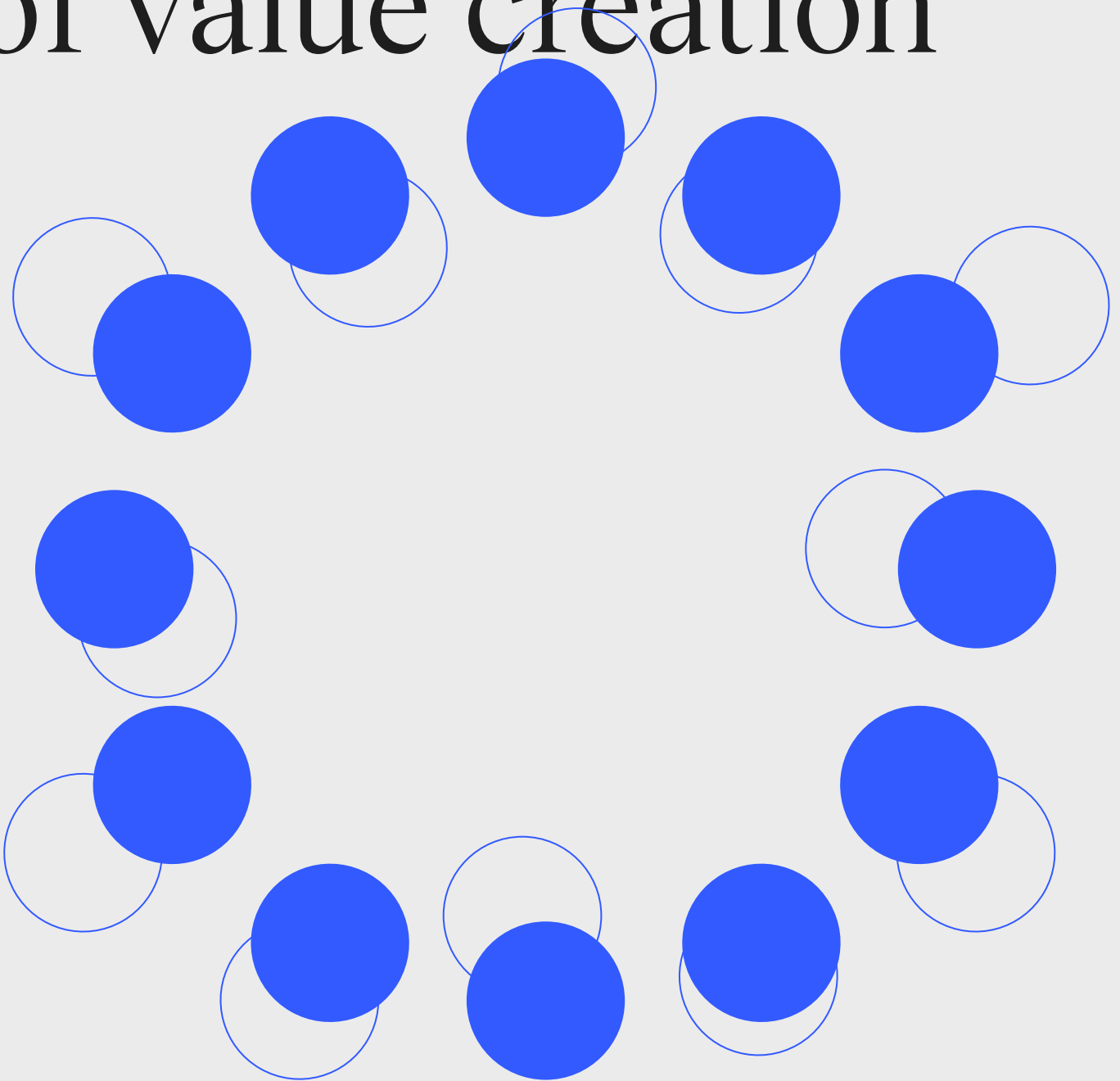


Leadership Teams as enablers of value creation



What European active investors are currently doing
to align Portfolio company's Leadership Team members

How does **good governance and alignment** among members of a Leadership Team – and between the Leadership Team, shareholders and stakeholders – affect the performance of an organization?

How can Private Equity firms improve both the **quality and speed of execution** of their portfolio companies' strategy by supporting the alignment among their companies' Leadership Team?

To answer these questions, LTx conducted a **survey of 31 European Private Equity** firms to better understand what European active investors are currently doing to align Portfolio company's Leadership Team members, and Leadership Teams with shareholders and stakeholders' interests.

We share some of the **best practices** we have uncovered during the research and the key insights and results from our survey.

We intend for this to be the first of many studies focusing on Leadership Teams as key enablers of value creation.

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Leadership Teams as enablers of value creation

Growing environmental threats, revolution, increasing social divides, inflation, etc.; in recent years, we have been facing unprecedented levels of uncertainty, unpredictability, and volatility. To address these challenges, organizations have no other option than to **embrace a culture of change**.

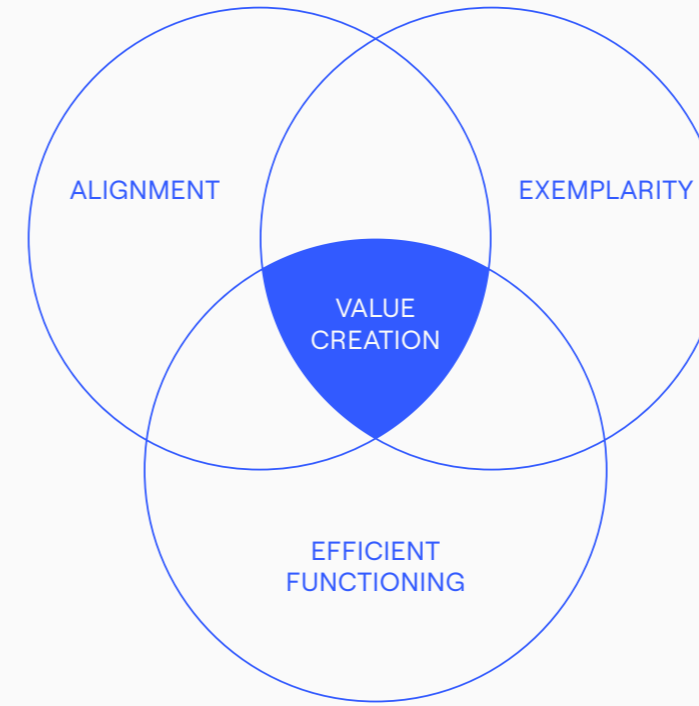
Nevertheless, only a few organizations satisfy the most important requirements for nurturing such a culture: **the full involvement and well-functioning of the Leadership Team**. If change is the business model, Leadership Teams are the driving force to make it happen. They are the **nerve centers that regulate an organization and transform intangible cultural levers into actionable business decisions**.

«Il pesce puzza dalla testa.»

Giovanni Verga, *I Malavoglia* (1890)

Only a Leadership Team that can **master its transformative levers**, can hold the space for people's talents and performance. This leads to:

- 01 Successfully implementing transformation,
- 02 Shortening the strategy-execution gap,
- 03 Solving uncertainties in the business model,
- 04 Balancing short- and long-term priorities,
- 05 Managing ESG challenges,
- 06 Attracting and retaining talent,
- 07 Leveraging technology and digitalization.



The cornerstone of value creation within the organization is the alignment, exemplarity, and efficient functioning of the Leadership Team.

The Leadership Team room is a place for radical pace and complexity, where contradictory voices and diverging forces meet, and **where the various interests of team members, stakeholders, and shareholders compete**.

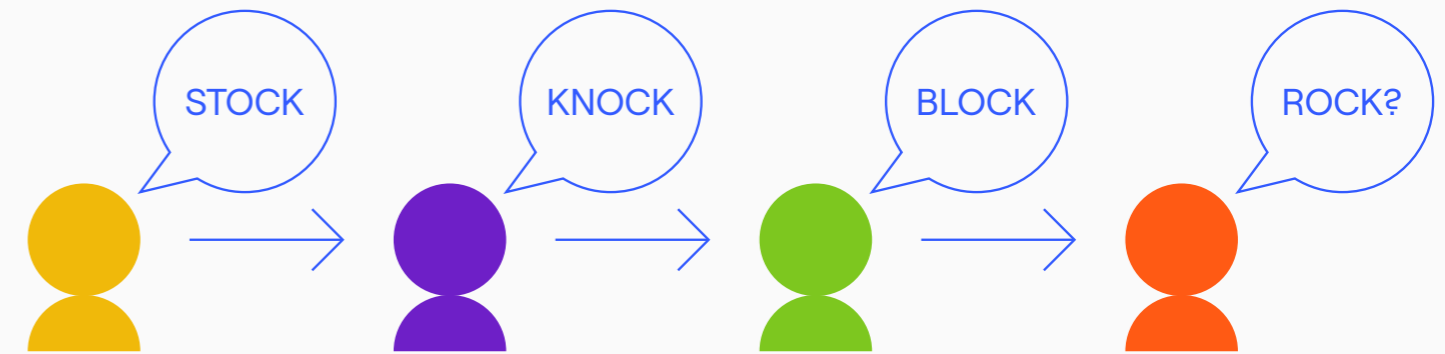
The Leadership Team is the focal point for organizational tensions, and the cultural matrix of the organization, irradiating purpose, culture, and behaviors.

How alignment among Leadership Team members impacts value creation

Governance is about establishing mechanisms to enable continuous collaboration, oversight, and the ability to make informed decisions that can improve performance despite negative external forces. Good governance models aim to **minimize the frictions** of control and ownership and **ensure a common purpose** among shareholders, the Leadership Team, as well as other stakeholders that influence the decision-making process.

However, the rules and processes created by governance models can quickly become ineffective, either because of new organizational structures or changes in the dynamics of team members. This can result in a **siloed organization**, where various parts of the organization fail to effectively communicate and share information, leading to diluted roles and responsibilities, ambiguous authority, and resource misallocation.

It is then necessary to realign members of the Leadership Team to ensure they have common strategy, goals, and purpose, as well as introduce the right rules and processes to ensure a good governance model within the organization. **Alignment is thus the process of creating good governance models.**



Just as in dance, which requires two bodies to be in sync and where there is continuous movement and positioning to create harmony, alignment and governance go hand-in-hand.

Good governance ensures alignment in the Leadership Team room while constant and dynamic alignment ensures that governance models remain effective.

Achieving proper alignment among Leadership Team members in strategy, goals, and purpose and good governance mechanisms, brings a clear competitive advantage to organizational performance. **A properly aligned organization with good governance models will ensure that they are diverting resources towards productive activities, reducing shareholder risk, and creating greater value for stakeholders.**

The relationship between Private Equity firms and Leadership Teams

Part 1: the alignment among the portfolio company Leadership Team members

Active investors, and particularly Private Equity firms, are uniquely positioned to support and stimulate the Leadership Teams of their portfolio companies by establishing good governance models and challenging Leadership Team members to continuously re-align on the Value Creation Plan.

However, alignment of Leadership Teams is an often-overlooked area for Private Equity firms, as it is too often perceived as mere HR topic. Many firms do not always promote the alignment within their portfolio companies, though **they do have a good understanding of the operating and financial risks of not doing so.**

By supporting the alignment among all members of the Leadership Team, PE firms can create greater resilience of their portfolio companies, improving both the quality and speed of execution of the Value Creation Plan.

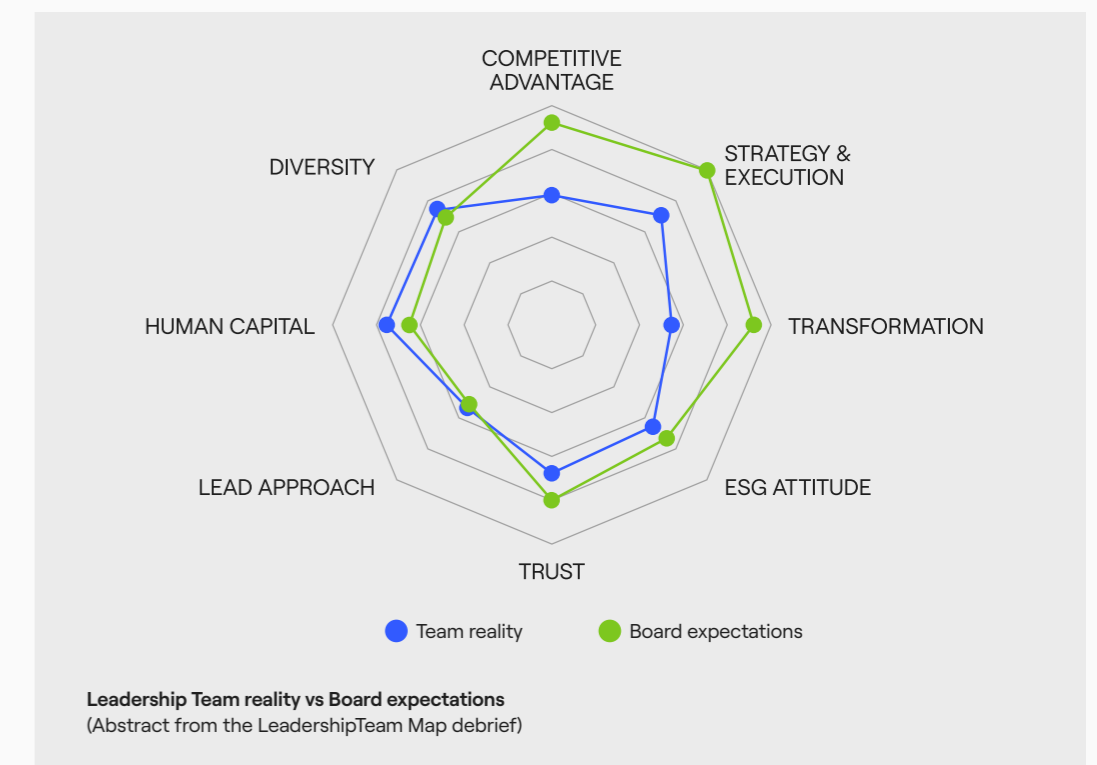


Part 2: the alignment between the PE firms and the portfolio company Leadership Team

Similarly, misalignments between Private Equity firms and their portfolio companies' Leadership Teams can trickle down to the organization, resulting in misalignment among Leadership Team members.

Any organization can get pulled in different directions if there isn't a common direction and congruence of intentions at the top.

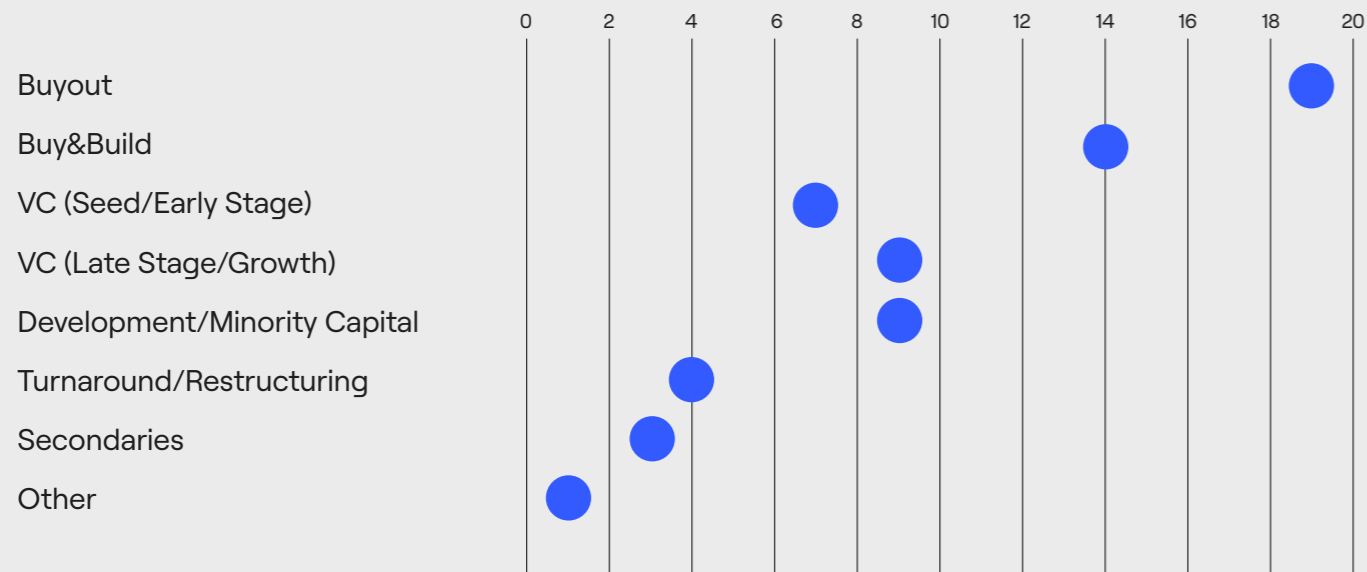
Misalignments between Private Equity firms and their portfolio companies' Leadership Teams can get amplified by the time it reaches the rest of the organization, as each level of management will have different interpretations of what is expected. As a result, this can cause silos, hesitation in decision-making, power games, lack of buy-in on strategic decisions, and ripple effects on performance.



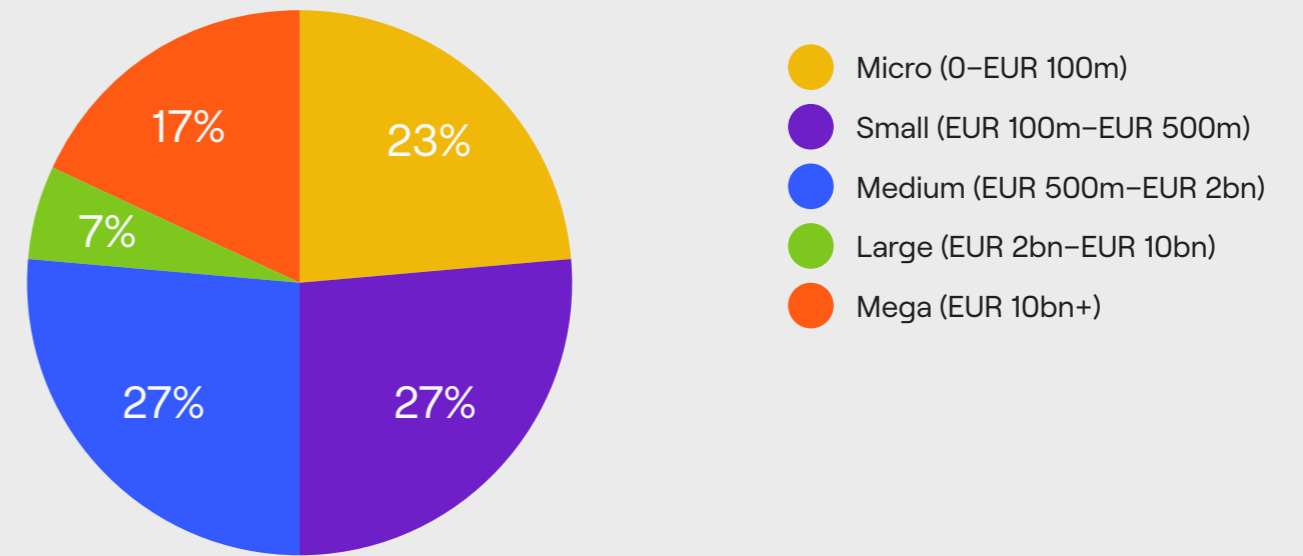
Key findings from our Survey

We conducted a survey of **31 PE firms** to better understand how PE firms address governance issues and how closely they work with their Leadership Teams to create greater alignment among all members. The respondents of our survey were from **8 countries** representing a **mix of fund sizes and investment strategies**. We explored how PE firms and their Leadership Teams align on the 7 enablers of value creation identified thanks to our statistical analysis on hundreds of Leadership Team members.

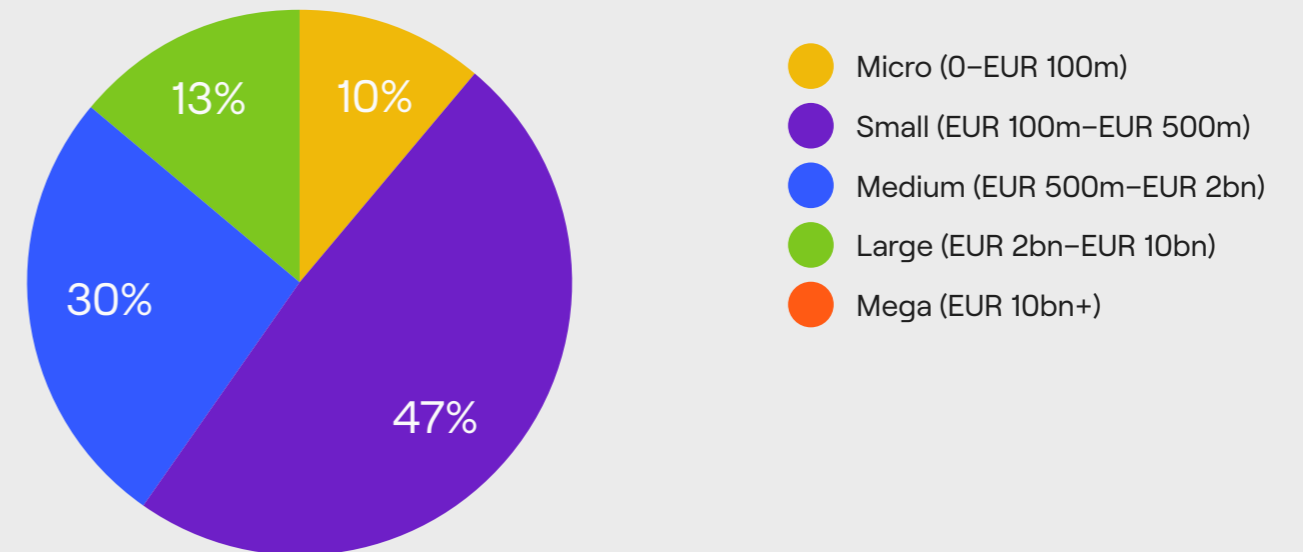
Responses by Fund Strategy



Responses by Fund size



Average Portfolio Company Size

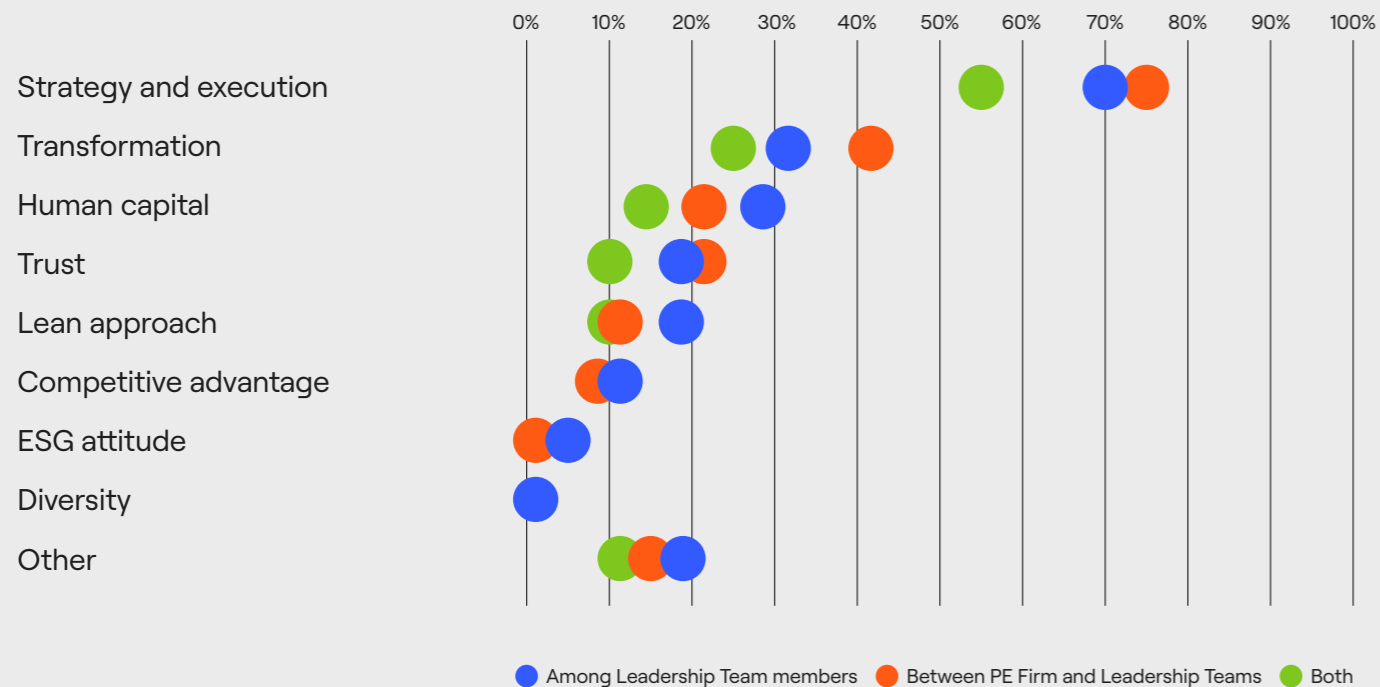


Finding #1: Strategy and Execution is the most important area of misalignment for PE Firms and respective portfolio companies

Among Leadership Team members as well as between the PE firm and the portfolio company Leadership Team, over 70% of respondents listed **Strategy and Execution** as the top area of misalignment.

55% of surveyed PE firms listed Strategy and Execution as an area of misalignment both among Leadership Team members and between the PE firm and Leadership Team.

What are the most important topics of misalignment?



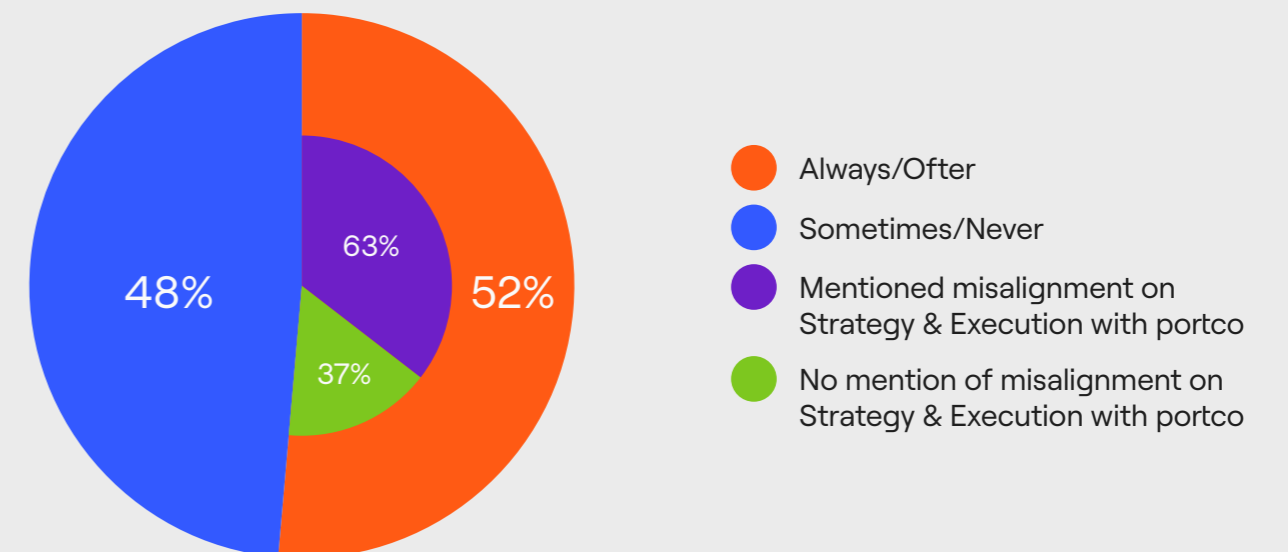
Finding #2: Alignment of interest is not sufficient to ensure alignment on execution

Most of the PE firms surveyed mentioned the importance of having a well-structured and appropriate incentive scheme for members of Leadership Teams as a best practice to help the execution of the Value Creation Plan.

Indeed, 52% of firms respondents believe that 'alignment of interest' (financial incentives) is always or often sufficient to ensure alignment on the execution of the VCP. However, of these respondents, **63% respond that there is still a misalignment with the portfolio company when it comes to Strategy and Execution.**

“Alignment of interest” is not “alignment on execution”!

The “alignment of interest” is sufficient to ensure alignment on the execution. 63% of those considering “alignment of interest” always or often sufficient to ensure alignment of execution are still misaligned.



Finding #3: Quality of communication between the PE firm and Leadership Team is more important than its frequency (and having a People Officer or a Leadership Capital Partner improves alignment)

PE firms that communicate daily with the Leadership Team of their portfolio companies still experience misalignment among Leadership Team members on Strategy and Execution, **questioning the benefits of frequency of communication.**

PE firms that communicate with the whole Leadership Team experience the lowest levels of misalignment on Strategy and Execution.

This raising importance of team-centric models might explain this phenomenon: communicating with all members of the Leadership Team might reduce potential misunderstandings and misinterpretations.

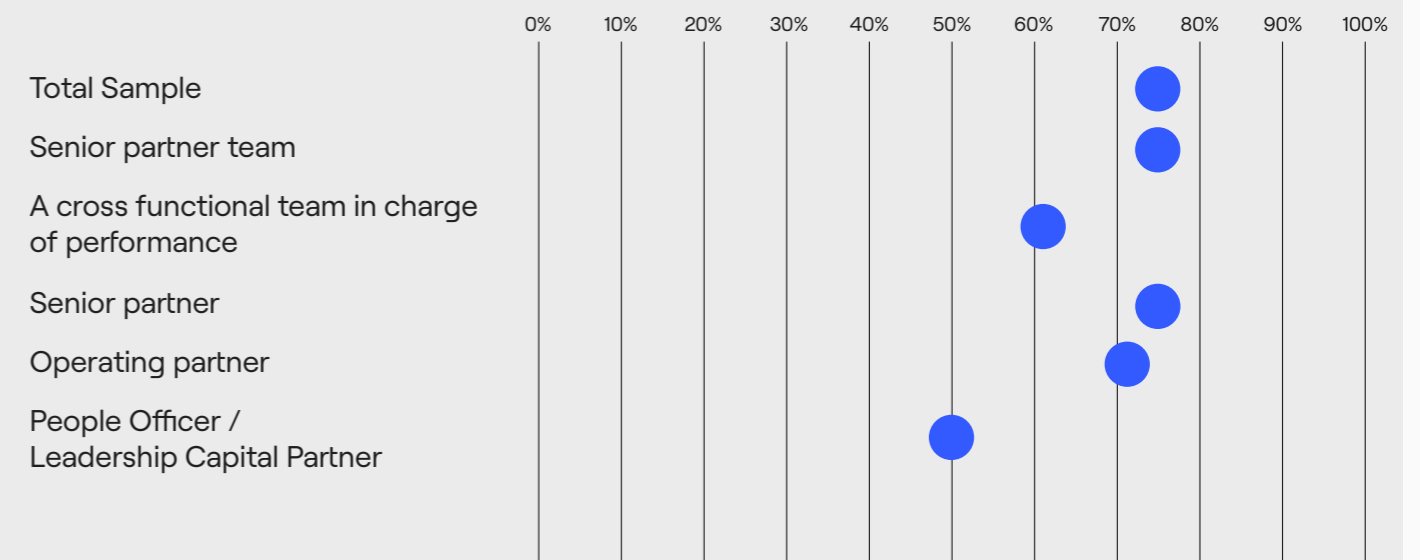
From the PE side, **having a People Officer or a Leadership Capital Partner responsible for communications with the Leadership Team yields the lowest level of misalignment between the PE firm and Leadership Team.**

From our experience, a people Officer or an external facilitator has the advantage of focusing more on how people talk (process) rather than on what people say (content).

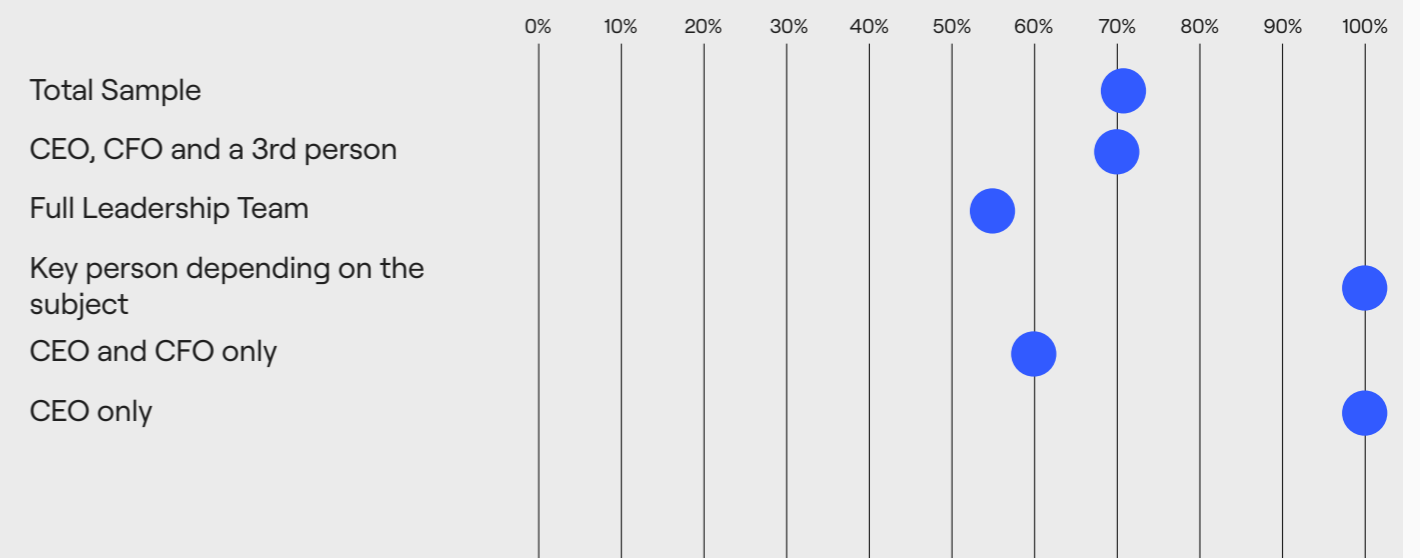
«65% of CEOs and leaders believe it is important to shift to a team centric model»

Deloitte, 2019

Who within PE firm is responsible to support the alignment and efficient functioning of the portco Leadership Team vs % Misalignment on Strategy and Execution



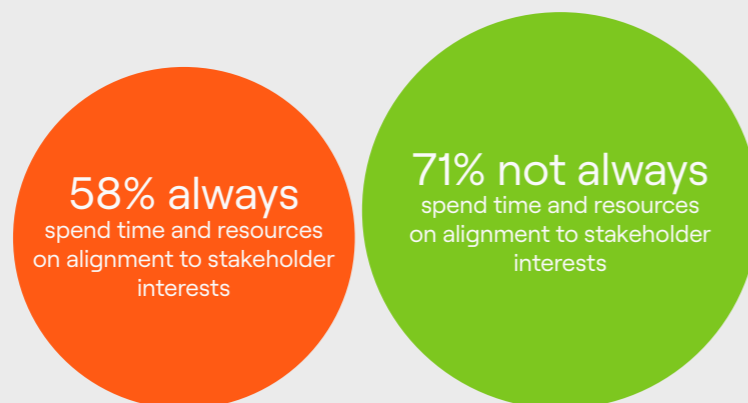
Who among Leadership Team do PE firms communicate with the most vs. % Misalignment on Strategy and Execution



Finding #4: Aligning on Stakeholder Interests is important to achieve alignment on Strategy and Execution among Leadership Team members

PE firms that spend time and resources on alignment of the portfolio company Leadership Team to stakeholder interests see lower levels of misalignment on Strategy and Execution among Leadership Team members (58% vs. 71% for the overall sample), as well as less misalignment on Competitive Advantage, Transformation, and Trust.

Alignment to Stakeholder Interests vs. Misalignment on Strategy and Execution: % of responses for misalignment on Strategy and Execution



Best practices

We have asked our surveyed respondents “**What are the best practices of your fund to align and support your portfolio companies’ Leadership Teams on your Value Creation Plan?**”.

Here below a selection of the most relevant answers received by the surveyed respondents:

- Continuous assessment of M&A opportunities
- Openly discuss and agree upon ESG KPIs with the Leadership Team, in order to ensure both alignment on strategy/execution and on our Fund mission;
- Strong investment on governance (e.g.: strategy plan annexed to legal documents, regular strategy sessions, compensation package linked to plan, bad leaver clauses etc.);
- Inhouse consulting team for strategic support;
- Management Incentive Plans (MIP) that ensure returns for the investors;
- Portfolio monitoring by the Investment Team and Board presence;
- Special projects undertaken with the supervision of monitoring team of the fund;
- Regular troikas among Chairperson, CEO and Private Equity Partner;
- Create a plan together and have monthly check-ins to report on the plan;
- Make sure they know where to find help and support them on a daily basis (open door approach);
- Co-creation of value creation plan with the entire first and second tier Leadership Team in combination with sessions to improve team cooperation;
- Collaboration to devise the strategy and regular communications to ensure the execution of the plan;
- Intervention of external consultants (only in crisis mode);
- Regular meetings focusing solely on Value Creation and not on current business (monthly meetings are in place for that);
- When starting the collaboration you need to put serious time and effort to truly get to know each other to create safety, connection and trust;
- Meet at least quarterly in person to be able to truly connect;
- We include a full day of strategy exploration and definition as part of our Due Diligence process. In this work, we work to clarify the path for all major business functions in Y2 and Y5.

It's about Time

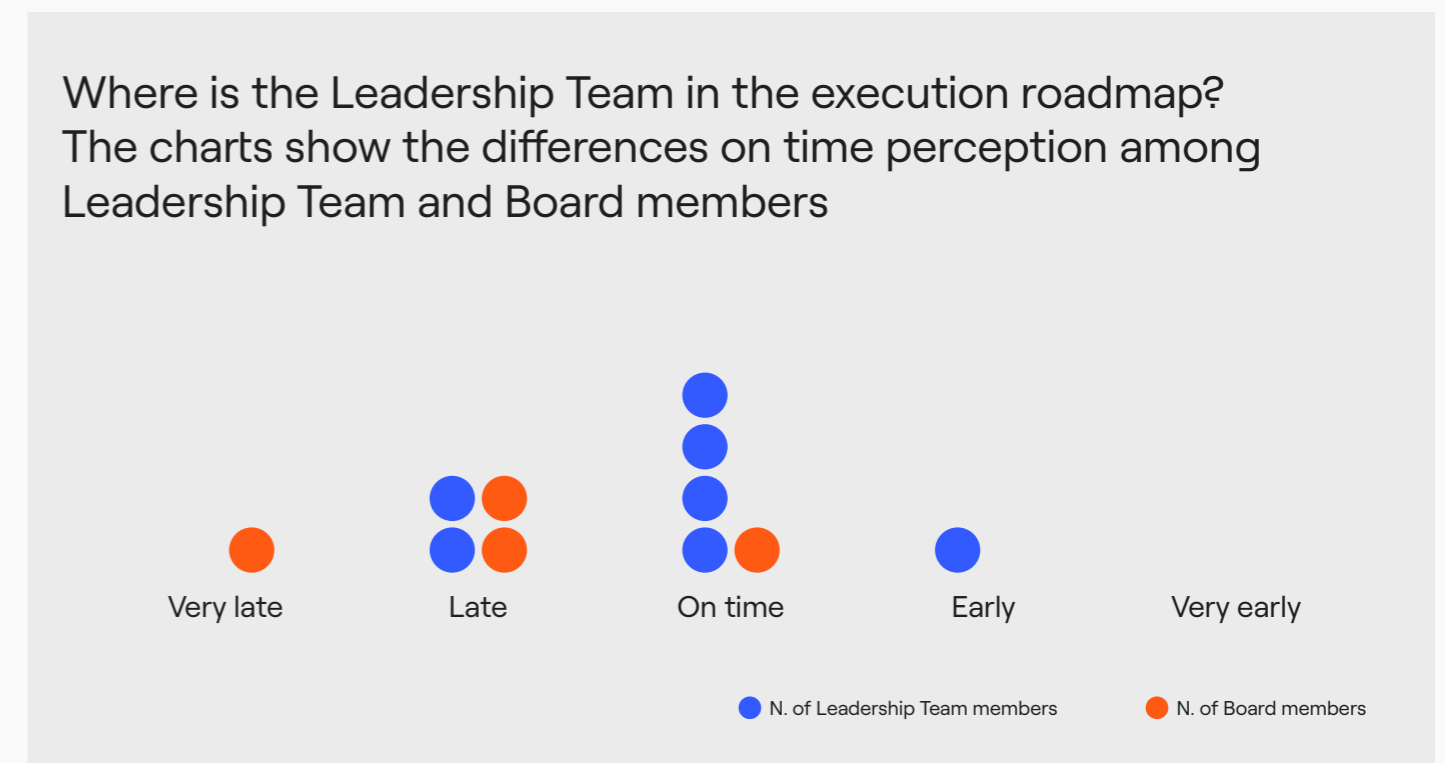
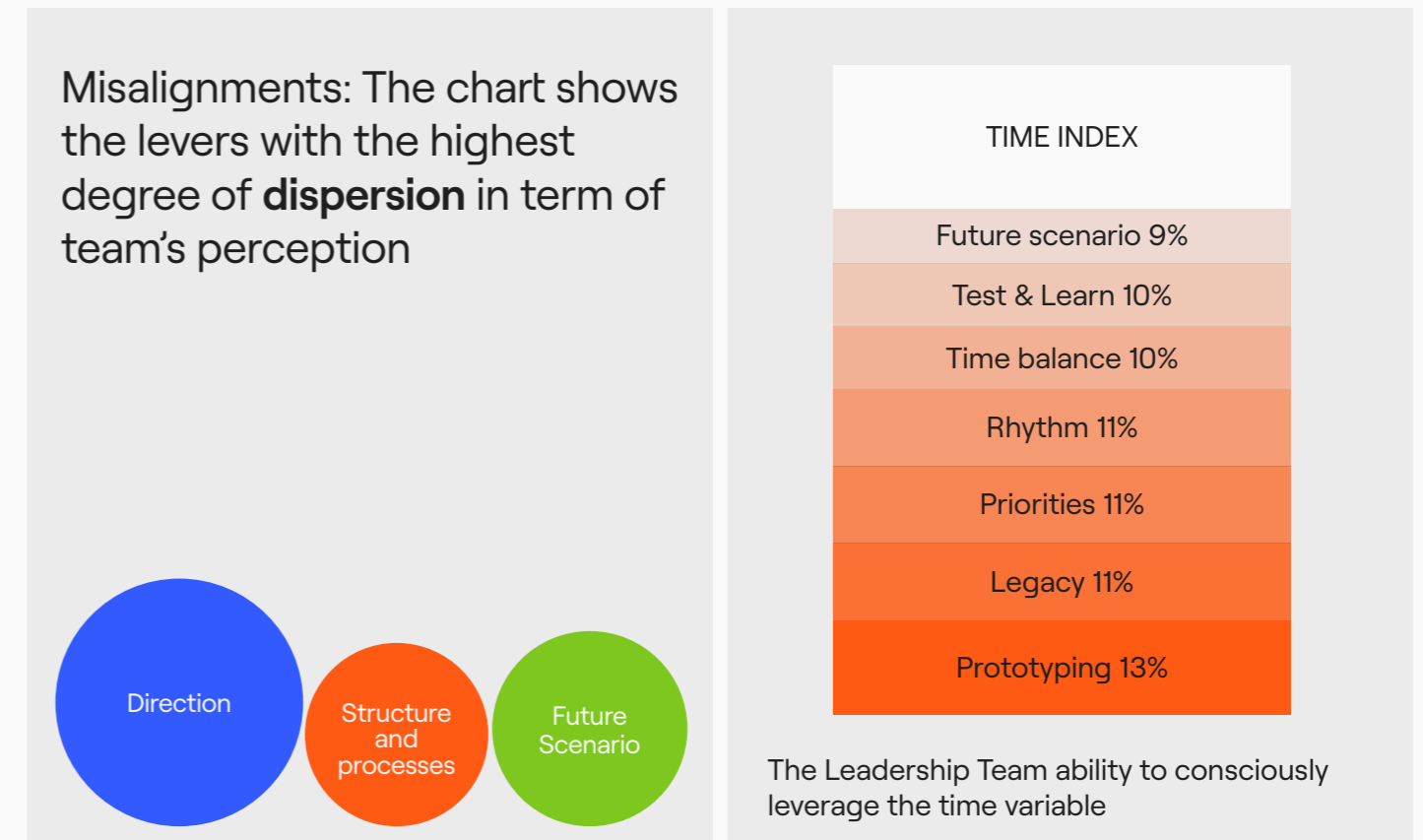
From our experience and the various conversations run with Board members and Leadership Team members, we see **the “time” variable as the most critical element in the relationship among shareholders, management and stakeholders.**

Time is the focal point of competing interests:

- Potential friction between the **long-term interests** of the portfolio company stakeholders vs. the **shorter-term needs** of the shareholder;
- Similarly, between **growth** ambitions and short-term **profitability**;
- Potential tensions at the Board level among different shareholders, who have **different needs in terms of exit timing**, and try to influence the Leadership Team accordingly;
- Lack of clarity on **who should dictate the tempo** of the portfolio company - the founder? the CEO? the shareholder? the Board? - and at what rhythm and tempo should the Leadership Team play?
- Choices on **talent acquisition** and on talent **allocation** (e.g.: on long-term projects or on today's profitability);
- And even minor issues such as differences about the **frequency and length of meetings** might reveal hidden cultural tensions.

It is not that members of the Leadership Team don't recognize these tensions - they are familiar to anyone who runs a business - but rather that they prefer not to make them explicit in order to avoid conflicts. But a Leadership Team aware of, and able to, reconcile these tensions will unleash people's talent and performance. At LTx, time is a key indicator that we explore in order to determine the alignment of Leadership Team members and the Board. Through this, we help organizations understand how differences in the perception of time affect their decision-making, and their strategy and execution

Some insight about the “time variable” you might get from our diagnosis:



How do governance and alignment interact

(by ChatGPT)

We have asked this question (how do governance and alignment interact?) to many investors and Leadership Team members, and each time we have received a different answer.

We hoped AI could surprise us and find a good synthesis. It did.

Governance and alignment are two related concepts that are important for achieving organizational goals. Governance refers to the set of policies, procedures, and practices that are put in place to guide decision-making and ensure accountability in an organization. Alignment, on the other hand, refers to the process of ensuring that the goals and objectives of different departments, teams, or individuals within an organization are aligned with each other and with the overall mission and vision of the organization.

Governance and alignment interact in several ways:

01 Governance can help to create alignment: By setting clear policies and procedures for decision-making, governance can help to ensure that all decisions are made in a way that is consistent with the organization's goals and objectives. This can help to create alignment between different departments, teams, or individuals within the organization;

02 Alignment can help to improve governance: When different departments, teams, or individuals are aligned with each other and with the overall mission and vision of the organization, it can be easier to implement and enforce governance policies and procedures. This is because everyone is working towards the same goals and objectives, making it easier to ensure that decisions are made in a way that is consistent with the organization's values and principles;

03 Governance and alignment can reinforce each other: When governance policies and procedures are aligned with the organization's goals and objectives, it can help to reinforce alignment between different departments, teams, or individuals within the organization. Similarly, when different departments, teams, or individuals are aligned with each other and with the overall mission and vision of the organization, it can help to reinforce governance policies and procedures.

In summary, governance and alignment are two related concepts that interact in several ways. By creating clear policies and procedures for decision-making, **governance can help to create alignment between different departments, teams, or individuals within the organization. At the same time, alignment can help to improve governance** by making it easier to implement and enforce policies and procedures that are consistent with the organization's goals and objectives. Finally, governance and alignment can reinforce each other, helping to create a more effective and efficient organization.

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