Middle Market Methods™

Value Creating Solutions in Private Equity

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The Four Horsemen of the Deal Team Apocalypse

By John A. Lanier

Over 10 years, across 24 sponsors, for over 100 portfolio companies, and beyond 300 deliverables, certain patterns emerge. Let’s call these an 80-20 observation from *Middle Market Methods*™’s vantage point. This article addresses one such observation. Deal teams should think critically about four behavioral enemies of value creation. We call these The Four Horsemen of the Deal Team Apocalypse.

Procrastination

The human condition is punctuated with preferences and avoidances. Deal teams are no different. The sizzle is in the next transaction. Comparatively, the operational side of the investment is boring. However, execution vindicates the investment thesis. Moreover, small, unattended problems may metastasize into full-scale crises.

Procrastination, denial, alpha-dog behavior, and hoarding are enemies of value creation.

Assuming the dashboard metrics have a practical mix of leading and lagging metrics, i.e., input, process, and output metrics, questions should be asked routinely about underlying root causes for variation against expectations. No different than a medical diagnosis, early detection and treatment underwrites good fiscal health.

The points are simple. First, measure and analyze the “right things.” Second, react quickly to variation to verify whether it is a hiccup or a developing trend.

Denial

Denial regards self-deception through cognitive dissonance, i.e., filtering out stimuli contrary to one’s existing paradigm of “reality.” What’s the difference between denial and procrastination? They are first cousins. Whereas procrastination regards delaying execution that one knows should happen, denial is the inability or refusal to see the obvious need for action. For example, one who delays writing their will is a procrastinator. One who eschews the wisdom of a will is in denial.

Denial adopts irrational conclusions about negative dashboard metric variance. To wit, “This cannot be right (because we just renegotiated bank covenants)! Root cause(s)? Perhaps the forecast assumptions were flawed, the tracking metrics are unaligned, or both.

The most common area of denial witnessed by *Middle Market Methods*™ regards portfolio company leadership teams. In Jim Collins vernacular, this regards the right people, with the right skills, in the right positions, at the right time.

Private equity transactions often place new responsibilities on portfolio company C-levels. Absent the aptitude and attitude to learn, the correct decision is a fait accompli because these C-level professionals are not sufficiently equipped to execute the responsibilities of their roles relative to the investment thesis.

Great leaders chronically struggle with tough personnel decisions. Upon making the decision, most lament their denial that resulted in value-destructive procrastination.

Alpha-dog behavior is a euphemism for control.

Alpha-Dog Behavior

“Alpha-dog behavior” is another way of saying “control.” For openers, “control” is illusionary. Leaders only accomplish great performance through proselytized followers. Followers do not commit until they internalize the WIIFM—“What’s in it for me?” In deference to this new reality, leadership styles have changed dramatically over time. This entails abandoning command and control dicta in favor of more inclusive and collaborative styles.

Leadership style evolution is somewhat a generational phenomenon. Millennials have a different “flight-or-fight” DNA from baby-boomers. Millennials’ version of Maslow’s hierarchical aspirations of fulfillment and self-actualization has different definitions.

A recent client experience encapsulates the point. The managing director fumed, “Doesn’t the (portfolio company) leadership team understand that they should be grateful to have a job in this economy?” Since the U.S. has enjoyed a basically robust economy from 1983 until 2008 (notwithstanding the mild recessions following Desert Storm and the dot-com bubble), millions of employees have a skewed perspective for “tough times.”

The picture is complicated. Sandwiched between employees and deal teams are C-levels. These C-levels may struggle with deal team directives. Why? Some deal team members lack managerial experience that translates into credibility chits with the C-levels. Recessionary dynamics exacerbate the phenomenon.

Hoarding

Hoarding is the antithesis of delegation. What's the difference between hoarding and control? Actually, they, too, are first cousins. However, whereas control is a power manifestation of centralized decision-making, hoarding is related to execution. A prime symptom of hoarding is "around-to-it." Translation: I'll get around to it (eventually).

Two counterpoints are offered. First, even Superman is vulnerable to kryptonite. Second, there are only 24 hours in a day; consequently, bandwidth is a finite commodity.

The solution is to prioritize and delegate to the lowest level of functional competency. This may be within the firm, within the portfolio company, or to an outsourced vendor.

Hoarding is not a sign of strength. Hoarding may be viewed as a sign of insecurity. Moreover, hoarding may limit upward career mobility. A sage mentor once quipped, "If you cannot be replaced, you cannot be promoted."

Relationship-minded vendors mentor their clients to transfer knowledge.

Effective leaders delegate. They also respect followers who push back for clarification on priorities and the corresponding execution implications. Successful leaders engineer efficiently executed deliverables. Superior leaders do not burn out their subordinates.

Summary

Many seasoned veterans opine that the more they learn, the more they realize how little they actually know. The "I don't know" epiphany may be a healthy step toward value creation. The litmus test for leadership is what such professionals choose to do when confronted with the unknown.

Electing to master new skills is laudable but time consuming. Outsourcing to subject matter vendors is a viable alternative. Relationship-minded vendors mentor their clients to transfer knowledge. The decision-drivers are speed, costs, and benefits, i.e., IRR on the value-add. Value creation hangs in the balance of the decision.

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Middle Market Methods™'s tool box keeps deal teams doing what they love without worrying about what they loathe.