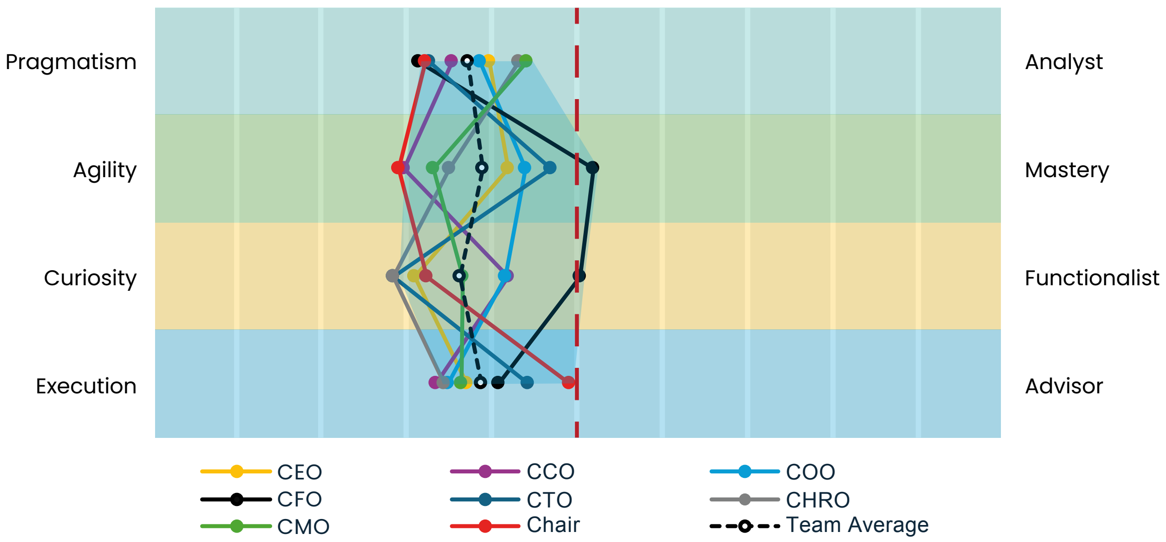
Four leadership behaviours drive performance

PACE (Pragmatism, Agility, Curiosity and Execution) is the leading private equity behavioural evaluation, which allows high-performing leaders to understand their strengths, weaknesses, and how they will interact as a team. It is the only behavioural evaluation designed for the unique leadership demands of venture, private and growth capital.

Each leader has an individual PACE profile, which is mapped alongside their colleagues to assess areas of complementarity, overlap or misalignment. This enables us to predict how they will perform together and the likelihood of successfully delivering the value creation plan.

Our previous analysis has found that the best performing teams demonstrate balance and cognitive diversity across their PACE profiles. Assessing teams against this template enables us to minimise the chance of groupthink, which can impact decision-making, creativity, and risk management.

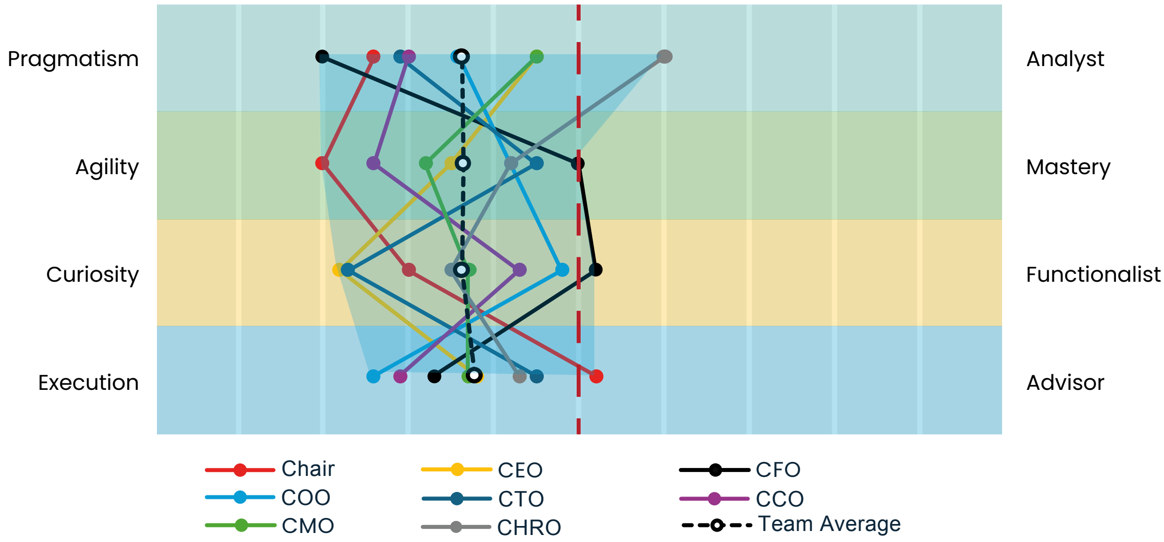
Lower performing businesses show lower diversity within their behaviours



In lower quartile teams, clusters and areas of concentration indicate lower cognitive and behavioural diversity, which can be indicative of groupthink. In the above example, there is a greater concentration within pragmatism, telling us this team is keen to get stuck into the delivery of a strategy, though may forge ahead too quickly to be efficient. Consequently, they may need to pause and assess how their plans will be effective in the long-term and account for potential obstacles on their growth journey.

This would be particularly so if combined with lower situational experience. Collectively this team demonstrates balanced (or mid) agility, telling us that, as a team, they have a mixed blend of growth and fixed mindsets. Those with more fixed mindsets (mastery) tend to be specialists in a particular area, though may be reluctant to learn outside their specialism. This can be additive in some businesses and less so in others, depending on situation and role requirements.

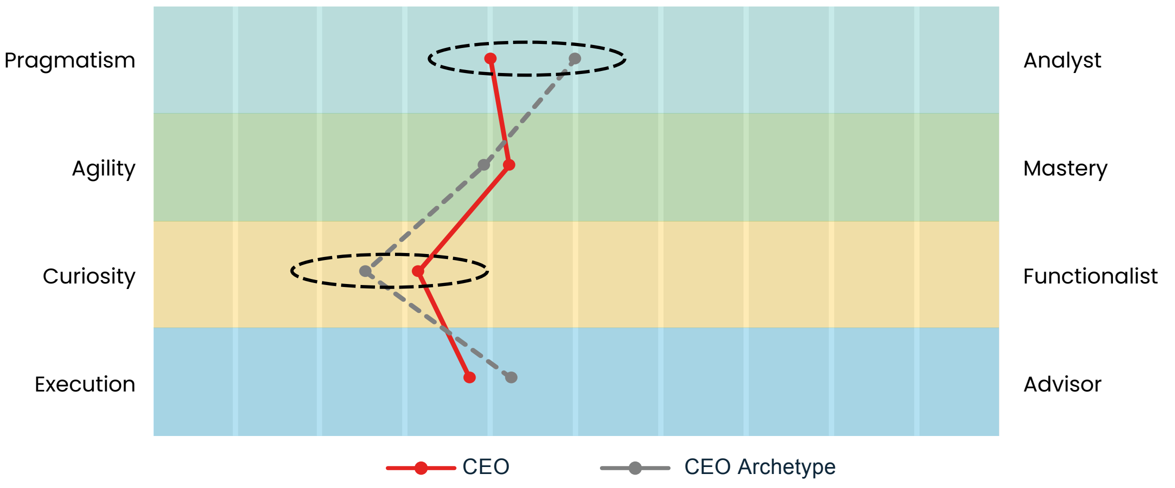
Top performing businesses show behavioural diversity with greater preferential behaviours



Clear variance and balance within upper quartile PACE behaviours point to a higher level of cognitive diversity within the team. Contrasting approaches and constructive challenge will lead to innovative solutions and well-rounded plans for growth, accounting for potential roadblocks. The CEO shows strong curiosity which indicates they provide innovative growth solutions, while the COO's more functionalist approach is well placed to alter current business processes to enable this change. Different perspectives on execution across the team will be influenced by their role type, providing a balanced approach overall.

Can leaders develop PACE behaviours to aid performance?

Can leaders develop PACE behaviours to aid performance?



Given that better performing businesses tend to exhibit greater cognitive diversity across the leadership team, it begs the question: Can leadership teams that do not exhibit this diversity in their thinking and behaviours change or develop their behavioural preferences?

Behaviours can be learned – by some

Traditional psychometric assessments, such as Myers-Briggs and Hogan categorise leaders into fixed leadership types, which can miss the nuances of behavioural variations. PACE is different as it allows us to address specific business behaviours that characterise personality traits, and, over time, some of these are more malleable than others.

However, the likelihood of changing or developing a behaviour also depends on the individual. For example, those with a strong outcome motivation are more likely to learn from their surroundings and adapt to improve performance. Similarly, proactive individuals with clear personal agency will actively look to change their behaviours to best suit their leadership role. For those without these traits, altering their behaviour will be harder.

Given the correlation between behavioural diversity and performance, lower performing businesses could therefore aim to hire leaders with the ability to adapt how they behave. This could help compensate for competency gaps, enhancing leaders' potential for successful value creation.

Gender diversity: a tale of action and inaction

- **Women represent fewer than one in five PE-backed leaders at the time of business exit**
- **Female leadership decreases during the hold period, across all quartiles**
- **Yet, a sub-set of businesses appear to be prioritising gender diversity**

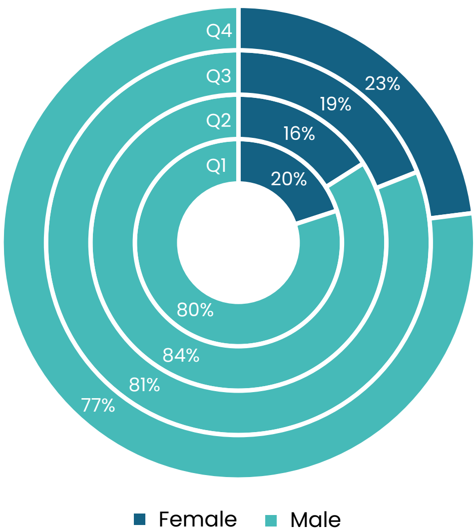
Gender diversity at the executive level is not just a matter of social equity but also business efficacy and performance. Numerous studies have shown that diverse boards and leadership teams can enhance decision-making, foster creative solutions, and mirror the gender composition of customer and employee bases.

We know that achieving gender diversity in leadership is a longstanding issue across all types of businesses, although figures for private equity-backed companies have often been hard to come by. Here we provide a detailed examination of the rates of female executives across various functions, and the implications for the PE sector and corporate governance.

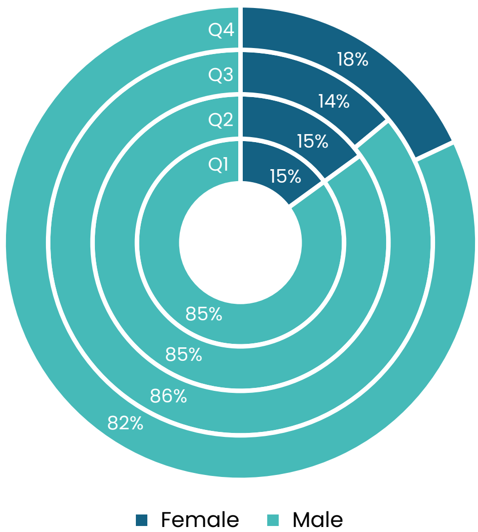
Women make up less than a fifth of executives at time of exit

The figures reveal a stark disparity in the representation of women in key executive roles. In the UK's PE-backed marketplace, women represent a mere 17% of all executives at the point of exit, compared to 23.3% across the general business landscape*. This highlights the persistent gender inequality that exists in high-stakes, high-impact positions.

Gender differences at start

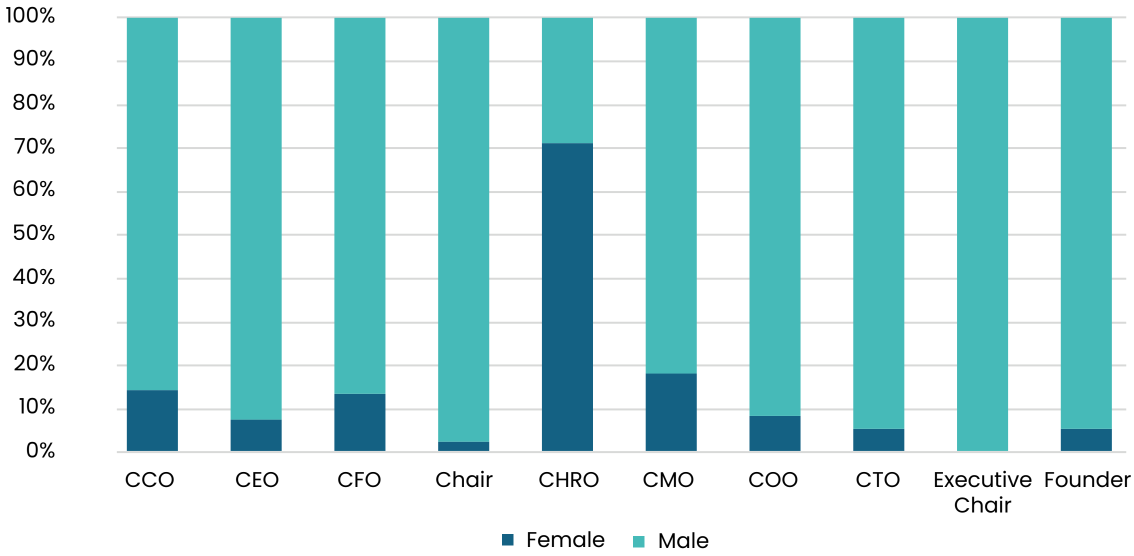


Gender differences at exit



* Deloitte Women in the Boardroom Report 2024

Gender split by role



When disaggregating this data by role, the disparities become even more pronounced:

- **Chairs:** Only 2% of chairs are female, translating to a ratio of one in fifty. Given the chair's critical role in setting strategic direction and overseeing the entire board's function, this is particularly concerning.
- **CEOs:** The most pivotal role for shaping the company's culture, strategy, and financial success has only 7% female representation.
- **CFOs:** Women hold 13% of CFO positions, or one in eight. Although slightly better compared to other roles, the CFO's crucial influence on financial stewardship and strategic fiscal planning remains predominantly male.
- **Technology leaders:** Only 5% of technology leaders are women, approximately one in twenty. This underrepresentation is significant given the critical role of technology in driving innovation and future-proofing businesses.
- **Revenue and marketing leaders:** These roles have a relatively higher representation at 16% female, or one in six. Nonetheless, this still reflects a significant gap in leadership in customer engagement roles.
- **HR leaders:** The only function where women are significantly represented, holding 71% of these positions, or three quarters. This suggests traditional gender role stereotyping continues to influence career paths. Interestingly, this figure is still lower than the general business average which stands at 78%*.
- **Operations leaders:** Operational leadership, which is crucial for overseeing daily business functions, sees only 8% of female participation, or one in twelve.

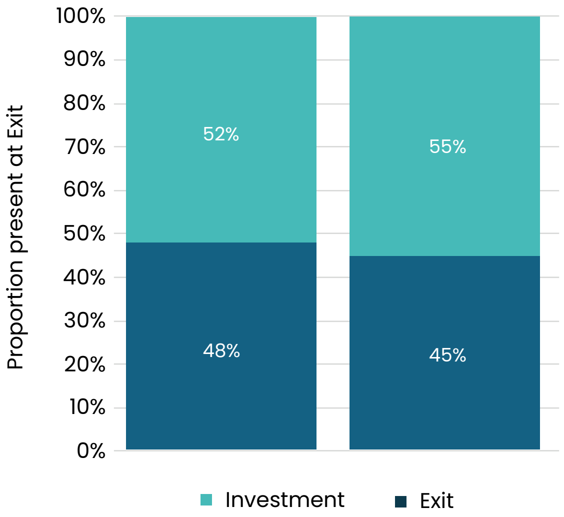
* CHRO Trends Report: It's the Year of the Female - TalentQ (talent-quarterly.com)

Portfolio diversity

Female leadership decreases during the hold period
Also, concerningly, across all quartiles, the proportion of female leadership is lower at the point of exit than it was at the point of investment. In top quartile businesses, the proportion of female leaders dropped five percentage points (20% to 15%) from investment to exit, with a similar drop across other quartiles. Further analysis indicates this is driven by more males than females being hired during the hold period; 80% of new hires were male.

One explanation for this could be businesses seeking leaders with prior private equity experience during turbulent conditions. As female leaders often join PE-backed businesses from outside the usual talent pool, and via a diverse search process, a failure to look beyond the 'tried and tested' could have exacerbated the lack of diversity for this cohort of exiting businesses.

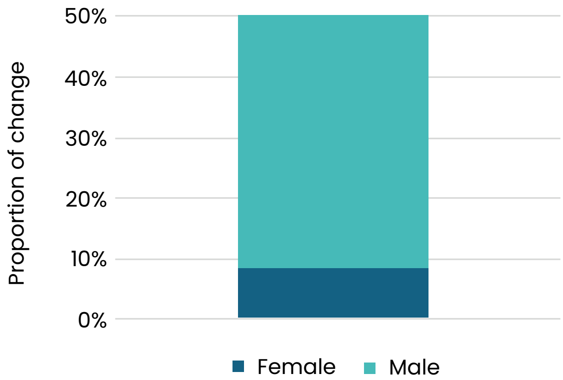
Proportion of fully male boards at point of Investment and exit



Sub-set of gender diversity trailblazers
On a more positive note, there is evidence of a notable subset of businesses where gender diversity appears to be more actively promoted. Among businesses with at least one female C-suite member, 45% had two or more, representing 30% of the C-suite team.

This suggests that gender diversity within PE-backed organisations is a tale of both progress and stagnation, with some companies making strides towards greater female representation in executive roles. These trailblazers are benefitting from a greater level of cognitive diversity, with positive impacts for decision-making, innovation, oversight, and even financial results. A more concerted effort is needed to replicate this more widely across the industry.

Females only accounted for 8% of the collective C-Suite growth throughout the investment journey



5. Emerging leadership roles

Shifting business priorities demand new leadership roles and responsibilities. Is the balance of power shifting on PE-backed boards?

Rise of high impact chair

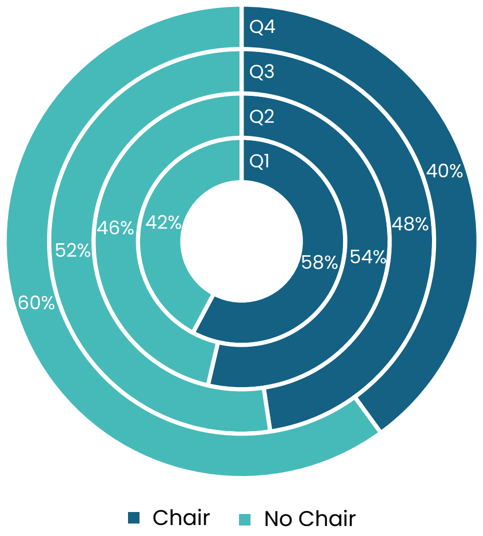
- Best performing businesses exit with a chair and/or NEDs in place
- Market and journey (situational) expertise more important than 'plural' or functional experience
- Chair change is driving impact throughout the hold period, not just at the outset

The pandemic and post-pandemic period has had a huge influence on what is expected from private equity-backed chairs and NEDs, as rapidly changing markets put greater demands on their time and expertise. Here we see that the presence of a chair and/or NED on the board is strongly correlated with top performing exits. However, just having a chair or NED is not enough; it must be the right individual, with experience and competencies that align with the value creation plan and complement the wider leadership team.

Better performing businesses exit with a chair and/or NEDs in place

The data reveals a clear trend: better-performing businesses exiting the PE market are more likely to have seasoned chairs and NEDs in place. In the last 12 months, over half of top and second quartile businesses exited with a chair or NED in place, compared to just 40% of the poorest performing businesses.

Q1 businesses more likely to exit with Chair or NED in situ



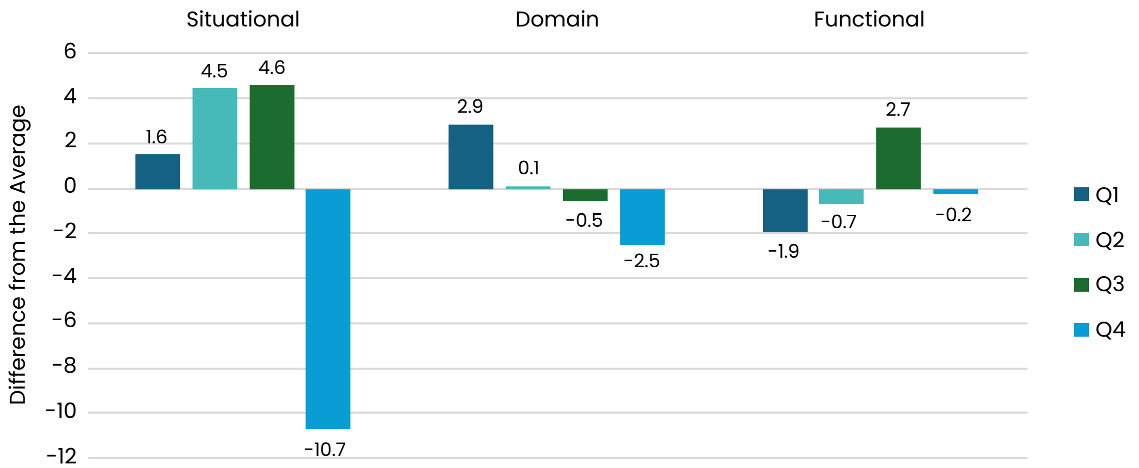
Most effective chairs and NEDs are market and growth specialists

Furthermore, the difference in experience between chairs and NEDs of top performing versus bottom quartile businesses is stark. Effective chairs and NEDs in successful firms typically possess extensive industry-specific knowledge and a proven track record in executing growth plans successfully.

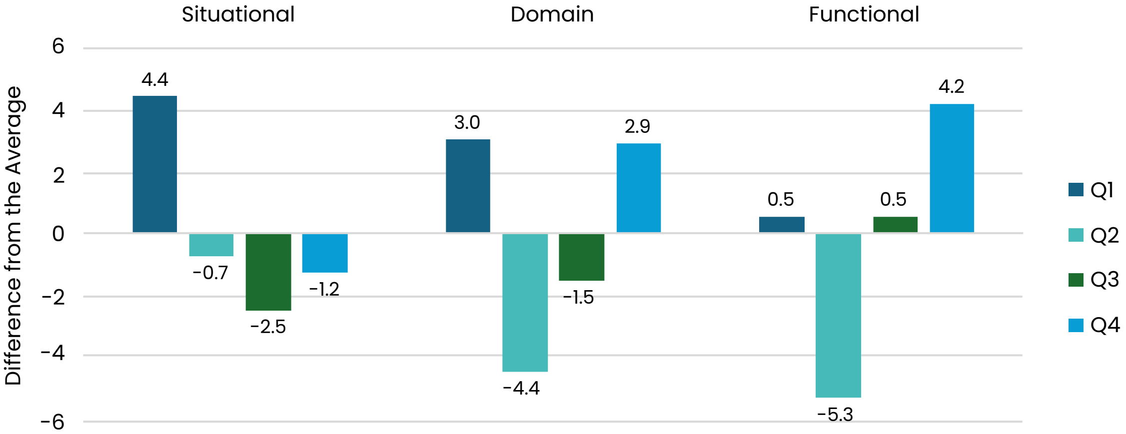
This expertise enables them to provide nuanced guidance, anticipate market trends, and make informed decisions that drive sustainable growth for the portfolio company. With lower functional experience, they may have less chair experience than the average, indicating a history of plural roles is not essential.

In contrast, chairs and NEDs in lower-performing businesses often lack comparable depth of domain and situational experience, especially the latter. This deficit can limit their effectiveness in providing strategic direction to enable execution of the business goals and hinder their ability to foresee potential obstacles the business may encounter.

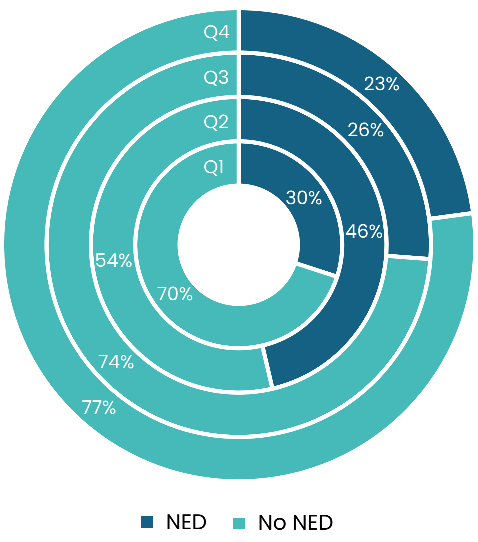
Best Chairs have stronger situational and domain experience than average



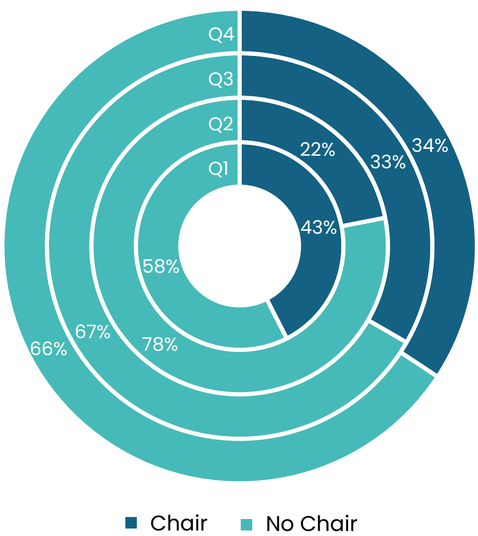
Q1 NEDs have stronger situational experience whereas Q4 have greater domain and functional experience



Best performing businesses are more likely to utilise a NED



25% more Q1 businesses had a Chair at Eexit

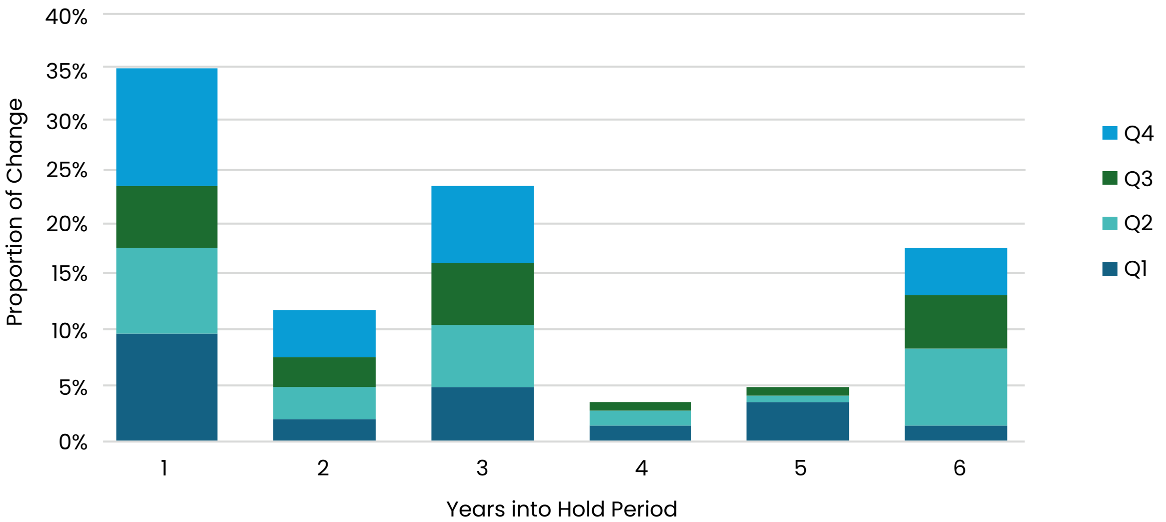


Chair change is driving impact throughout the hold period

Chairs have traditionally been brought into PE-backed businesses at the outset of the hold period, when they can best influence strategic planning. However, this year's findings suggest investors are increasingly looking to optimise chairs throughout the hold period, as a way to maximise their impact on value creation. Here, we see three distinct spikes in chair changes in PE-backed businesses:

- Over a third are made in the first year, to align the board with the strategic vision set by the PE firm and management team.
- There is another spike in year three of the hold period, when nearly a quarter of chair changes are made. This is driven by the need to adapt to evolving market conditions, operational challenges, or strategic shifts within the portfolio company.
- Finally, around a fifth of chair changes happen six years into the hold period, when investors and leadership teams are often focused on preparing the company for exit. PE firms may seek to strengthen the board with individuals experienced in navigating exit processes, negotiating with buyers, and maximising shareholder value.

Chairs are brought in early, middle and late in the hold period

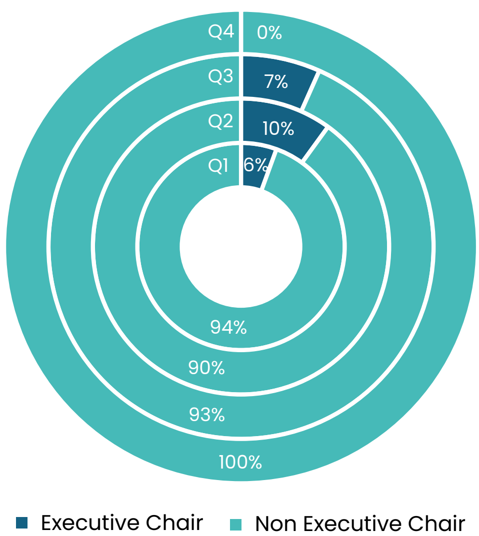


Best performing businesses leverage executive chairs

For the first time this year, we analyse the use of executive chairs in PE-backed businesses, to assess how these more hands-on chairs are being used by businesses across performance quartiles. What we see is that it is the better performing businesses that are utilising these executives; 16% of upper and second quartile businesses did so, compared to just 7% of businesses in the bottom two quartiles.

This suggests that better performing businesses use executive chairs to manage periods of turbulence within the business and its leadership, for example to mitigate CEO exits, and manage CEO transitional periods. In contrast, lower performers were more likely to resort to interim CEOs to perform this function, providing a temporary figure head for the business through periods of leadership change, although less leadership continuity is a result.

Q4 businesses did not use Executive Chairs During the hold period



M&A directors emerge as buy-and-build picks up pace

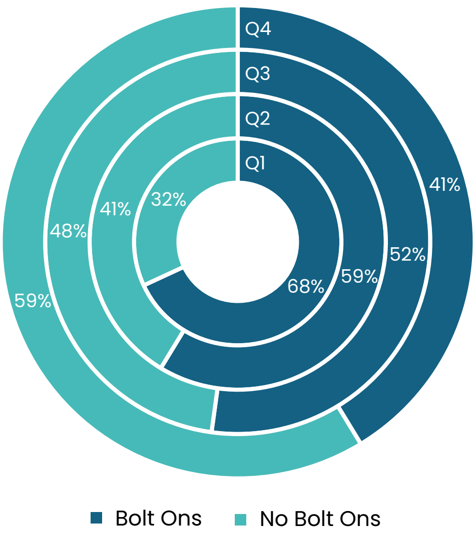
- **Two thirds of top quartile businesses (68%) make bolt on acquisitions, compared to 41% of the lowest quartile**
- **A quarter of top performing businesses have an M&A Director and one in eight (12%) of the second quartile**
- **M&A directors excel for market knowledge over situational and functional expertise**

This year, for the first time, our analysis encompasses leaders in corporate development and M&A, who play a pivotal role in driving inorganic growth through buy-and-build. In the current market, bolt-on acquisitions can be a highly effective growth lever, where organic growth has slowed, and valuations are depressed, opening opportunities for consolidation. M&A and corporate development roles provide the bandwidth to leadership teams to pursue, and squeeze maximum value, from these strategies.

Yet, as the M&A Director role is in its infancy, we are just starting to develop a clearer picture of its focus, where it sits in the organisation, and how businesses can leverage these leaders to deliver maximum value.

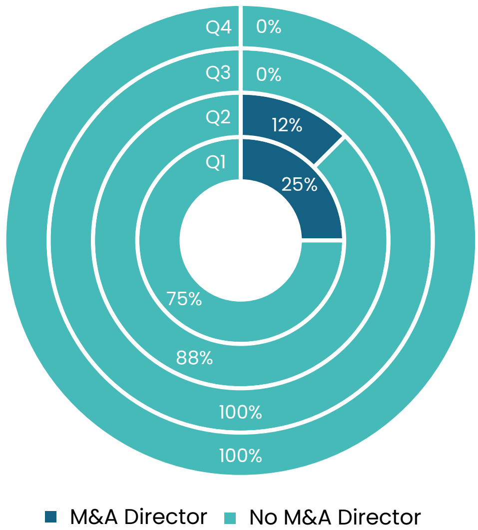
Top performing businesses execute more bolt-ons
As you might expect, it is the best performing businesses that are making the most bolt-on acquisitions; 68% of this year's businesses did so. Nonetheless, a relatively high proportion of poorer performing businesses are also attempting to expand through bolt-ons, including 41% of those in the bottom quartile. This suggests that businesses across the board would benefit from a leader in this function to maximise the success of these transactions.

Q1 business more likely to make bolt on acquisitions



A quarter of top performing businesses have an M&A Director
Despite a wide variety of businesses pursuing M&A, our findings show that M&A directors are only found in the best performing businesses at present. One in four top quartile businesses have an M&A director in place, along with one in eight of those in the second quartile. In contrast, none of the businesses in the bottom two quartiles are yet leveraging the potential of this role for developing and executing an acquisition strategy.

Businesses making more acquisitions are more likely to have an M&A Director

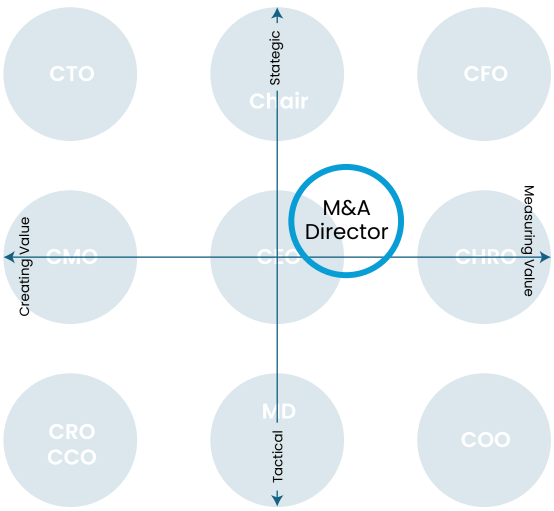


M&A directors are more junior, but bring strong domain expertise

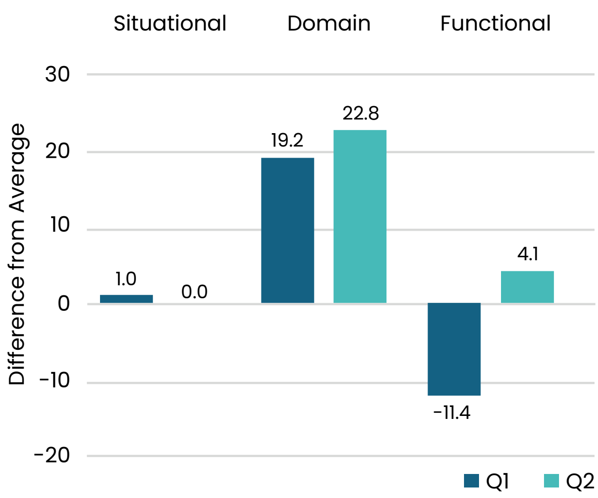
The experience profile of M&A and corporate development directors suggests that they are generally more junior professionals, who lack the situational experience of some of their leadership peers. Similarly, as this is a fledgling role, they also have less functional M&A leadership experience, as other leaders may have in their functional area. However, where they do excel is in their knowledge of the market, which positions them strongly to seek out the most attractive targets for M&A, understand where there is business alignment, and have the contacts to scope out and execute deals successfully.

On the functional balance chart, M&A Directors sit next to the CEO archetype, however with a greater focus on strategy and measuring value. This suggests that their value comes from a combination of market knowledge and strategic insight into the financial and people factors that contribute to the success of a deal.

Average corporate development /M&A Director profile



M&A Directors are typically more junior but have strong domain expertise



CHROs prove their value in the boardroom

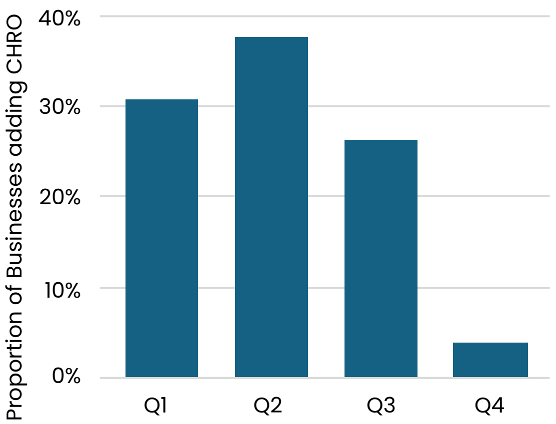
- **One in three of the best performers hire a CHRO during the hold period**
- **Better performing businesses twice as likely to have a CHRO at exit**
- **CHRO combines dual role as people head and leadership team curator**

Historically, CHROs have been a relative rarity in PE-backed leadership teams, however, as organic growth, employee engagement, and leadership optimisation move up the agenda, that is now changing. Better-performing businesses increasingly see the value of a CHRO to help build a focused, engaged and productive workforce, to deliver the change and growth required in a defined timescale. But equally as important is the CHRO's pivotal role as custodian of the leadership team and succession planning. This dual role is part of the reason why the CHRO is a key differentiator for better performing PE-backed businesses.

A third of best performers hire a CHRO

Their pivotal role as an architect of people, employee engagement, and team dynamics is why around a third of the best performing businesses (30% of upper quartile and 37% of second quartile) added a CHRO to their team at some point during the hold period. This compares to a quarter of third quartile businesses and just 5% of the poorest performers, suggesting their presence translates into better team performance and ultimately, superior business outcomes.

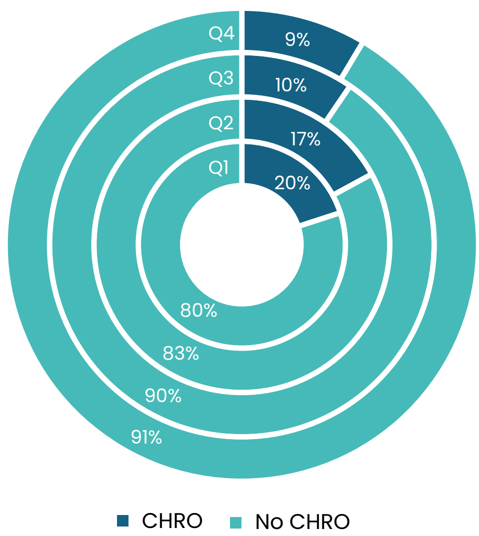
Better performing businesses are more likely to add a CHRO to their team



Top performers twice as likely to have a CHRO at time of exit

According to our data, the presence of a Chief Human Resources Officer (CHRO) correlates significantly with company performance. Top quartile performers are twice as likely to have a CHRO at the time of exit; 20% for upper quartile businesses compared to just 9% of those in the lower quartile. However, given that only one in five top performers have a CHRO in place, this shows there is still significant scope to maximise the potential of this role.

Q1 companies more likely to exit with CHRO

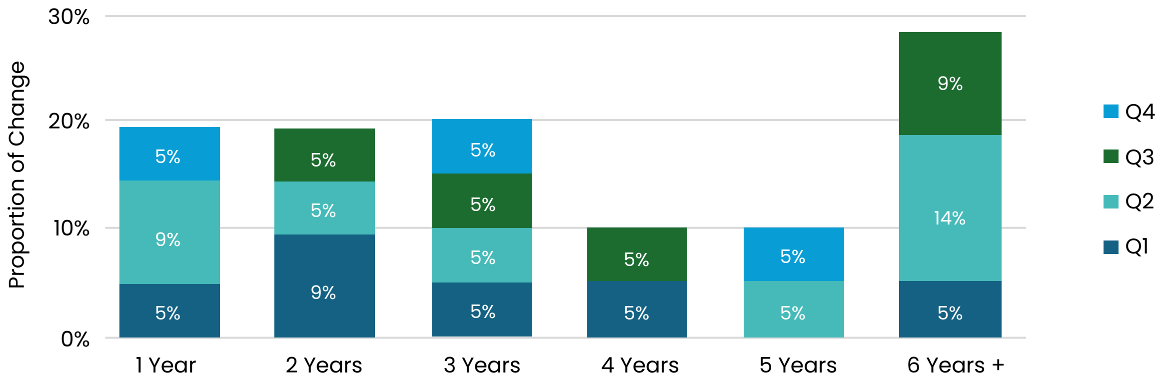


Upper and second quartile businesses make CHRO changes sooner

The best performing companies tend to make CHRO changes earlier, with over a quarter of Q1 and Q2 companies (28%) doing so within the first two years.

Bringing a CHRO in early in the hold period can bring huge value in putting the right talent and engagement strategies in place, while also providing strategic insight and guidance into the development of the leadership team itself.

Better performing Businesses make changes to their CHRO earlier

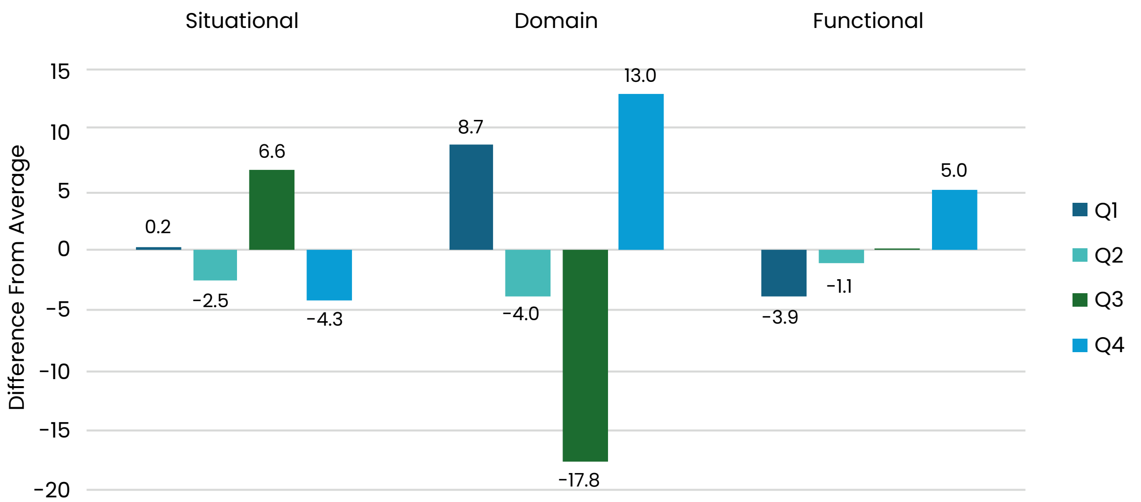


CHROs excel in domain experience

CHROs in top performing businesses stand out due to their high level of domain experience combined with strong situational experience, but less functional HR expertise. The high level of domain experience aligns with a trend seen across several leadership roles, most likely driven by a market in which difficulties delivering value have sparked a need to double down on understanding the customer and how to attract, retain and engage talent within that sector.

The experience profile of top performers also suggests these businesses are hiring people leaders from outside the organisation, with varied situational experience, rather than promoting talent internally. In contrast, looking at CHROs in the bottom quartile businesses, their high domain and high functional experience suggests that they have been within the organisation for a long time and worked their way up the ranks, limiting their range of experiences.

Upper quartile CHROs excel in domain knowledge paired with strong situational experience



The strategic role of tech leaders in better performing companies

"Technology is critical at every level of the business world, and strategic IT leadership ensures companies keep up with the blistering pace of change. The breadth and complexity of tech leadership roles now reflects a dynamic and vibrant market, but it's important to remember that job titles should always come secondary to ensuring a leader's competencies and experience meet the unique needs of each business. An early-stage venture has vastly different IT leadership needs to a global corporation, which has vastly different needs to a mid-market services business. So, while job roles provide a guide on expertise and experience, the real value comes from identifying the best leader, or leaders, for each business's size, scale, sector and growth ambitions."

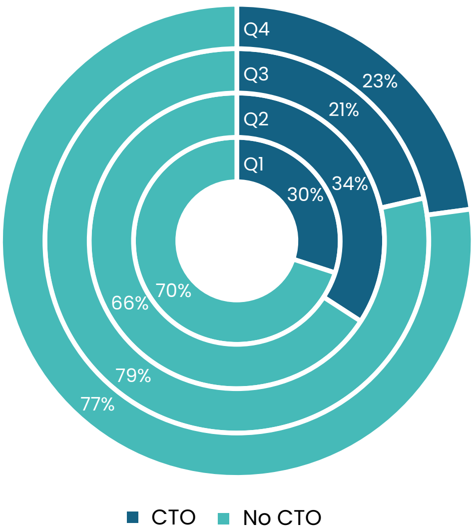
Duncan Finlayson, Chief Exec & Co-founder, Drax Affinity

As technology has become critical to driving efficiency, business growth and differentiation, tech leadership has not only become a vital part of PE-backed leadership teams, but the demands of the role have become increasingly multi-dimensional and diverse. How are better-performing businesses leveraging technology leaders compared to their less successful counterparts?

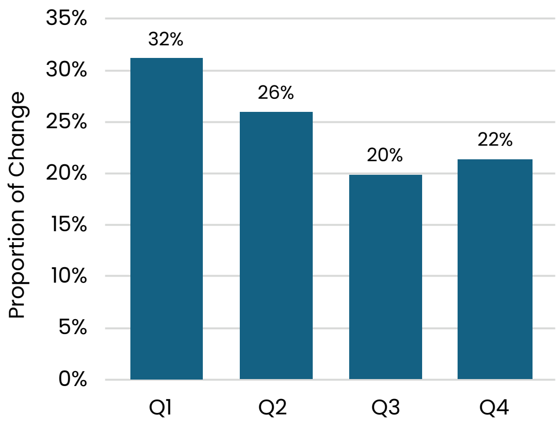
Best performers more likely to hire a tech leader and have one on exit

Data shows that a third of top-performing companies (30%) and second-tier performers (34%) have a tech leader on the C-suite at the time of exit, compared to around a fifth of third and fourth quartile performers (21% and 23%). Furthermore, 32% of upper quartile businesses hired or changed a tech leader during the hold period, compared to just 22% of the bottom quartile. This trend suggests dedicated technology leadership is a hallmark of successful companies, potentially due to the strategic oversight and innovation they bring to the table.

Better performing companies have a CTO at exit



Better performing businesses make more CTO Changes

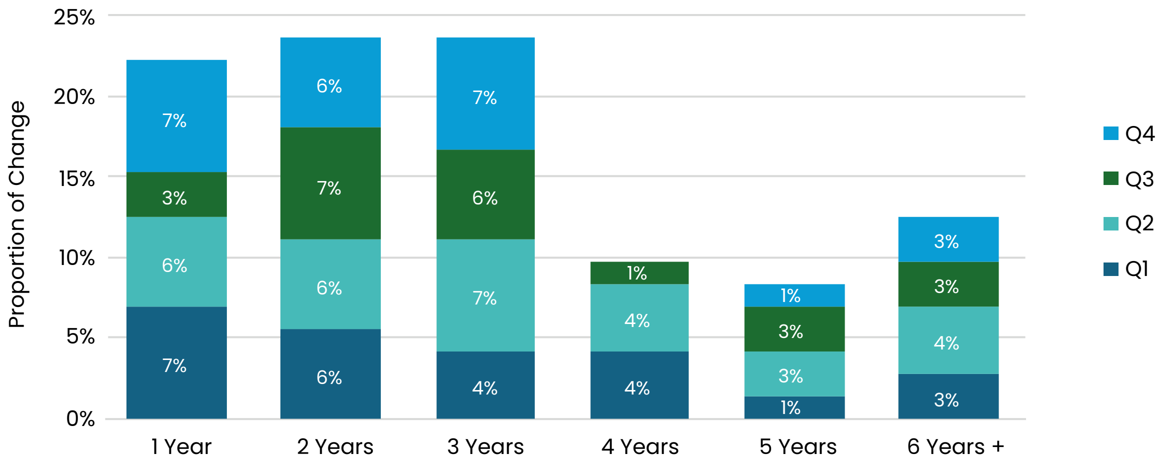


Top quartile companies make IT leadership changes sooner

Better-performing businesses (Q1 and Q2) are proactive in making tech leadership changes earlier in the hold period, with 13% doing so in the first year, compared to just 10% of those in the third and fourth quartiles.

In lower-performing companies (Q3 and Q4), a greater proportion of tech leadership changes occur in the second and third years, indicating that early alignment of technology strategy with business goals, and team focus, can significantly impact performance.

Better performing businesses make CTO changes earlier

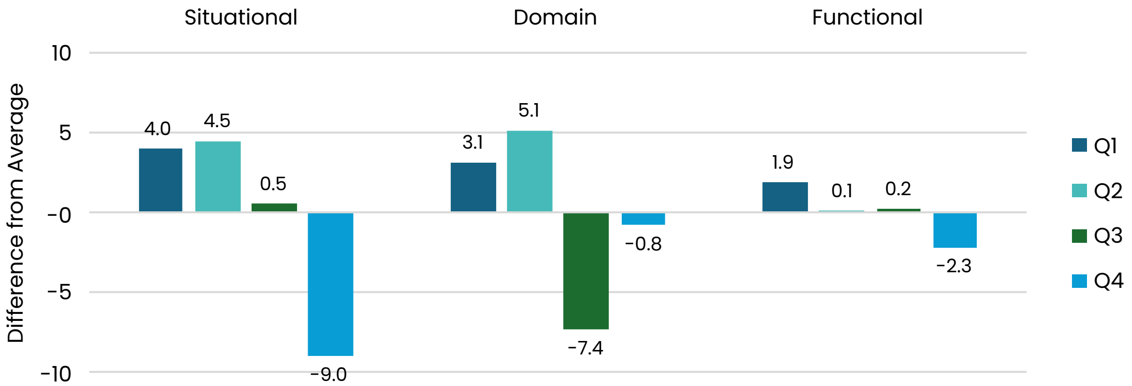


Situational and domain experience linked to technology value creation

Better-performing companies place a high value on situational and domain-specific experience when hiring IT leaders. This indicates a preference for those who can effectively align to the growth strategy, ensuring agility and resilience, and who can tailor technology strategies to meet industry-specific needs and challenges.

While functional knowledge (expertise in specific technology functions) is emphasised less overall, top quartile companies still show a slight positive preference (1.9) compared to Q4 companies (-2.3). This suggests that while specific functional expertise is important, it is the broader situational and domain experience that truly differentiates top-performing IT leaders.

Better performing companies prioritise CTOs with strong situational experience



More than a CTO: how tech leadership is evolving

- **Top performers include an average of three tech leaders**
- **Teams with diverse tech expertise see best returns**
- **Top quartile businesses prioritise externally focused tech leaders**

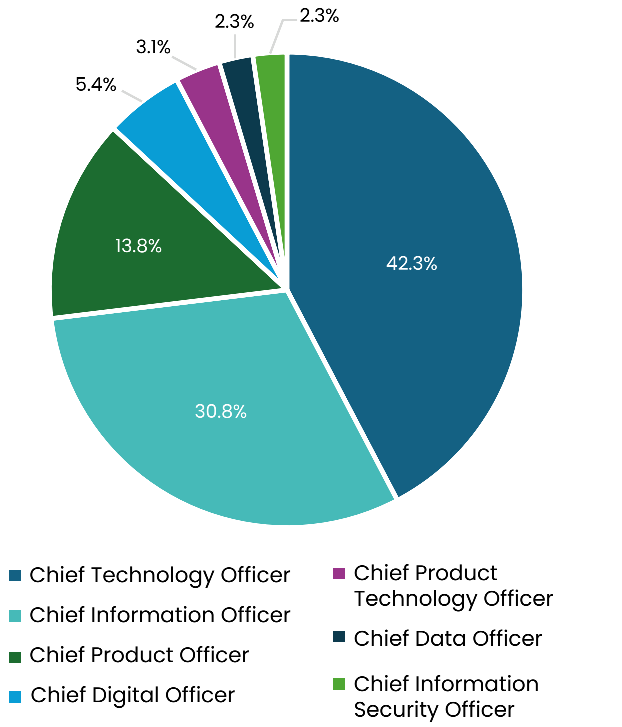
Traditionally split primarily into CTO or CIO, the growing complexity and diversity of the technology function means there are now at least seven distinct tech leadership titles, with responsibilities spanning full-stack technology, IT functions, data, security and product management. To add to complexity, many of these roles are converging and changing, as seen with the rise of the Chief Technology and Product Officer (CTPO), which has become increasingly common in recent years. Furthermore, for many businesses, one IT leader is not enough.

CTO functional Nexus

CTO, CIO and CPO most common tech leadership roles

CTO is still the most common job title for tech leaders, making up 44% of roles, however, over half of tech leaders (56%) now hold one of six other roles, spanning Chief Information Officer (32%), Chief Product Officer (14%), Chief Digital Officer (6%), Chief Data Officer, Chief Product and Technology Officer (3%) and Chief Information Security Officer (2%).

The proportion of roles categorised into 'CTO'



This reflects a variety of focus areas, although even these roles are far from fixed, and the exact focus varies significantly depending on the size, scale and nature of the business:

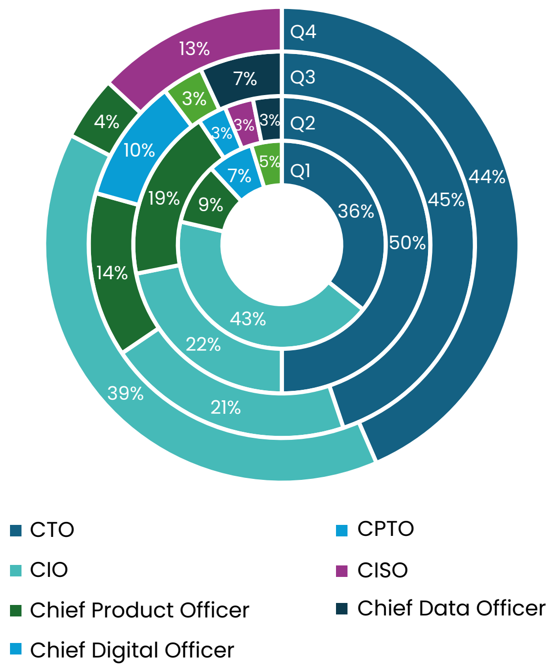
- **CTO:** Commonly from a technical background, responsibilities include software engineering, information technology, security, data functions, and platforms.
- **CIO:** A less technical role, spanning IT operations and business applications, IT project management & infrastructure, enterprise architecture, and cyber security.
- **Chief Product Officer:** Oversees the development and management of the company's product portfolio, often collaborating closely with the CTO.
- **Chief Digital Officer:** Commonly a non-technical role covering marketing functions, commercial functions, product management, product design, and marketing data platforms.
- **Chief Data Officer:** Oversees the management and governance of data across the organisation, including a strategic focus on data as a business asset.
- **Chief Information Security Officer:** Leads an organisation's information and cybersecurity strategy, protecting data and systems from cyber threats.
- **CPTO:** Increasingly common role which combines CTO and CPO responsibilities, including software engineering, product management, product design, data function, and platforms.

Top performers take more dynamic, commercial approach to technology leadership

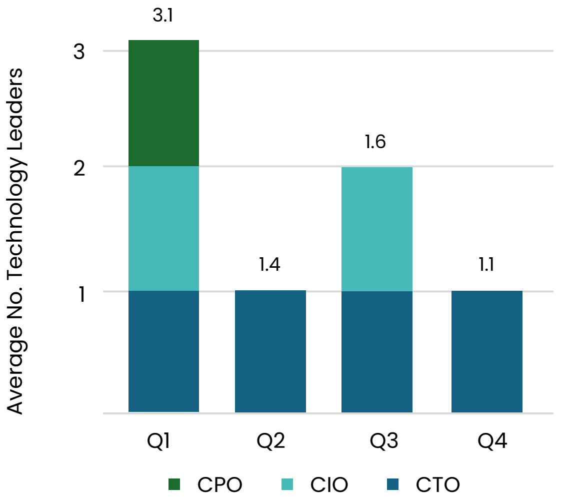
The best performing businesses often have several technology leaders on their top team, with those in the top quartile boasting an average of three. This indicates a comprehensive and multifaceted approach to technology management, and a focus on aligning technology specialism with the needs of the business. In contrast, poorer performing businesses (Q2, Q3 and Q4) have half the number of technology leaders, reflecting a less diversified leadership structure and potentially limiting their ability to address technological challenges effectively.

Not only do the best performing businesses have a greater diversity of tech leadership but they also prioritise outward facing technology leadership roles, such as CTO, and Chief Product Officer to drive innovation. Meanwhile, poorer performing businesses have less diversity in expertise, for example, 83% of bottom quartile technology leaders are either CTO or CIO, whereas in the top quartile, technology leaders are spread across several different roles. This suggests a less dynamic approach to technology leadership.

Variation of CTO role by quartile



Average technology leadership in businesses with CTOs



6. Applying the insights

What can leadership teams and investors take away from the report?

Applying the insights

Samuel Robberts,
Chief Strategy Officer
at The LCap Group

Businesses exiting this year epitomise a new approach to leadership in private equity backed businesses, which is proactive, fast-moving and data led. With twice as much leadership change happening amongst this cohort of exiting businesses compared to last year, the findings provide rich insights on what works, what doesn't, and new strategies coming to the fore.

Yet again, we saw that the most successful businesses make more change, make change faster, and have larger, more balanced leadership teams. Yet, we also saw important shifts, such as the role of domain expertise in helping businesses through uncertain times. New leadership roles have also emerged to bolster expertise, strategic oversight and execution in key areas, while core leadership roles have evolved and expanded, amplifying the impact they can have on business success.

How can investors apply these insights going forward?

Always-on leadership strategy

Leadership Capital should be a constant focus for PE-backed investors and leadership teams, particularly in the face of a rapid change. Leadership is an asset whose value can increase or decrease, and the best performing businesses are fast to make strategic changes in the face of adversity or market shifts. A data-led approach gives investors and current leadership the objective insights to spot leadership issues and opportunities, have challenging conversations, and have the conviction to act in a targeted way.

Evaluate leadership pre-deal

This 'always-on' approach equally applies pre-deal, when investors should look to evaluate leadership at arms-length as part of due diligence. With leadership analytics, investors can analyse the balance of competencies, identify any gaps, and map out potential change, without the involvement of the individuals themselves. This ensures investors start the hold period on the front foot, with the most effective team, maximising the runway for growth.

From visionary founder to functional leaders

Founders are hugely valuable to PE-backed businesses, but they won't be around forever. Think ahead and consider the breadth of functional roles required around the founder to scale the business. When planning to replace a founder, replicating their competencies and experiences isn't enough. The next business leader should build and complement the founder's strengths, with functional and situational competencies coming to the fore.

Don't neglect market and customer expertise

Operating within an unpredictable climate, leaders who can respond intuitively to the market and customer needs are at an advantage. This year's report is a lesson to always value domain focused leaders, even where their situational competencies may be lower. Their expertise and insight is just as valuable as seasoned value creation experts, adding to a much deeper resilience within the team.

Think beyond traditional leadership 'templates'

Innovation is critical in every area of business, including leadership roles and responsibilities. Instead of limiting your leadership options to the traditional templates, or how things have always been done, consider how roles can evolve to encapsulate the changing needs of your business. That could mean bringing in an executive chair, an M&A director, multiple technology leaders, or another role unique to your business.

Creative use of interims

Investors are thinking more creatively about how they can best leverage leadership for maximum impact and, as part of that approach, interim leaders shouldn't be overlooked. Interims support a strategy that favours operators over consultants, providing execution ability within the business, for rapid impact and results. For those businesses in need of a fast turnaround, they can be the ideal solution.

Run a diverse, data-led search process

While gender is only one aspect of diversity, our findings suggest that many PE-backed businesses need to do more to hire cognitively diverse leadership teams. Change is undoubtedly needed at a structural and systemic level, but businesses can increase their chances of hiring diversely by looking beyond the usual pool of talent and focusing on objective leadership data rather than more subjective measures such as referrals and CVs.

Innovative leadership

If you take just one message away, it's this: Innovation is as important in Leadership Capital, as in any other area of business. We live in the era of AI and automation, but as with technological development, it is vital to continuously review and rethink our approach to leadership. Management roles and relationships needn't always follow the same predefined template, and changing times call for shifting strategies. This must be borne out in leadership focus, competencies, and evolution throughout the hold period – and beyond.

Looking ahead...

Employee engagement moves centre stage

Organic growth is increasingly separating winners and losers and people are central to transforming operations and boosting margins, particularly given persistent skills shortages in numerous sectors. Consequently, we're going to see increasing investment in employee engagement, under the leadership of a strategic CHRO, to enable PE-backed companies to get the most out of their people. Studies have shown that employee engagement is linked to performance, and investors are increasingly looking to find an edge through hybrid working, career development opportunities, and employee incentive plans. Several private equity firms, including KKR, Apollo and TPG, have already committed to create more employee ownership schemes, with KKR recently announcing it will be taking its employee ownership programme worldwide, having previously created 6x average returns by implementing these schemes.

Continued rise of M&A

The popularity of M&A as a value creation lever looks set to continue, however given the elevated interest rate environment and increasing competition for the best deals, investors will have their work cut out in realising value from buy and build. To avoid creating a group of businesses that is less than the sum of its parts, investors and portfolio company leadership – bolstered by a specialist M&A Director - will need to be clear on where value will come from, whether through adding new capabilities and services, enabling international expansion, or acquiring new skills and technology. Maximising synergies in brand, culture and leadership will also be vital to ensuring success.

Technology drives operational effectiveness

Rapid technology advances in areas such as artificial intelligence (AI) and automation promise huge opportunities for operational effectiveness. However, the challenge in a private equity-backed environment is ensuring investment in these emerging technologies is targeted towards real performance and productivity improvements, to deliver value in a defined timescale. AI as a case in point shows potential to drive substantial efficiency gains, yet as with all new technologies, there are likely to be multiple failed use cases, and false dawns along the way. This will be a major obstacle for leaders in the next 12 months and beyond and a significant part of the challenge will be upskilling, preparing and engaging the workforce to embrace technological advances and opportunities when they do arrive. Another big opportunity for the CHRO and technology leaders to prove their value on the board.

The LCap Group in numbers

Over 150 employees

Clients across 20 countries

Worked with
163
funds in 2023

Over
30,500
PE teams evaluated for Leadership Dynamics

87%
Placement success rate (vs industry standard of 50%)

33%
Female placement across the LCap Group
(vs PE industry standard of 11%)

Over
27%
Of all UK PE leaders have taken our PACE behavioural evaluation

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