PROOF POINT

KORN FERRY
Institute

Develop and select the best CEOs.

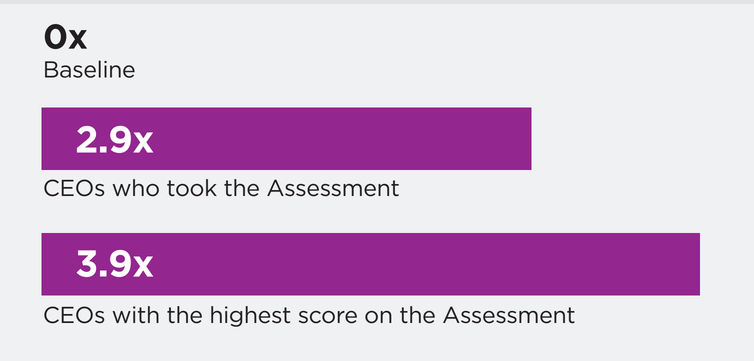
CEOs who scored high on rigorous assessments were four times more likely to lead companies in the top 20% of financial performers.

The influence of CEOs at public US companies has increased substantially over the last six decades (Quigley, Crossland, & Campbell, 2016). The “CEO effect”—the variance in firm performance that can be statistically attributed to CEO-level factors—rose significantly between 1950 and 2009 (Mackey, 2008). Given the growing influence that CEOs have been found to have on shareholder value, it has become more critical than ever to ensure effective CEO succession.

The Korn Ferry Institute studied 229 leaders who participated in Korn Ferry’s CEO Assessment and later became CEOs. The research found that the companies of CEOs who scored high on the Assessment were 3.9 times more likely to be a top financial performer.

Additionally, the research found a clear positive developmental benefit of the assessment experience: Regardless of their score on Korn Ferry’s Assessment, CEOs who went through the assessment, which includes in-depth development feedback, were 2.9 times more likely to be at a top financial performer than a competing company. These outcomes suggest the assessment has a track record for measuring which candidates are ready to be successful CEOs but also provides critical developmental input for candidates with the potential to become CEO in the future (see Figure 1).

Figure 1
How much more likely were the CEOs to be strong financial performers compared to competitor companies?



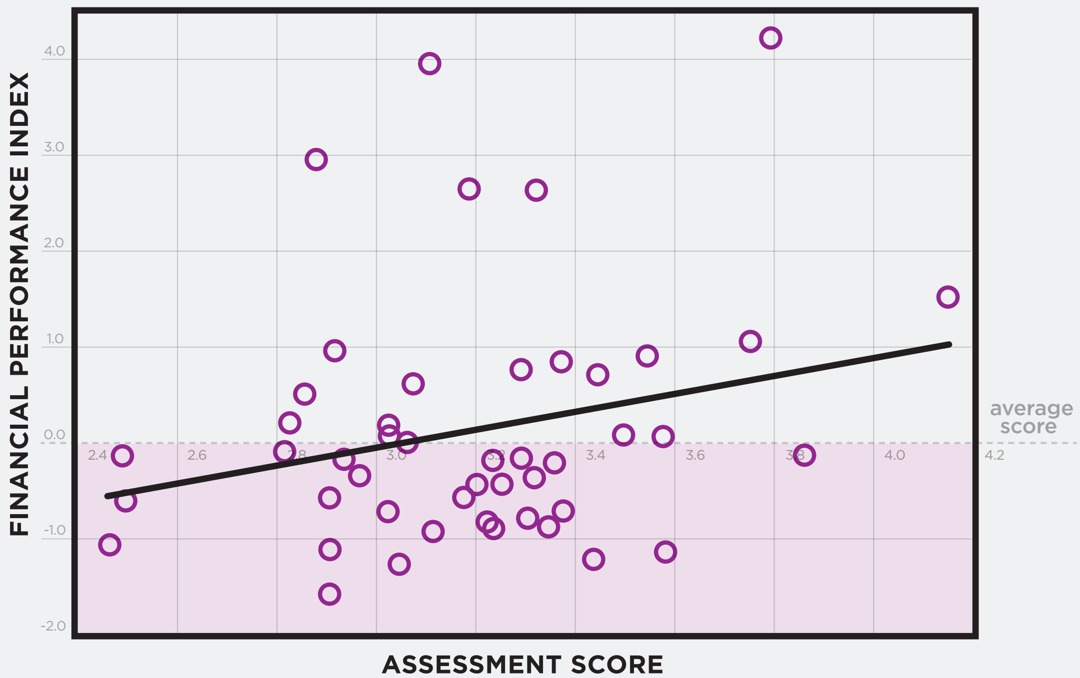
Putting CEO candidates through a rigorous assessment has clear benefits for organizations: CEOs who scored high on Korn Ferry’s CEO Assessment, which includes a daylong business simulation, were 3.9 times more likely to lead companies in the top 20% of a financial performance index. Additionally, CEOs who went through the CEO Assessment, regardless of their scores on it, were 2.9 times more likely to be in the top 20%.

Using publicly available data,[1] CEOs' companies' financial metrics were gathered from the year the CEO first took office until he or she departed, or until 2016. Financial metrics were gathered for CEOs' companies as well as for more than a thousand competitor companies organized into competitor groups, with on average five competitor companies per CEO company.

Six financial metrics were collected between 1995 and 2016: revenue, market cap, stock price, earnings per share (EPS), total shareholder return (TSR), and earnings before interest, taxes, depreciation, and amortization (EBITDA). The metrics were standardized and integrated into a Korn Ferry financial performance index (FPI) for a total of 186 companies and competitor groups.[2]

There was a positive correlation between Assessment performance and the financial performance index score. In other words, CEO candidates who did better on the Assessment on average lead companies that placed higher on the financial performance index (see Figure 2).[3]

Figure 2
Score on the financial performance index by assessment performance



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[1] Primarily from the following databases: Bloomberg, CapitalIQ, and GuideStar.

[2] A number of the CEOs run private or non-profit organizations for which no financial metrics were found.

[3] The correlation between overall Korn Ferry CEO Assessment score and score on the Korn Ferry financial performance index was $r(86) = .21$, $p = .047$. Assessment scores ranged from 2.38 to 4.15; financial performance index scores ranged from -1.76 to 4.24. A score of 0 on the financial performance index indicates average performance.

The research found that CEOs who did the best on Korn Ferry's Assessment were nearly four times more likely to be a top 20% financial performer.

Study after study shows that companies are not adequately prepared for CEO succession. Organizations might be missing this important opportunity for a multitude of reasons: the task is viewed as a one-off occurrence instead of a continuous strategic priority; the process, with so many unknowns, seems too nebulous to institute; there is a desire to avoid a "horse race"; or the board and CEO disagree on successors and therefore end up at a standstill. As with any seemingly overwhelming task, however, a few small steps can make all the difference. The first step is for the board to create a CEO success profile that aligns with the company's future strategy. Doing so will help the board identify near-term successor candidates who can be assessed for their readiness for the role, while identifying other longer-term candidates with potential.

Conclusion

Taking the right steps toward a proactive approach to succession starts with the success profile, before moving to identifying high potentials, assessing their readiness, and finding ways to accelerate their development. The highest performers on Korn Ferry's CEO Assessment were found to have the greatest positive financial impact on their organizations. In addition, simply going through the assessment may have development benefits; even candidates who scored lower and eventually became CEOs outperformed the competition.

The average CEO tenure is known: eight years (Korn Ferry, 2017). The average turnover rate for CEOs also is known: 14.2% in 2016 (Strategy&, 2017). Yet many organizations fail to institute a CEO succession plan that successfully anticipates the next transition. Crucially, a CEO succession plan offers a seamless and planned transition for the sustainability of the organization, ensures alignment of the top leadership to the future strategy, and provides a safety net in case of emergencies. Employing Korn Ferry's CEO Assessment adds an additional safety net: People who do best on the assessment have a greater probability of becoming top performing CEOs.

Korn Ferry's CEO Assessment takes candidates through a day in the life of a new CEO of a fictional global company with a diversified portfolio of businesses. As CEOs, candidates must develop growth strategies that may involve investments, acquisitions, or divestitures of current businesses. They undergo exercises in which they interact with key internal and external stakeholders (who are Korn Ferry assessors). They must address issues ranging from sluggish top-line growth, investor concerns over missed expectations, executive team alignment, low employee engagement, and others. Also included are structured behavioral and market interviews, personality and conceptual reasoning tests, and 360° feedback or reference checking. Candidates receive rich feedback and coaching throughout and work with a coach to craft a leadership development plan.

References

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