

# THE POWER OF PEOPLE: HARNESSING HUMAN CAPITAL FOR MAXIMAL RETURN

LODESTONE PEOPLE CONSULTING

A key belief that has shifted over the last few years for the private equity (PE) industry is the growing realization that leadership effectiveness is the foundation of deals success and investment returns. In AlixPartners' 2022 survey of PE executives\*, leadership effectiveness emerged as the most important lever for creating value in portfolio companies, cited 70% more frequently than operational effectiveness.

However, despite acknowledging the importance of effective leadership, often old habits die hard and PE firms tend to prioritize rapid operational changes and go-to-market strategies, underemphasizing time and investment on talent and culture concerns. This divergence can lead to strategic misalignment, cultural conflicts, and ultimately, suboptimal performance. For instance, a CEO focused solely on operational efficiency may inadvertently alienate key talent and customers, resulting in talent attrition and revenue decline. Statistics also show that about three out of five CEOs depart after a PE acquisition\*\*, often due to unplanned exits, which can lead to significant disruptions and erosion of return on investment.

Such instability not only impacts the financial returns for PE firms, but also hampers the growth trajectory and competitive positioning of the portfolio company. Furthermore, a disconnect between the current leadership's vision and the desired future state can lead to employee disengagement, further undermining organizational performance and hindering strategic progress.

***To navigate these challenges and optimize leadership effectiveness, PE firms can leverage comprehensive solutions offered by organizational psychologists who serve as human capital consultants.***

These solutions encompass various services, including rigorous assessments, targeted executive coaching, and customized leadership development programs. By focusing on cultivating authentic, inspiring, and emotionally intelligent leaders, these interventions can help align leadership priorities, enhance collaboration, and drive performance enhancement throughout the organization. Moreover, by fostering a culture of continuous learning and development, PE firms can build a robust leadership pipeline and build a strong organizational bench of talent, ensuring long-term organizational resilience and sustainable growth

Many mid-sized companies lack the deep knowledge and scientific background to diligently enhance leadership capabilities to increase growth on their own. However, equipping the C-suite teams with necessary tools and in returns. By engaging business psychologists to maximize C-suite capabilities, firms can not only enhance their portfolio companies' resilience but also position them for sustained success in a rapidly evolving business landscape.

### **Human Capital Inefficiencies Kill Value Creation**

How many of your portfolio companies are living through these understandable, yet value diminishing, growing pains?

- 1) Under-qualified executives
- 2) Lack of alignment between board/sponsors and executive priorities
- 3) Trust and conflict drama within the executive team or between the team and the board
- 4) Inability or unwillingness to hold the organization accountable
- 5) Poor, if any, succession plans rooted in objective data with supporting processes

These issues can be solved with scientific business psychology interventions. They can be most effectively and efficiently solved when handled proactively, as opposed to waiting for a problem to arise, and when systematically approaching solutions with a goal of strategic integration across human resource management, compared to piecemealing quick fixes.

## **Crafting High-Performing Management Teams for Value Creation: Not a One Solution Task**

The success of Value Creation Plans rests on the shoulders of C-Level Portfolio leaders, or the "C-Team." Progressive PE firms meticulously assess the readiness of these teams to achieve the company's business imperatives.

Mid-sized companies excel when they prioritize growth, operational excellence, and talent enhancement. Effective C-Teams orchestrate these imperatives, requiring constant oversight and strategic direction. Collective capabilities within the enterprise, but especially within the executive team, are crucial for success.

As PE firms acquire and integrate new organizations, strategic re-setting of the executive team becomes essential. But too often, firms delay in making improvements to the team or take a piecemeal approach: get coaching for one executive, assess a candidate to join the team but do nothing to help that new executive accelerate assimilation into the team and organization, assume the executive team will both naturally "gel" and function appropriately and intuitively know how to respond to the board's expectations.

### **A Better Approach is Proactively and Holistically Solving the Issues**

Simply put,

***The whole is greater than the sum of its parts.***

Our research and experience has shown us that when boards start with the assumption that an executive team will need human capital support and proactively bundle three key initiatives and commit upfront to providing that support before issues arise, the portfolio company experiences accelerated excellence with less conflict along the way.

### **Initiative One: Executive Assessment**

Discerning private equity firms start with scientific assessment of the existing executive team and as they seek to add or replace members, use the same process and tools. Lodestone's approach in this arena is to assess both behavior and the underlying personality which explains the behavior. Many executives can impression manage their way through an interview, particularly an unstructured one.

Scientific best practice uses business simulations and the validated personality predictors of performance (i.e., measuring what are called The Big Five), combined with business impact interviews conducted by experienced business psychologists and anchored around the key business imperatives that drive the investment thesis. Notably, executive assessment is only as strong as the interpretation of the data; the role of business psychologists with credentials to administer, evaluate, and discuss implications of data is paramount for success with scientific assessment.

These methods increase predictive power of executive success when compared to simply score-carding or clinical or anthropological assessments. In addition, and importantly, scientific assessments where candidates get to demonstrate their capabilities and competencies, as opposed to simply talking about them, are better received by candidates, perceived as more just and fairer, and help to level the playing field with underrepresented groups. Simply put, assessment methods like the above

***increase the likelihood of choosing an executive who will deliver upon your investment thesis and decrease implicit bias and choosing a candidate “just like me”***

## **Initiative Two: Individual Executive Development**

Many firms are familiar with and utilize executive coaching. Too often, this is done as a “fix the person” initiative versus proactively working to enhance the executive’s leadership capabilities and align the leader’s strengths and development areas with both short and long-term organizational strategy and vision. For even the most talented and motivated C-suite leaders, a new sponsor and the many challenges of fast growth and scalability create tremendous change. The stress—even if it’s positive stress—associated with this fast change brings out derailing patterns in any executive.

Understanding this phenomenon and proactively contracting with an executive coach smooths the change curve and increases leader effectiveness. Not insignificantly, a coach for the CEO often makes the sponsor’s life easier as the leader has a “safe space” who understands the pace and expectations of private equity and can advise the leader on how best to meet your expectations. Further, part of the investment thesis imperatives usually includes scaling talent and implementing more sophisticated human capital systems, often before a true CHRO is in place.

***A strong leadership advisor often has had CHRO experience or CHRO de facto experience, and can provide strategic guidance on people initiatives in addition to leadership coaching.***

### **Initiative Three: C-Suite Team Effectiveness**

Selecting a great CEO based on scientific assessment and setting that great CEO up with a qualified coach are nice, but the CEO does not operate in a vacuum. The success of the organization requires a highly functioning executive team, not just a highly functioning chief executive. Particularly when a new CEO is brought into an organization, trust issues between the “old and new” can emerge, creating barriers to effective change.

Even where trust issues aren’t pervasive, quick moving operationally- or market-focused leaders often move too quickly through important expectation setting steps around executive team operating norms and responsibilities. When a team does not take the time upfront to address how they will operate together, including understanding the personalities and characteristics which comprise their team mosaic, they invariably will face frustration, conflict, unmet expectations, and fall short of optimal performance.

Team sessions, facilitated by someone trained in leadership and team psychology and dynamics, are essential for success, smooth transitions, meaningful change, and maximized business impact. Such sessions are not simply “touchy feely team building.” Effective team sessions are about understanding scientifically the personalities around the table, who is best suited for what, where diversity of thought will serve as a strategic asset, scenario planning for best decision-making process given the mosaic of the team and establishing clear RACIs—both between team members and with respect to the board.

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## Exemplary Companies Pull All Three Initiatives Together for Accelerated Positive Impact

### Case 1: Systemic Human Capital Optimization Increases Company Value

**Situation:** A leading PE firm was experiencing the complex venture of trying to unify a newly minted organization made up of one primary platform and a selection of add-ons. These additions were each led by executives with unique leadership styles and corporate cultures, which posed a significant challenge. The firm was about to appoint a first-time CEO and sought scientific data to substantiate their belief in her potential to unify these diverse elements into a single, high-performing company.

**Approach:** Lodestone was commissioned for its expertise in swift, precise, executive assessment and feedback, evaluating each member of the ELT, including the CEO, CFO, CRO, VP of HR, and OGC. The board and CEO were provided with a comprehensive "talent mosaic," forecasting the team's capacity to meet the investment thesis goals. With the guidance of Lodestone's Leadership Advisory Services, the CEO adeptly navigated team dynamics and board interactions, and also undertook strategic HR initiatives through Lodestone in the absence of a CHRO. The ELT then engaged in Lodestone's 'Knowing Me, Knowing You™' and 'Vision and Values' sessions, laying the cornerstone for their collective values, operational norms, and accountability structures. Moreover, the CRO adopted the advisory services, integrating scientific assessment in the development of the sales leadership team.

**Result:** This strategic intervention and leadership fortification led the company to be heralded as the PE firm's 'Portfolio Company of the Year.' The board and the deal team both attributed their success to the robustness of the executive team and their exceptional operational functionality. The crowning glory came when the company was acquired soon after by another firm, resulting in an exceptionally profitable return for the client PE firm.



## **Case 2: Sustainable Energy Company Tries Piecemeal Approach, Delays Growth**

**Situation:** A firm faced the critical decision of appointing a CEO for a recently acquired portfolio company. Confident in their own due diligence processes, they initially bypassed comprehensive assessment services, but then decided to have Lodestone assess their final CEO candidate “just in case” and to not engage beyond the assessment and feedback.

**Initial Approach:** The firm asked Lodestone to assess the chosen candidate to give him feedback on his strengths and on development areas. This feedback highlighted for the CEO his narrow but strong operational focus and likelihood of friction with some direct reports.

**Result:** The appointed CEO hit the ground running, swiftly implementing operational efficiencies and strategically recruiting a CRO within the pivotal first 100 days. However, beneath this veneer of early success, a discord brewed. Before half a year had passed, a stark misalignment emerged between the CEO and CRO around market strategy, with the CEO's operational obsession inadvertently sidelining the broader market vision and talent development. Further, other ELT members including the COO were disengaging and feeling micromanaged by the CEO.

**Revised Approach:** Recognizing the urgency to salvage the situation, the sponsor re-engaged Lodestone to orchestrate an ELT intervention. Through tailored team effectiveness sessions and targeted Leadership Advisory Services (LAS) for the CEO, Lodestone set to work realigning the executive team's vision, strategy, and focus.

**New Result:** This recalibrated approach fostered a renewed sense of unity and purpose within the executive ranks. The company, albeit delayed, began to realize its market potential, pivoting towards a balanced operational and market-centric strategy. This newfound synergy not only propelled the company towards its targeted goals but also reinforced the importance of holistic leadership assessment and alignment from the beginning.

### **Case 3: CEO/COO Calibration to Scale the Organization**

**Situation:** At a critical point of growth, a PE firm identified the need to optimize the leadership tandem of a highly promising yet struggling CEO and his COO. Prior to engaging Lodestone, the firm had conducted a baseline objective scorecard assessment on the CEO, revealing a discrepancy between his ambitious vision and the immediate pragmatic needs of the business, a gap that jeopardized both market confidence and vital funding. Meanwhile, the COO, essential for driving operational efficiency, faced the daunting task of rapidly scaling the company's operations. In light of these insights, the PE firm enlisted Lodestone's Leadership Advisory Services to recalibrate and enhance the executive partnership.

**Approach:** The strategy hinged on fostering a symbiotic partnership between the CEO and COO, so Lodestone used a specific version of leadership advisory services—dyadic coaching. Lodestone focused on realigning the CEO and COO's individual strengths to the company's tactical and strategic objectives. This was orchestrated through bi-monthly dyadic coaching sessions designed for intentional and ongoing role calibration. These sessions heavily leaned on the organization's business imperatives as a guiding compass, helping to create clear 'swim lanes' of accountability and ensuring that the dreamer CEO's expansive visions were grounded by the executor COO's practical focus.

**Result:** Through Lodestone's dedicated coaching process, the CEO and COO were able to come together in a dynamic where dreams met execution. As they learned to navigate and respect their distinct 'swim lanes', frustration gave way to functional collaboration. A robust RACI matrix allowed them to lock in their operational harmony, leading to enhanced effectiveness. The organization not only witnessed improved business performance but also enjoyed a revitalized leadership relationship. The threat of internal discord dissipated, replaced by a collective clarity of purpose and direction.



## **The Bottom Line on Business Psychology's Positive Impact**

In the fast-paced world of PE, the acceleration of value creation and rapid attainment of insights are not just goals but imperatives. This acceleration is only able to be accomplished when executive assessment, bespoke executive development, and team effectiveness all blend in pursuit of operational excellence. The integration of these three pillars facilitated by expert business psychologists—equipped with both scientific data and sound, practical wisdom—ensures that a company will not only advance in organizational effectiveness, but also soar in its return on human capital endeavors.

***Embracing a methodical and holistic regimen in human capital optimization isn't just a strategic choice; it is the foundation for building sustainable growth and success.***

## About Us

*Lodestone People Consulting is a firm of workplace psychologists who bring human capital science to sponsors and their portfolio companies. We help discerning Private Equity Firms understand people and people systems during due diligence. After your acquisition, we conduct your new executive selection, bolster or change HR practices, enhance organizational culture, and provide individual and team development. The result is a more effectively running organization, thus increasing your ROI.*

*If you need assistance with any of the issues addressed here, please contact us at [info@LodestoneHR.com](mailto:info@LodestoneHR.com) or our founder, Dr. Sandy Fiaschetti, at the conference.*



### **Sandy Fiaschetti, Ph.D.**

Dr. Fiaschetti is the founder and Managing Partner of Lodestone People Consulting. She has been both an internal and external consultant to both private equity firms and mid-cap and large companies across a variety of industries. Sandy's experience has been focused on organizational culture and effectiveness, talent assessment, and leader development. She has assessed and advised hundreds of C-suite executives. She is particularly passionate about the importance of pragmatically integrating people initiatives into strategic business plans to increase value.



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