Forbes

Hiring A New CEO? Go Outside The Company

By Klaus Kneale

Chief executive officers promoted from within a company don't perform nearly as well as ones recruited from outside. That's what a new study by **Vell Executive Search** found. The study looked at 51 CEOs and their companies' revenue growth, focusing on publicly owned technology outfits based in New England with $100 million or more in annual revenues.

Externally hired CEOs at companies with over $1 billion in revenue brought in a median three-year revenue growth of 99%; their internally promoted counterparts achieved only 35% growth. Founders, which were concentrated in smaller companies, outperformed both of these groups.

Dora Vell, CEO at the firm, says founders generally know their product, industry and customer better than anyone. But why would an outside CEO do better than an inside one? Vell says it comes down to the hiring process.

Some CEOs avoid surrounding themselves with strong top-tier executives, Vell says, because they don't want internal competition. This can make for a weak pool of homegrown candidates, and the result can be the wrong person in the job, especially if the company is trying to please long-term directors.

Also, the chance that an internal hire will be willing to break with existing strategy or set truly new goals seems lower, so the company will have more difficulty adapting to changing market conditions. This seems particularly evident in technology businesses.

Robert Calderoni, CEO of the management solutions company Ariba, adds to that explanation: "Typically when a company goes outside for a candidate, either the company is in crisis or the board recognizes a need for change for some other reason. The external candidate typically has a platform for change and is unburdened by the status quo. The internal hire often is married to the past or was involved in creating it."

Another finding: The best CEO is an experienced CEO -- in most cases. Vell correlated CEOs' performances with their backgrounds (strategy, consulting, engineering and so on); with all backgrounds but one experience trumped inexperience. CEOs with prior CEO experience did better. No surprise. What faltered? Finance.

CEOs with no experience in finance running companies with revenues between $100 million and $1 billion oversaw median three-year revenue growth of 91%. CEOs who had been in finance returned just 43%. That may reflect the times we're in. Fast financial moves just don't work these days, and CEOs with a number-crunching past are probably more likely to have focused on money than on the underlying business. "You can't save your way to profits," Vell says.

Experience in venture capital and private equity made the best showing, with three-year revenue growth of 200% vs. 82% more generally. The advantage to that kind of experience, Vell says, is that you've seen many companies on the inside, learned first-hand what works, and gotten used to managing multiple accounts at once. It certainly doesn't hurt that someone with a venture capital or private equity background is probably more likely to pick a successful company to run. VC is the decathlon of CEO training.

Hiring A New CEO? Go Outside The Company

By Klaus Kneale

The survey also found that younger CEOs returned better results than older ones, though again that might be more true in tech than elsewhere. CEOs who had been on the job seven or more years did worse than ones who had served three to six. That too may reflect the peculiarities of tech.

Vell also looked at how CEOs who were also chairmen did compared with CEOs who weren't. That question, she conceded, needs more study. CEOs who weren't chairmen performed better, but Vell thinks they may still be virtual chairmen, avoiding the title so they can share responsibility without sharing power.

Finally, an age-old question: Do Ivy League grads make better CEOs? Yes. Ivy-Leaguers at companies with revenues of $100 million to $1 billion enjoyed median three-year revenue growth of 287%; non-Ivies managed only 86%. Even the worst growth for an Ivy-run company broke 40%; non-Ivies saw as bad as a 20% decline.

Similarly, MBA grads in the same group managed median growth of 159%; non-MBA grads, only 89%.

CEO selection is a difficult business. Vell says that taking the less expensive or less qualified CEO rarely works out at all. Such a CEO often makes a mistake in the first few months on the job that loses the company more money than it will ever save on compensation.

Some CEOs are actually worth their pay.

Dora Vell *is the CEO of* ***Vell Executive Search****, a premier retained technology executive search firm in Boston. Ms. Vell is an internationally recognized expert in recruiting technology executives including: CEOs, COOs, CTOs, CMOs, CROs, board members and others. She works with VC-backed, PE-backed private companies and public companies. She can be reached at dora@vell.com.*