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Leadership vs. Management

By

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Introduction

Two quarters ago, I authored an article called “Who’s Minding the Store?” Its opening began with a point about the terms “leadership” and “management” being erroneously exchanged as synonyms. This misstep eschews a critical distinction of middle market value-creation algorithm. The Venn diagram below frames the architecture of this article:

- Some good leaders may also be good managers.
- Some good managers may be good leaders.
- Both traits are existential necessities to all business models.
- Excellence in one does not infer excellence in the other.
- Scenario objectives may dictate which skill should be more beneficial.

This article will revisit the leadership versus management theme with supplemental points for contemplating the contrasts and complements of these two vital value-creating skills.

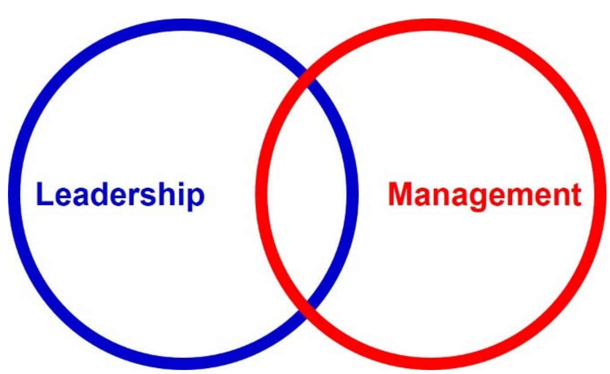

Figure 1: Leadership vs. Management

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Initial Point of Reference

Some private equity investors find the lower middle market alluring for practical reasons, including relatively lower EBITDA purchase multiples. Whereas this statement may be empirically validated, “bargain” prices may mask inherent challenges: those companies may not be configured to realize the investment thesis. Middle Market Methods (“M3”) describes the challenge as the absence of *robustly scalable organizational architecture*. Let us parse that italicized phrase as foundational to the objective of this article.

“Robust” is the root word of “robustly,” an engineering term which in practical parlance means the ability to ingest and digest variation while producing predictable outcomes. Basic training in the branches of the U.S. military are poster children for this phenomenon. Despite the variety of inductees, training produces homogenous models of cognition, physicality, and performance.

“Scalable” alludes to the ability to grow. To be clear, a model can scale without necessarily being profitable. When paired with “robust” as the modifying adjective, “robust scalability” means the ability to grow with predictable outcomes despite occasional speedbumps. Consider a muscle car from my formative years: a 1967 Chevrolet Chevelle Super Sport with a 396 cubic inch V-8. With a few hotrod modifications—such as a full cam, Holley four-barrel carburetor, headers, and glasspack exhaust, the horsepower was sufficiently improved for Saturday night drag racing. What happens when the accelerator is stomped upon the starter flag touching the ground? A “robustly scalable” Chevelle burns rubber as it gains traction toward turning a faster quarter mile than its rival. A deficiently modified Chevelle may suffer some combination of numerous possible anomalies, e.g., a blown engine or snapped universal joint on an over-torqued drive train. (Did anyone think of Beach Boy music after reading that?)

A lower middle market investor must be prepared to address inevitable growing pains.

“Organ” is the root word of “organizational.” The human anatomy metaphor is deliberate. Organs are part of the digestive system. Both humans and business models ingest, digest, and produce. The root word for architecture is “arkhitekton.” In Greek, this means "master builder." Legends like Frank Lloyd Wright strove to reconcile architectural variables like form and function while taming heft and height. Business models have analogous differentiation issues.

“Organizational architecture” is a device M3 wields to get people out of the mindset of “org chart.” Organizational architecture determines whether robust scalability may be maintained irrespective of human asset disaster recovery or business continuity—especially regarding C-levels. This is a massive point of inflection. Many, if not most, lower middle market companies led by founding entrepreneurs have a de facto governance mechanism of control. Symptomatically, a dearth of empowerment results in most decisions being made by the CEO. Whereas this may not necessarily be negatively impactful when the recapitalization is consummated, growth tends to “manufacture” a predictable problem. The CEO may eventually exhaust their bandwidth. Early hints of the developing chokepoint include slower decision making. This is analogous to our PCs locking up when too many open apps and files overwhelm its CPU (central processing unit) and RAM (random access memory) capacity.

Robustly scalable organization architecture is essential to profitable growth.

Further complicating matters is the CEO’s inability and/or reluctance to empower the organization with spans of control accountability. In M3’s observations, a material portion of CEOs who acknowledge the risk and embrace the need for change have trouble with the transition. Indeed, they may be unfamiliar with delegating. It is not as easy as it sounds. Why? Particularly for CEOs whose pedigrees lack experience in larger companies with good governance, perspective is deficient, i.e., they were not acculturated in some basic best practices. When the CEO’s new company was forming, the boss had no one to whom delegation was possible. When their business was starting and evolving, cash may have been tight. Multitasking was normative for budgetary reasons. To wit, someone must do the work. As the company progresses through forming and storming to norming en route to performing, what happens if the CEO foregoes empowerment in favor of autocracy because directing may be more comfortable than delegating?

Unfortunately, some CEOs may never be comfortable relinquishing control. The risk may exceed the obvious. A controlling CEO could become indisposed one second after completing the investment. This is not succession risk. This is replacement risk. Finally, some teams may not be capable of wielding delegated control and/or they may be psychologically anchored in someone else telling them what to do. A "coachable" scenario may be no better than a 50-50 proposition.

Let us bring in Jan and Dean for muscle car Muzak in completing the cycle. "Robustly scalable organizational architecture" means the business model can profitably and predictably grow irrespective of who is at the helm. Indeed, the prerequisite talent pipeline management process finds, wins, and keeps the people capable of consistently delivering to customers in increasing quantities the non-negotiable quality and timeliness of goods and services—all done profitably. Period. Investors assume sufficiency on this necessity at their own peril.

Take-away: Investor diligence should include the leadership team to decipher in WHOM they are investing because the post-close stewardship of that group has major implications for WHAT they are investing.

A Common Conundrum

Succession is a common lower middle market challenge. In contrast to the immediacy of replacement, succession infers a reasonable about of lead time to accomplish the objective. However, either scenario is a protracted proposition which is possibly made worse by timing. A rock star candidate may be unwilling to walk away from a performance bonus.

A selling CEO may rollover a minority equity position as a hedge strategy to keep him/her focused on the business. A typical understanding is that the CEO would stay with the business until the next recapitalization. Alternatively, an employment contract may specify duration less that the estimated investment exit. The “boss shopping” expedition may commence proximal to deal closure, with the deliberate overlap of executives for assimilation and tribal knowledge transfer.

What, then, is the type of executive which a Board of Directors should recruit? Like having an acquisition strike zone for market defragmentation strategies, a CEO strike zone for succession is advisable. M3’s observation is that this is a frequent flub. Recruiters routinely lay siege to Fortune 1000 companies for candidates. This makes sense in many respects, not the least of which is that these candidates are accustomed to governance whose maturity exceeds that of a smaller company. This is a two-edged sword which masks a supremely important criterion: builder vs. administrator. A builder creates something from scratch. At a minimum, a builder must institutionalize dramatic changes to the business model to achieve the investment thesis. By contrast, an administrator largely oversees something established by predecessors. Larger companies may also possess dedicated staffs for continuous process improvement and project management which are absent in smaller companies. In the lower middle market, bold strides are often necessary. Incrementalism does not suffice.

Do CEO candidates’ pedigrees match investment thesis requirements?

A simple point of reference illuminates the point. A common investment thesis is 3xn3, i.e., triple the EBITDA in three years. Ponder the answer if posed to a Fortune 1000 denizen. The revenue numbers alone may seem unfathomable. The interviewer question regimen before punting on a “qualified candidate” might include something like “walk me through an example whereby you created and grew a revenue stream from scratch.”

Placing material qualifiers on the question relative to the candidate's present company make it is necessarily a stretch goal scenario.

Take-way: If the candidate lacks results for operating in a small lab with Spartan tools whereby atoms were transformed into complex molecules, then the likely fit in a smaller company is questionable.

What the Company Needs

Senior executives wielding both world class business development and operational excellence credentials are uncommon. Fortunately, the quest is unnecessary. A successful CEO may be either. However, the right CEO profile for the investment thesis should be anchored in the most pressing company need. If the company cannot keep up with its opportunities, it may need an operator. If the company has excess capacity, it may need a commercialization protagonist.

The primary need of the company should determine operational or business development pedigree.

There is a corollary which also begs attention. A strong primary skillset needs an accountable complement for secondary needs. The secondary needs may be latent with legacy incumbents but require coaching. The question is whether the CEO can do the coaching and gauging the consequences if the CEO cannot. The symbiosis between the primary and secondary responsibilities should be as artfully graceful as ballet dangers.

The Apostle Paul memorialized an axiom that even secular circles ponder: "Money is the root of all evil." What if money is only the enabler of the "real" root of all evil: power. Nineteen century Member of Parliament Lord John Emerich Edward Dalberg-Acton observed that "power corrupts, and absolute power corrupts absolutely." Power is addictive. What does this have to do with the lower middle market? Hoarded power is antithetical to modern value-creation best practices. For either type of CEO, beware the

"I" versus "we" phenomenon. Robustly scalable organizational architecture in the lower middle market requires full engagement of all employees. The rules of engagement by which leadership and/or management are/is applied is integral to leveraging the talent pool. Open-ended questions to CEO candidates should reveal the values by which their success was influenced. The Board of Directors should satisfy themselves that those values align with the company's aspirations. Values of the individual and the organization need not be identical, but they must be compatible and enabling.

Take-way: Focus on the company's most pressing need when recruiting its next leader.

Leadership versus Management

Leadership and management are not entitlements. They are earned responsibilities. The great executives religiously prepare for the opportunity to be recognized as ready. When assigned the role, they rally their charges with energy and conviction. However, they may—and likely do—go about it differently.

Let us revisit Peter Drucker's axiom: "Leaders do the right things; managers do things [the] right [way]." These typically are chameleon characteristics for great C-levels.

Style fluidity in deference to scenario is a virtuous capability.

Perhaps doing the right thing is a strategic trait, i.e., vision; whereas, doing things the right way is a tactical attribute, i.e., execution. Stated another way and in ecclesiastical fashion, there are distinct seasons for each attribute. Clearly, both skills are needed in C-levels; however, there tend to be proclivities for one versus the other. The rhetorical question is whether the chameleon senses which color is required for the season. This may be perceived as a left hand-right hand phenomenon. Either side may be dominant, but it takes both to clap.

George Bernard Shaw immortalized a useful quip for a point: “You see things, and you [ask] “Why?” . . . I dream things that never were and I [ask,] “Why not?” Both leaders and managers may map to Shaw’s philosophy, but though different prisms. Leaders may be invested a dream; managers may obsess over superlative results. Leaders may be comfortable in the abstract; managers may be grounded in the concrete. Leaders may pioneer the new; managers may make the familiar more productive.

One of my early mentors described leaders as those who create chaos to preclude dulling of the senses by entrenched bureaucracy. Chaos can be an antidote to groupthink. Managers subsequently distilled the chaos into sustainable action. Walter Isaacson documented Steve Jobs’ challenge to Apple’s product developers as the “reality distortion field” to tame the seemingly impossible. The reward for consumers is the enjoyable, iconic products and services. One of the traits of this phenomenon is thus: leaders may be more prone to hiring talent for which no position exists; whereas managers may be more inclined to fill open positions.

A leader or manager who eschews continuous learning is dangerous.

What might this look like using Vijay Govindarajan’s model as depicted in *The Three-Box Solution: A Strategy for Leading Innovation*? One box protects the sustainable and core value-creation drivers of the business model. Some may see this as the cash cow of a business. However, like bovine creatures, legacy revenue streams are mortal and may exhaust their useful lives. The leader must continually critique the viability of the core business. The Porter Five Forces Model is a useful tool for such scrutiny. Whatever the decision, the manager profile assures productive execution by the most appropriate means.

Another Govindarajan box regards deliberately removing blinders that prevent the business from defining its future. More tersely speaking, all businesses need to stop doing some things over their course of their existence. Product lifecycle management abides this challenge. Deliberate retirement of a product is a firewall preventing expensive, antiquated production support and maintenance costs. It may take the leader to declare “it’s time” and a manager to methodically retire the impediment or separate the company from the obstacle.

The third Govindarajan box is creation. A leader must build a fortress around disruptively innovative endeavors, i.e., a skunkworks. The initiative must be protected from the core business because the “new” is threatening to the status quo. Clayton Christensen wrote extensively on the topic of disruptive innovation. Agile is a valuable technique for failing forward quickly in pursuit of a minimally viable product whose market traction fuels feedback for improving iterations.

Emotional intelligence, or EQ, is more valuable than technical skills. Daniel Goleman delivered an epistle on the subject which has proselytized legions as evidenced by its 10th edition. A layman’s definition of EQ is the ability to promptly read people as a precursor to adjusting one’s style for more effective communication. Celebrated novelist Ann Patchett’s “What Now?” commencement address to her Saint Lawrence College alma mater offered some nuggets for how she developed her EQ modus operandi by putting her journalism degree to work as a waitress. She expressed joy in her epiphanies to include humility and teamwork. Perhaps Patchett’s conveyance is tantamount to empathy and perspective. How can anyone understand how sustainable and scalable value may be created if they ignore (i) validating the customer value proposition and (ii) experiencing the value chain from their employees’ perspective?

The ability to connect with people is priceless.

Continuous learning is necessary to remain competitive. Steven Covey described this as “sharpening the saw” in *The 7 Habits of Highly Effective People*. All knowledge has a half-life. Talent development is non-negotiable. The business model’s “university” curriculum imbues desirable, differentiable skills. There are five learning styles: visual, auditory, written, kinesthetic, and multimodal. Individual learning profiles are akin to fingerprints—and contextual emphasis may differ. Leaders make sure the required skills are identified and training is funded. Managers make sure that the learning curve progresses promptly through competency, proficiency, and excellence.

Simon Sinek explains that effective leadership explains the “Why?” behind the “What?” Managers focus on the “How?” and “When?” In unvarnished terms, if subordinates follow a person because they believe in what is explained to them, then that is leadership; if subordinates comply with a directive from someone with position authority, then that is management.

Followers are a prerequisite for leadership. The most effective leadership is influential. Coincidentally, it is also the least efficient. Subordinates define management. The most efficient execution is by directive. Coincidentally, it is also the least effective and risks collateral damage. Both leaders and managers operate between the bookends of effectiveness versus efficiency as dictated by the situation. Wise leaders and managers explain the ground rules for those occasions.

Excellence is not a birthright. It is a perpetual quest.

No one is a born leader or manager. It takes mentoring, training, and practice—and relentless, maniacal resolve to be the best. Sadly, not all people in official positions were trained to occupy them. Who developed the talent to guide the company which investors want to own? Who is developing existing employees and new hires to deliver the investment thesis? Both questions must be answered by someone responsible to the Board of Directors.

Zig Ziglar pithily imparted that “your attitude, not your aptitude determines your altitude.” During the darkest hours of World War II, British Prime Minister Winston Churchill rallied his citizenry with the attitudinal inspiration “we shall never surrender.” The manifestations of a winning attitude are further conveyed in Admiral William H. McRaven’s 2014 commencement address at The University of Texas at Austin whereby he described Navy Seal training, beginning with making one’s bed in the morning. Admiral McRaven explained the importance of beginning each day with foundational success. *The Wall Street Journal* published it, so it is easily found on the web. Treat yourself to the tale of warriors. The common denominator across these three examples is psychological discipline to succeed, i.e., mind over matter.

Take-away: The Board of Directors should know the criteria by which the CEO gets to the right things before doing them the right way.

Conclusion

A recent tweet found me. The alleged author is Richard P. Feynman, PhD, and contributor to the Manhattan Project. Interestingly, he died 18 years before Twitter was founded. Wonders never cease. In any event, @ProfFeynman tweeted something timelessly profound: “Knowledge is having the right answers. Intelligence is asking the right questions. Wisdom is knowing when to ask the right questions.” For some reason, I had a flashback of Forrest Gump’s soliloquy at Jenny’s graveside whereby he wondered if we are predisposed to destiny or “it happens.” (The beneficiary of Gump’s quip added a couple of letters before “it” for the caption beneath the smiley face upon a t-shirt.) Forrest reasoned that it was probably both. Analogously, professionals are leadership and management hybrids. What determines the rock stars from the lab rats? Perhaps it is the ability to blend the leadership-management ratio relative to circumstance.

When leaders and managers prepare their teams and deliver results, it garners attention. As poet Dr. Kent M. Keith describes it in “The Paradoxical Commandments,” “If you are successful, you will win false friends and true enemies. Succeed anyway.” Stoics prepared for this suffering with peace of mind. Works for me.

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