CHIEF FINANCIAL OFFICERS IN PRIVATE EQUITY FUNDED COMPANIES

Functional Competencies and Behavioral Attributes Critical for Success

BY KEITH GIARMAN, GLOBAL LEADER PRIVATE EQUITY PRACTICE
Dear Private Equity Professional,

As global leader of DHR’s Private Equity Practice, I am pleased to present our white paper exploring the leadership and functional competencies of Chief Financial Officers that lead to success in private equity sponsored companies. One might argue that these attributes are required in any company - public, private, or PE funded. That being said, as the key partner to the CEO on the executive team, and a primary contact with investors and the Board, the CFO plays a critical role in ensuring true value creation in PE funded companies.

Having successfully completed hundreds of C-level search assignments working with our PE clients (CEO, COO, CFO, and many other roles), we look for trends related to hiring practices, organizational structure, leadership and team assessment, executive level competencies, Board governance, equity and cash compensation, and so forth, which are of interest to our clients. As the fifth largest and fastest growing retained executive search firm in the United States, DHR International has made a strategic commitment to the private equity industry and will continue to explore human capital issues as part of the Private Equity Practice charter. We hope you find the white paper informative and look forward to being of service to you and your firm in the near future.

Best,

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R. Keith Giarman

Global Leader, Private Equity Practice
Introduction

Some consider the skill set of the Chief Financial Officer (CFO) to be more “portable” from industry to industry or business model to business model than other senior level members of the executive team. Based on the experience of our clients in the Private Equity Practice, the core financial acumen and analytical competencies of an effective CFO can be appropriately applied in different industry or business settings; however, their success will depend on a multitude of situational factors. Is the CFO who successfully partnered with the CEO to grow a company and related infrastructure from $25 million to $100 million qualified to do the same in a company growing from $250 million to $1 billion? Perhaps not. Stage and proof points from prior experience matter.

Core financial functional expertise must be coupled with strong leadership skills and a tight cultural fit that meets the business inflection point of the business. While the determination of the best profile for any executive role is situational, success will always hinge on the successful assimilation of the CFO into the company, its culture, and onto the executive team. DHR has isolated certain characteristics of successful CFOs that are routinely defined by our clients as critical for success in private equity sponsored companies (regardless of industry focus or strategy).
The CFO is an effective leader and organizational manager acting as a partner to the CEO and focuses on specific strategic and operational initiatives that support the well-defined value creation objectives of the business.

Great CFOs know how to engrain the analytic engine of finance into the fabric of the business. They and the overall finance team help focus the entire business on key financial objectives that support the value creation plan of the entity – moving from reactive measurement to proactive forecasting and analysis, while not losing sight of the basic accounting and control functions. Thus, the CFO must not only have tremendous analytical skill and financial acumen working with the CEO and the Board, but he or she must have deep organizational management skills to build relationships with business peers and cultivate a motivated finance team to operate in a manner that supports the key objectives of the business (as opposed to basic reporting and accounting).

The CFO is innately curious, with a keen eye for continuous improvements steeped in the development and deployment of Key Performance Indicators (KPIs) that measure and therefore promote profit and cash flow.

The most effective CFOs want to learn and develop a truly in-depth understanding of the business and how to create value. Innately curious and focused on profit, the CFO is maniacal in developing the metrics that reflect and ultimately help predict true business performance, deploying and adjusting KPIs, working with the general managers, running the business, and activating the finance team to provide the objective measurements, systems, processes, and controls that will yield continuous improvement in the business for the long-haul. Importantly, this is not a static process; KPIs must be monitored, adjusted, and improved as business conditions evolve.

The CFO has a quantitative intellect and fluency with numbers that enables effective management of the controller and accounting functions, but does not need to be fluent in the intricate mechanics of accounting.

It would be impossible for a CFO to succeed without the numbers-oriented analytical skill that allows him or her to effectively manage the overall functions of the organization, especially the controller function. However, in most cases a CPA and/or deep accounting experience is not needed to succeed. While it would be unfair to assume that an executive steeped in accounting cannot rise to the strategic and operational capabilities required to partner well with the Board and CEO, the broader and more strategic training that comes from more generalized business experience, and perhaps MBA education, may be more suitable. Great CFOs need to manage accounting, not understand every detail of the accounting process, but will require a very strong executive who occupies the Controller role for the company.
Cash Flow Driven

The CFO knows how to manage and improve a business with a leveraged balance sheet focusing on cash flow as the key indicator of entity health.

Unlike some environments, PE funded companies are aligned with the Board, CEO, and management in driving a return on investment scenario that is positive for all stakeholders along the way. Typically, the investment thesis includes some meaningful leverage in the business to achieve business results. Thus, the company must pay down debt as part of its daily, weekly, and monthly objectives, and the CFO must see this as a critical part of the team’s charter. As the company drives towards liquidity via sale or IPO, the finance team must focus the organization on both cost and revenue-related activities that lead to increased and sustainable profit and cash flow post-acquisition.

External Manager

The CFO is not just a strong internal manager, but is also effective working with banks, capital market players and outside service providers (like audit firms) as part of their team’s duties.

CFOs and their team must know how to deal effectively with the players that require proper management of cash flow and proper capitalization along the way, both critical to a healthy balance sheet at all phases of the company’s performance against the agreed-upon value creation plan. This includes working with banks and other entities who have provided the debt associated with the business. The CFO and their team must also work constructively with institutional investors during capital-raising activities, investment banks during public offerings, and audit firms that ensure proper compliance during the life of the investment while private.

Thinks Like an Owner

The CFO, like the CEO and others on the executive team, thinks like an owner of the business.

In summary, great CFOs of private equity sponsored companies think like an owner of the business and apply a willful long-term management approach that results in “followership” throughout the organization (not just the finance organization) in the fulfillment of their duties. Investment-related decisions are driven by a thoughtful, fact-based, and strategic process that aligns with the value creation plan - a process where capital is spent wisely and intelligent resource allocation is the mantra. Accordingly, there is rigor in determining when to spend money on what and how it supports business priorities and financial transparency along the way. Equally important, there is tremendous emphasis placed on measuring the accuracy of financial decisions tied to verifiable business results with well-defined KPIs that align with the value-creation plan. There is a “closed loop” where real-time learning and continuous improvement feed the evolving strategy and value creation plan of the business.
This white paper was prepared by Keith Giarman, Global Leader of the Private Equity Practice at DHR International. Please contact Keith Giarman at (415) 617-6234 or kgiarman@dhrinternational.com for more information related to the report, DHR's services or future events.

Keith Giarman serves as Global Leader of the Private Equity Practice in the firm’s San Francisco, CA and New York, NY offices. He is also part of the firm’s Advanced Technology, Financial Services, Board & CEO, and Financial Officer practice groups.

Mr. Giarman oversees C- and VP-level search assignments in portfolio companies working closely with boards, management teams and their investors where the mantra is accelerated value creation, growth, profitability and liquidity. He also works closely with top-tier principal investing funds in the build-out of their investment, portfolio support and related teams. Prior to DHR, Mr. Giarman built the CEO practice for one of the premiere boutique executive recruiting firms in Silicon Valley serving the venture capital community.

Mr. Giarman has worked extensively with investors in prior operating roles in companies at various stages of growth, most recently as president and CEO of Clarus Systems (acquired by OpNet) where he raised more than $20 million to launch the company. He has also held operating or consulting roles working with other start-up and PE sponsored companies, including IAsia Works (IPO), NightFire (acquired by Neustar), Cygent (acquired by Convergys) and Sintec (acquired by Riverwood Capital).

Prior to his executive level experience in Silicon Valley, Mr. Giarman was vice president of sales, service, and marketing at Citizens Communications (NYSE: CZN), today a $3 billion full-service communications carrier that was merged with Frontier. He was one of five executives on the senior leadership team and was responsible for an organization consisting of 800 employees, $1 billion in revenue, and $200 million in operating income.

Mr. Giarman earned his BA at the University of California, San Diego (where he played varsity baseball as a catcher) and his MBA from Harvard Business School (where he was recruited into the PhD program in leadership and organizational behavior). Mr. Giarman is a former member of the board of trustees for Schools of the Sacred Heart in San Francisco where he chaired the President’s Evaluation & Compensation Committee and was chairman of the board’s Search Committee overseeing the successful recruiting of a new president for the institution in 2012. He is also a former member of the board of trustees at the Hopkins School in New Haven, CT and former chairman of the Western region board of Jumpstart based in Boston, MA. He is an advisor to several technology companies and funds, including Zapoint, Aktana, Factor Lab and Taldan Capital.
Established in 1989, DHR International is one of the largest retained executive search firms in the world, with more than 50 offices around the globe. We conduct search assignments at the board of director, C-level, and functional vice president levels. DHR’s renowned consultants specialize in all industries and functions in order to provide unparalleled senior-level executive search, management assessment and succession planning services tailored to the unique qualities and specifications of our select client base.