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Synthesis

Made for each other? What makes you so sure?

Assessing management teams is a crucial element of any due diligence as part of an M&A process.

By Sushmitha Swaminathan, Egon Zehnder, and Felix Kusch, AVIV Group / Axel Springer Digital

What makes an investment flourish or fail? In answering this vital question, investors must weigh up many complex factors. One key element is the quality and fit of the management team – which plays a defining role in the success of any merger or acquisition.

Nevertheless, management team assessments are often carried out in an unstructured, informal manner. In the current environment, with longer investment cycles, this can no longer suffice; it is essential for any investor to invest in HR due diligence before taking the plunge. Conscientious investors must find ways of gauging how a management team functions – as individuals, and as a whole. This can be challenging, particularly if interaction with the team is limited.

There are several important dynamics to observe here: How well does each member of the management team meet his or her job requirements? Do individuals' skills and personalities complement each other – do they work well together? And lastly, how does the team view the future evolution of their organization?

Matching the right person to the right job

An introverted sales director? A CFO with no head for numbers? Hold on a minute! Unfortunately, leader personalities often do not match or meet the key requirements of their jobs; this turns up in due-diligence processes more often than an unsuspecting investor might assume.

To assess the fit of a senior executive to their current or possible future roles, it's helpful for investors to take a three-step approach:

- Before meeting a leader, analyze his or her work experience, education and any available references.
- During management meetings, gain an understanding of how that individual views his or her role.
- Finally, judge the extent to which mismatched personalities and skillsets might negatively affect an investment, and consider how to remedy this problem – in extreme cases, replacing an unsuitable individual should be an option.

This last point is tricky: It's rarely the case that an investor can simply "sack" a business executive. Investors can often do more good, and ultimately get more value, by avoiding the upheaval associated with the exit of a long-term team member.

In our experience, a good compromise is often to move such executives into less operational roles – such as onto an advisory board, where they can act as the interface between investor and company.

Forming a united front

In any management team, individual members need to mesh to form a cohesive whole. Personalities should be complementary: An introverted, analytical person might channel the energy of an extrovert. Skillsets, too, should fit together: One person may cover analytics and financials, for example, while another focuses on sales. And ideally, the team should share a common history, enabling them to get along and shrug off any upsets.

Attending management team meetings allows potential investors to understand how the team interacts. In order to assess individual members, investors should request that each one make a presentation, or lead part of a discussion. Even management meetings held via video (now common due to COVID) can be helpful here: A video conversation can reveal much about management culture, as well as potential conflicts.

Remember to show your "nice" side: Investment is a two-way process, and executives might bristle if an investor appears arrogant or overly critical. Carefully consider your personnel decisions, so as not to derail the process or create bad blood before the real, post-investment work begins.

Looking to the future

A management team that is keen to add new investors needs to demonstrate strategic foresight: Going forward, how do they plan to build and strengthen the organization? How much freedom will they have to foster a modern work culture, enabling the organization to react swiftly and in an agile way to developments? Do they understand where and how new hires, such as an additional middle-management layer, might aid the operation? Strategies should be in place for dealing with the organization's historical debt as it ages and matures, or for further developing colleagues when they outgrow their current role.

When pondering a deal, an observant investor should be alert to all these strengths and weaknesses. But they should not stop there. As in other investment-critical areas such as go-to-market strategy or pricing, the due-diligence process is the ideal starting point for drawing the roadmap for a company's future.

Ideally, investors should continue to engage in a structured dialogue with their management team post-deal, to bring the company's organization to the next level. In our experience, such a process may be lengthy – up to a year; but if conducted well, it can bridge the gap between pure analysis (in the due-diligence phase) and getting things done on the ground.

Assessment is only the first link in the chain of building a talent and development culture. All too often, it is a neglected aspect of the process – but it is one that a modern, diligent investor cannot afford to skip.

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About Egon Zehnder

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