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LEAPFROG SUCCESSION

A NEW TREND IN APPOINTING CEOs?

By Roselinde Torres, Gerry Hansell, Kaye Foster, and David Baron

Corporate boards of directors are increasingly reaching down below the second layer of management to name new chief executive officers. By accelerating the promotion of these executives, boards hope that the new CEOs' ability to understand and act upon signals in today's unpredictable environment will more than offset their relative inexperience.

Many of these new CEOs were only in their thirties when they were appointed. Marissa Mayer was 37 when Yahoo! named her CEO. She had been a vice president at Google. Burger King selected 33-year-old Daniel Schwartz to be CEO even though he had only three years of fast-food experience. The board of Electronic Arts passed over two older internal candidates to name Andrew Wilson, 39 at the time, as CEO.

It is fast-track promotion, not age, however, that defines these "leapfrog leaders." Mary Barra of General Motors and Mark Bertolini of Aetna, for instance, were in their fifties when they became CEOs. If most CEOs come well seasoned from the second management level, or L2, these new CEOs are often accelerated from L3. We are in the early days of studying this phenomenon—and determining whether it represents a coincidence, fad, or trend. We are trying to understand the forces driving these appointments, the common characteristics of these new CEOs, whether they are concentrated in specific industries, whether they are effective, and what will improve their odds of success.

Leadership Context

Each unconventional CEO appointment, to paraphrase Tolstoy, is unconventional in its own distinctive way. Even so, two broad scenarios can be discerned in most cases.

First, a high-performing and dependable CEO is coming up for retirement but is persuaded to stay on in order to provide a steady hand on the tiller, to weather an upcoming storm, or perhaps simply to maintain progress. So the incumbent CEO remains at the helm for an extended period, contrary to the recent tendency toward shorter CEO tenures. (See Exhibit 1.) The members of his or her senior leadership team likewise extend their tenure. By the time the CEO does finally retire, however, conditions are more complex and uncertain. The company now needs a change of course and a new type of leader who has more relevant experience and a more future-oriented perspective. The potential L2 candidates have, or are perceived to have, profiles that are too similar to that of the long-serving CEO. Boards—and commentators—may therefore view them as "institutionalized" at a time when fresher, outward-looking leadership is needed. As a leading headhunter explains, "The trends that led to [former CEOs'] success often change, leaving their like-minded successors ill suited to handle new realities."[1]

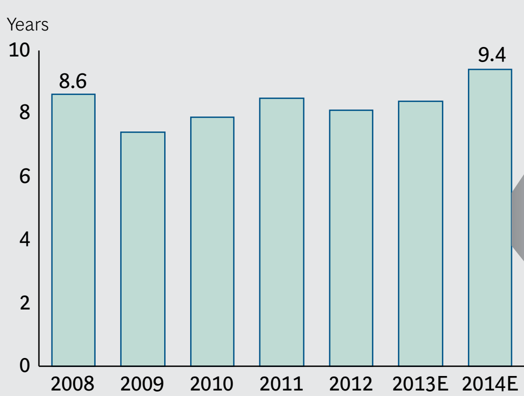
Second, a CEO's planned departure occurs during a time of uncertainty. The company may be facing unfamiliar regulatory pressures, industry consolidation, globalization, complex emerging technologies, changing consumer behavior, or other such disruptive and disorienting forces. The board is looking for a leader who understands these dynamics and has the foresight to enter new markets, introduce new products, acquire new skill sets, and develop a new business model. Frequently, however, a company's most senior leaders will share the same beliefs and worldview as the outgoing CEO, and could prove to be out of their depth in the wave of digital disruption sweeping through their industry. So the most suitable candidates will be found further down in the organization. (For two brief case studies of leapfrog succession, see the sidebar, "Different Challenges, Similar Solutions.")

Common Characteristics of the New CEOs

Many of the traditional CEO requirements, such as intelligence, integrity, and stamina, still matter. But boards are also now seeking other characteristics in their new CEOs, including an easy familiarity with disruptive technologies and digital media; a proven record of innovation; experience in leading high-ranking colleagues; an understanding of diverse markets and cultures, and of demographic shifts; and an adaptive approach to leadership based on such traits as curiosity, social sensitivity, and the courage to act. (For more details

Exhibit 1 | Top-Performing CEOs Maintain Above-Average Tenures

Average tenure of departing S&P 500 CEOs (2008–2014)



CEOs of companies demonstrating strong performance had above-average tenures

Company	Departing CEO's tenure (years)	10-year stock performance compared with S&P 500[1]
2014 average = ~9 years		
CenterPoint Energy	12	+48 percentage points
The Priceline Group	12	+5,400 percentage points
Danaher Corporation	13	+120 percentage points
Humana	14	+505 percentage points
Ross Stores	18	+517 percentage points
Coach	19	+98 percentage points[2]

Sources: The Conference Board; S&P Capital IQ; *Bloomberg Businessweek; Forbes;* BCG analysis.
Note: Data for 2008–2012 average CEO tenures were drawn from The Conference Board, *CEO Succession Practices: 2013 Edition*. Data for 2013–2014 were estimated from press releases and assessments of public data. Founding CEOs were omitted from the assessment.
[1]October 2004 through September 2014.
[2]As of the end of 2013.

DIFFERENT CHALLENGES, SIMILAR SOLUTIONS

Two different companies facing different kinds of corporate setbacks will sometimes adopt similar solutions.

In early 2008, Société Générale, the French bank, was caught up in a scandal. The company lost about $7 billion in fraudulent transactions and rogue trades. Investors called for the resignation of CEO Daniel Bouton. Rather than appoint a member of the old guard who might be associated with the scandal, the board promoted Frédéric Oudéa, 44, a rising star who was relatively unknown and sufficiently distanced from the crisis. In 2009, Oudéa also assumed the role of chairman, and he continues to oversee the revival of Société Générale's fortunes and reputation.

In 2013, Electronic Arts (EA), the global video-game developer, was ailing. Several big-budget console products had flopped. Nimble rivals like Zynga were prospering by building games for the fast-growing online and smartphone markets. EA's market capitalization had slumped to barely one-third of its peak six years earlier. As the outgoing CEO prepared to depart, the odds were on one of two senior L2 front-runners to succeed him. Instead, the board appointed Andrew Wilson, a 39-year-old dark horse and the former head of EA's digital distribution. He was less closely identified with the company's recent mishaps and seemed to represent a fresh and more forward-looking approach. He had experience in Asia and Europe as well as North America, had been successfully involved in market expansion, and showed a commitment to the industry's digital future. It's too soon to say how well he will fill his new role, but since he was appointed, EA has beaten the Nasdaq by 10 percentage points.

on the ideal traits of a modern CEO, see Exhibit 2.)

Distribution Across Sectors

The phenomenon of fast-track CEO succession appears to be most prominent in the retail sector and in the technology, media, and telecommunications sector. Consider the youthful executives who have been appointed CEOs: Google's Larry Page was 38 at the time of his appointment; Microsoft's Satya Nadella, 47; PetSmart's David Lenhardt, 43; and GameStop's J. Paul Raines, 46.

This finding is in keeping with our hypotheses. After all, companies in these sectors are particularly affected by disruptive business models and unfamiliar competitors, so their boards are motivated to appoint CEOs equipped to rewire the company around consumer experience. Institutional investors seem to have taken these bold appointments in stride, but risk-averse companies might still fear the disapproval of investor groups and opt for more traditional and more seasoned successors.

Effectiveness of the New CEOs

It's much too early to judge the success or failure of these leapfrog leaders, who are all relatively new to their jobs. Old reasons rather than new moves by their CEOs can explain both the apparent upswing in the fortunes of Yahoo! and the recent setbacks at General Motors. Still, a few interim impressions are in order.

A leapfrog leader, attuned to the spirit of the times, has a stronger chance to uncover and release a company's latent potential, defying traditions if necessary. He or she will understand cultural norms sufficiently to break some of them without disrupting

Exhibit 2 | Profile of the Modern CEO: A Checklist of Specifications

The new-style outward-looking CEO typically displays many of the following characteristics, and ideally would have all of them.

	He or she...
Intelligence, integrity, and stamina	... has these and other traditional indispensable qualities in abundance
An easy familiarity with disruptive products or services	... has a passion for and understanding of emerging technologies or has a science background
Digital savvy	... is familiar and comfortable with social media and the uses of big data
A track record of innovation	... has skillfully devised and implemented new business models within or outside the company, and has introduced new products
Experience in leading a team of peers or even senior staff	... has previously had a rapid promotion to a leadership position, and has conciliated those who might have felt more entitled to the role
Confidence as a global citizen	... can operate comfortably in developed, developing, and emerging markets, and can maintain credible leadership across diverse cultures
An understanding of demographic shifts	... is alert to any potentially significant changes in the customer base—age, ethnicity, social class, or professional status—and can shape strategies accordingly, especially for new customer-experience channels
Adaptive leadership traits	... has personally embraced and championed disruptions; has demonstrated exceptional curiosity; has self-awareness, social sensitivity, open-mindedness, and the courage to act

Source: BCG analysis.

business continuity. Such leaders will likely face stiff opposition in the form of vested interests, traditional practices, and investor skepticism. But with toughness, persistence, and the backing of the board, the new CEO can make headway in revitalizing the company.

There are at least two risks, however. First, the new CEO may be unprepared for the job. Second, the executives who were passed over may be disappointed and become disaffected. They could quit at an awkward moment or try to undermine the new CEO.

So far as we can tell, those risks have not materialized. The performance of the leapfrog CEOs is at least comparable to that of their more senior counterparts. Their companies have not reported any marked decline in the morale of many L2 senior leaders or an increase in boardroom regret. Most of the CEOs have overcome initial skepticism about their abilities and have established their credibility.

But boards cannot afford to be complacent. They must remain heavily engaged during the grooming and transition of new leaders. The following recommendations will improve the new CEO's odds of success.

Leadership and Stakeholder Experience. A board considering promoting a relatively junior executive to CEO can take several steps to prepare this leader.

- If timing allows, test and prep the candidate by first appointing him or her as president, COO, or CFO.
- Place the candidate on a corporate board so that he or she can gain some experience engaging with directors and can observe how they make decisions.
- Ensure that the candidate has served in a general-manager role of a sizable operation, with P&L responsibilities.
- Have the candidate sponsor a major enterprise initiative to gain experience in mobilizing other leaders across the organization.
- Reassure investors through frequent, well-rehearsed exposures of the candidate or newly installed CEO.

Once the candidate has been appointed as the new CEO, the board can continue to set him or her up for success.

- Keep the roles of chair and CEO separate for the first year so that the new CEO can build traction and gravitas while the chair deals with the investment community.
- Establish a clear CEO-role-handover process and first-year plan.

Talent Management and Retention. The board should be prepared for senior leaders who were passed over to be disappointed. Careful planning will keep the discontent to a minimum.

- Anticipate some resignations and make contingency plans to appoint replacements and reassure stakeholders.
- Rally and encourage any bypassed executives by expanding their responsibilities and ensuring that their new roles offer them an opportunity to further diversify their experience.
- Institute long-term performance-based financial incentives that discourage unproductive behavior.

Succession Planning. Given the uncertainty of the business environment, the board should be revising its approach to succession planning and expanding the field of internal CEO candidates. It should insist on an executive succession process that includes the following actions:

- Reconsidering the required competencies of the full senior team, including the CEO.
- Expanding the process to include L3 executives as potential CEO candidates.
- Identifying promising candidates early in their careers and starting to train them for the CEO role.
- Moving some senior leaders from their positions in order to offer younger candidates opportunities to gain necessary experience.

Improving the Odds of Success

A bold fast-track CEO appointment needs to be made for the right reasons. If a leapfrog appointment is based on a compromise or is the “least worst” option, the new CEO has clearly not been properly prepared for the role and might well flounder when taking office. Compare two imaginary cases that are similar on the surface but very different in their potential for success.

In case A, the leapfrog successor is a very capable highflier, a protégée of the outgoing CEO—and remarkably like him in the way she envisages the company. She remains committed to his strategy and the preservation of the company’s traditions. She is a successful marketing executive who remained in that division for most of her career, forgoing opportunities for operational and general management experience. When she was appointed CEO, after the mysterious resignation of her predecessor, her colleagues and the stock market reacted with bewilderment.

In case B, the leapfrog successor is a very capable highflier, a protégée of the outgoing CEO—but remarkably unlike him in the way she envisages the company. Although she was involved in the past strategy, she has hands-on experience with potentially disruptive technologies and business models. The company has a tradition of stretching its talent through challenging and varying roles. The new CEO benefited directly from this tradition.

Several years earlier, the board in case B had realized the importance of succession planning and had embarked on a rigorous development program for promising candidates, with frequent assessment of their progress. Through this program, the person who would eventually become CEO had acquired greater visibility both internally and externally, notably to investors. She had even briefly taken on the role of COO prior to her appointment as CEO. So her appointment as CEO came as no surprise to her colleagues or to shareholders.

What different prospects the two cases offer—both for the two CEOs and for their respective companies. Early planning by the board made all the difference in case B. The more planning that goes into developing CEO candidates, the more options a board has for choosing a CEO who is suited to its strategic agenda. Prescient boards identify front-runners early on, groom them, arrange coaches and mentors for them, rigorously track their readiness, and set them up for success. A fast-track CEO succession should be the product of a deliberate strategy, not of desperation.

Note

1. "Campbell's Recipe for a CEO Yields Denise Morrison," *Bloomberg Businessweek Magazine,* June 23, 2011, http://www.businessweek.com/stories/2011-06-22/campbells-recipe-for-a-ceo-yields-denise-morrison.

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