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What makes a CEO 'exceptional'?

We assessed the early moves of CEOs with outstanding track records; some valuable lessons for leadership transitions emerged.

by Michael Birshan, Thomas Meakin, and Kurt Strovink

New CEOs face enormous challenges as they start assembling a management team and setting a strategic direction in today's volatile environment. To provide some guidance for transitioning CEOs, we looked at the experiences of *exceptional* CEOs, those defined as the very top performers in our data set of roughly 600 chief executives at S&P 500 companies between 2004 and 2014.

Our focus was on the top 5 percent of the CEOs in our sample as a whole whose companies' returns to shareholders had increased by more than 500 percent over their tenure. We contrasted this group both with our full sample and with a subset of CEOs whose companies achieved top-quintile performance during their tenure as compared with their peers.[1]

The exceptional group includes some leaders who managed remarkable performance in part due to unusual circumstances, for example, by guiding a company through bankruptcy proceedings and then returning it

[1] We ranked all CEOs by annualized total returns to shareholders (TRS), normalized for the performance of their broader industry. Those in the top quintile, the 120 highest-performing CEOs, achieved at least 9 percent TRS above industry cohorts each year they were CEO.

successfully to the public markets. It also includes CEOs who were able to deliver the highest returns through strategic repositioning and operational discipline over many years, within more normal industry and economic conditions. Overall, the exceptional CEOs were neither more nor less likely to be found in particular industries, to lead companies whose size differed from the mix in the broader S&P 500, or to join particularly high- or low-performing companies. Here are three lessons that emerged from close scrutiny of these exceptional leaders.

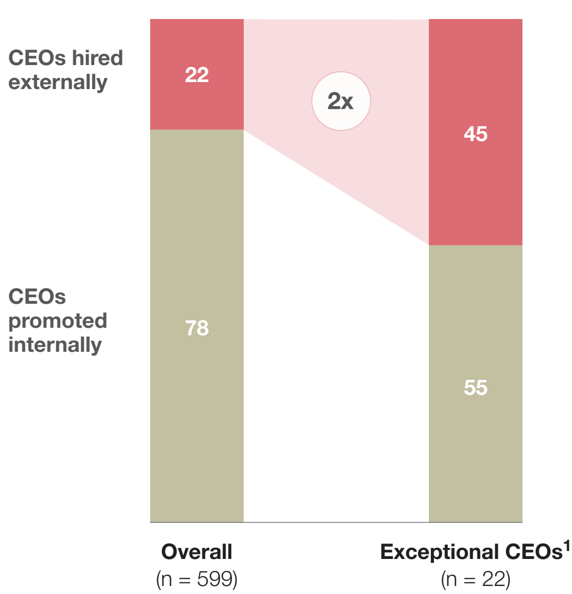
THE OUTSIDER'S EDGE

In our earlier research,[2] we found that on average, CEOs who are hired externally tend to pull more strategic levers than those who come from within and outperform their internal counterparts over tenure. Our research on exceptional CEOs reinforced this finding: these CEOs are twice as likely to have been hired from outside the company as the average CEO in our data set (Exhibit 1), and roughly 1.5 times as likely to have been external hires as the other top-quintile CEOs.

[2] See Michael Birshan, Thomas Meakin, and Kurt Strovink, "How new CEOs can boost their odds of success," *McKinsey Quarterly*, May 2016, McKinsey.com.

Exhibit 1

Exceptional CEOs are twice as likely to have been hired from outside the company.



[1] Defined as CEOs who delivered >500% growth in total returns to shareholders over tenure, normalized for performance of broader industry.

Still, 55 percent of the exceptional CEOs were internal hires. Clearly, insiders can move aggressively and achieve outstanding results. Doing so often means cultivating an outsider's point of view to challenge the company's culture with greater objectivity and overcome the organizational inertia that sometimes limits an insider's span of action.

STRATEGIC ACTIONS

The findings offered additional insights on how CEOs may gain a clear-eyed perspective for action. In our sample as a whole, CEO's joining low-performing companies derived the biggest benefits from conducting a strategic review. Our exceptional CEOs did not join struggling companies in disproportionate numbers, but they were significantly (about 60 percent) more likely to conduct a strategic review in their first two years on the job versus the average CEO in our sample (Exhibit 2).

Exhibit 2

CEOs with exceptional track records are more likely than others to conduct a strategic review early in their tenure.

Informed by this view of the company's past—and potential future—performance, this elite group was bolder than other top-quintile CEOs, far surpassing them in the average number of strategic moves they made in their first year. Changing strategic direction typically requires freeing up resources, often in part by cutting costs in lower-priority parts of the company. While cost-reduction programs are, according to our earlier research, a no-regrets move for all CEOs, the exceptional CEOs were significantly more likely to launch such initiatives than the average CEO, thereby building strategic momentum.

ORGANIZATIONAL BALANCE

In our research on CEOs overall, organization redesign appeared to be a critical part of the typical high-performing CEO's tool kit, and management reshuffles were particularly important for CEOs taking over lower-performing companies. Our sample of exceptional CEOs, though, was less likely than the average CEO to undertake organizational redesign or management-team reshuffles in the first two years in office. This could be a function of the strategic game they were playing: they may have inherited high-performing companies (which can be hurt by reshuffles) or prioritizing, since there are only so many initiatives and changes that organizations and people can absorb in a short space of time. Indeed, since the exceptional group contained an above-average proportion of outsider CEOs launching fundamental strategic rethinks, the data may reflect a sequencing of initiatives, with structural change following strategic shifts.

By definition, not all CEO's will be exceptional. Yet for any CEO starting a transition, there is much to learn from the best. Adopting an outsider's view will yield the unbiased insights needed for breakthrough moves. Likewise, investing in a robust strategic review will provide a surer perspective for setting a strategic direction. A grounding in the organization's context, meanwhile, will help calibrate the speed and scope of change. Those in our sample do much of this at the highest level, setting a benchmark for every CEO aspiring to a successful debut. Q

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