

CEO Hiring and Retention.
A view from Corporate Finance

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Towards a New Model of Boards of Directors

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The Market for CEOs

One of the most important decisions is to hire the right CEO.

How can a board assess and select the best fit?

- The market for CEO is not a classic competitive market. It requires costly search to find that gem.
- **Internal promotions account for 80% of new CEO**, in S&P 500 firms in 2020.
- CEOs moving across firms without connections are rare (3%).

Evidence that hiring is determined by **company-specific human capital and firm characteristics**, and **network connections**.

Could there be some inefficiencies? Benchmark with PE firms 75% of CEOs are external hires.

The Market for CEOs

Tenure: US & EU av of 5 years (2020).

Average age: US & EU 56-58.

Profiles:

- Managerial profiles are shifting to more general & transferable backgrounds.
- Networks matter: 70% for S&P500 CEOs have an MBA. 5x more likely Ivy League.
- Military background (60% in the 80s; 6% - 15% more recent).
- 54% have an engineering degree.

Gender: US & Europe : 90% men - 10% women.

Race: 93% of CEOs in the US are white.

Pay: CEO compensation keeps increasing.

- New CEOs Abnormal pay 0.5 M Internal vs 5.3M Outsiders
- Generalist's premia of 20% relative to specialists.
- Once account for outsiders generalist premia, risk of bad match, frictions (1.7)

Does the Identity of CEOs matter for performance?

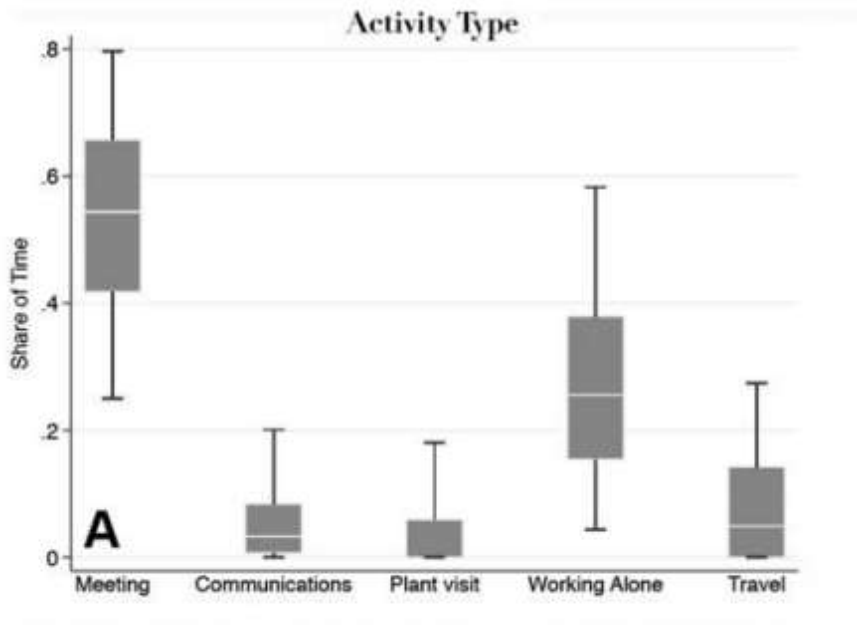
First approach, **What do CEOs do?**

Scale up shadowing approach. Collect detailed activity in diaries: 100+ features. 1,100 CEOs in 6 countries. (Bandiera, Hansen, Prat and Sadun, JPE 2020)

Machine learning - agnostic technique – to infer CEO behavioral "types".

How this heterogeneous behavior types relates to performance?

What do CEOs do?



Share of Activity:

56% spent in meetings.

1/3 One-on one vs 2/3 more
Planned ahead.

Insiders. Outsiders. C-suite.

25% working alone.

Emails, preparing.

10% personal matters.

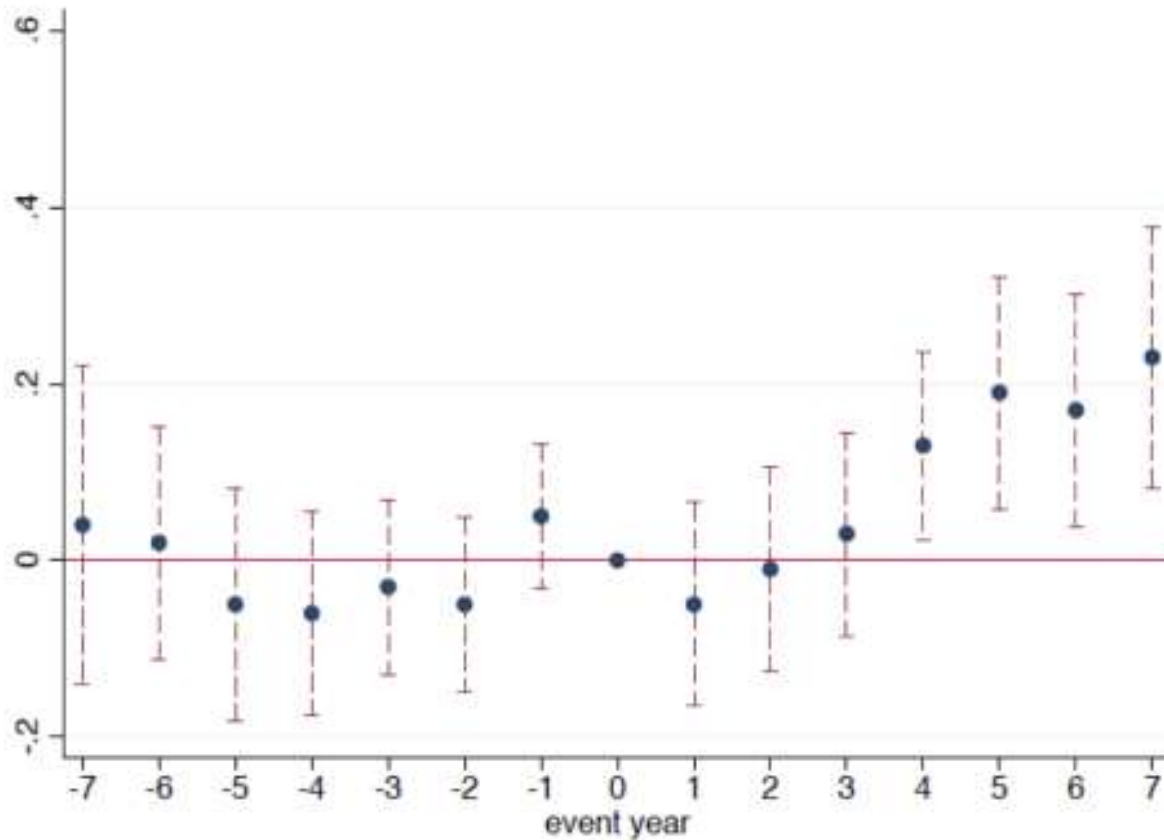
8% travelling.

Behavior Types

Feature	Manager	Feature	Leader
Plant Visits	0.11	Communications	1.9
Just Outsiders	0.5	Outsiders + Insiders	1.9
Production	0.5	C-suite	34
Suppliers	0.3	Multifunction	1.5

- Management-style: setting up systems to ensure that plans are implemented.
- Leadership-style: aims at the creation of organizational alignment, involves significant investments in interpersonal communication.

Does behavior impact performance?



CEOs with stronger Leadership style deliver higher performance 3 years after appointment. Impact: 1/5 as big as capital inputs.

Who should firms hire: leaders or managers?

Horizontal differentiation: demand for both types of CEOs across different firms, but matching is imperfect.

Vertical differentiation: demand only for leaders, but they are scarce.

The effect on performance is due to the MATCH: Some firms would be better with Manager CEOs. Not about the quality of the CEO herself.

The data suggests demand for both types but and **~20% of firms with CEO mis-match.**

Labor market frictions to find the right CEO.

Individual frictions to evolve from managers to leaders.

From behavior to abilities. Do certain abilities perform better?

Second approach: **Are CEOs abilities different from other top executives?**

2,600 executive assessments to study how CEO characteristics may differ from CFO, COO. (Kaplan and Sorensen JF 2021)

20-page reports: history, background, education, internal, outside view...

30+ abilities in 5 areas: Leadership, Personal, Intellectual, Motivational, Interpersonal.

Can consolidate into **4 factors with intuitive interpretations.**

Core abilities

Hires A-players
Develops people
Removes underperformers

Respect

Efficiency

Network

Flexible

Integrity

Organization

Calm

Aggressive

Fast

Strategic vision

Creative

Attention to detail

Enthusiasm

Persistence

Proactive

Work ethic

High standards

Listening skill

Open to criticism

Oral communication

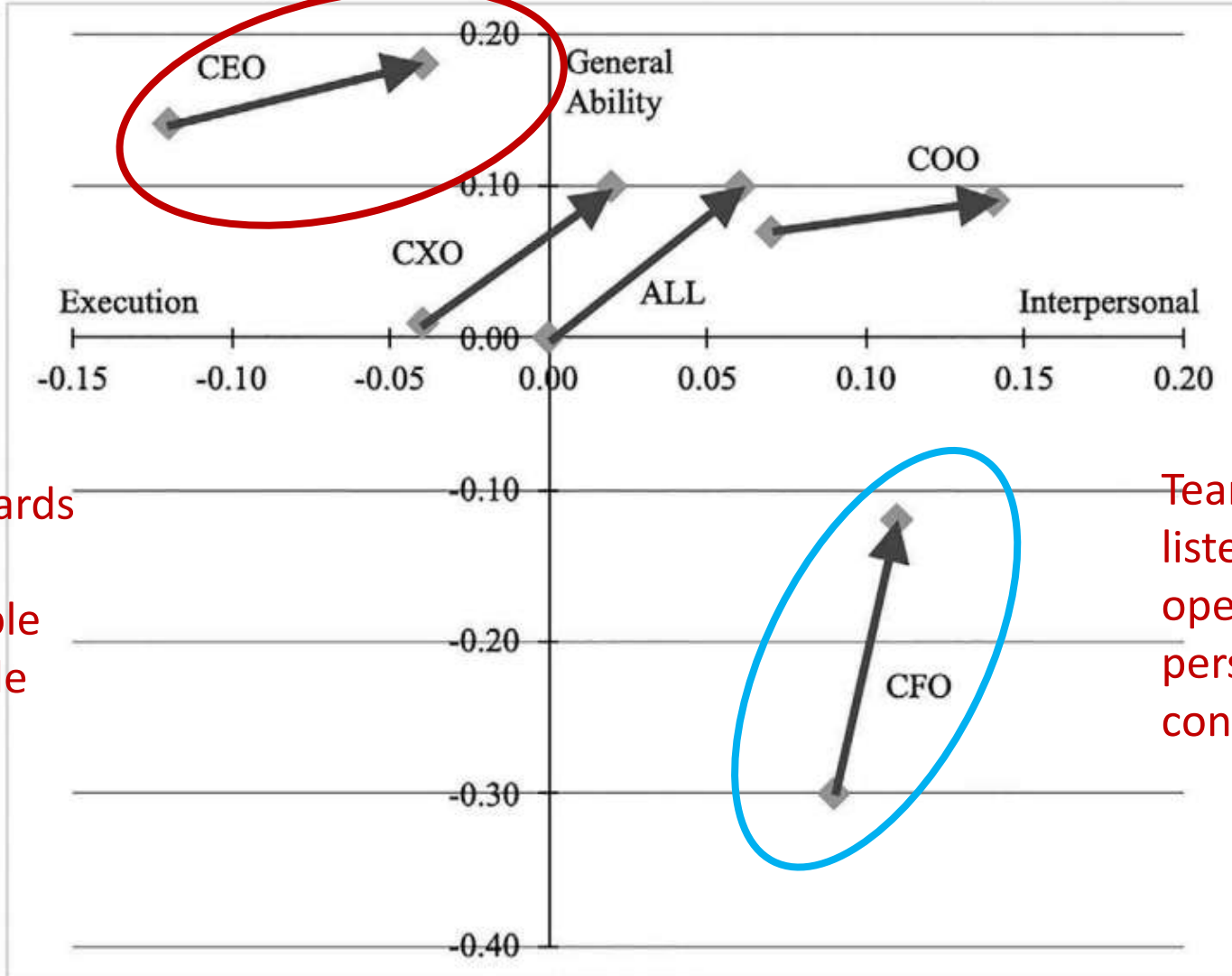
Teamwork

Persuasion

Holds people accountable

4 Factors: General Ability & Execution

Panel A: Factor 1 (General Ability) and Factor 2 (Execution vs. Interpersonal)

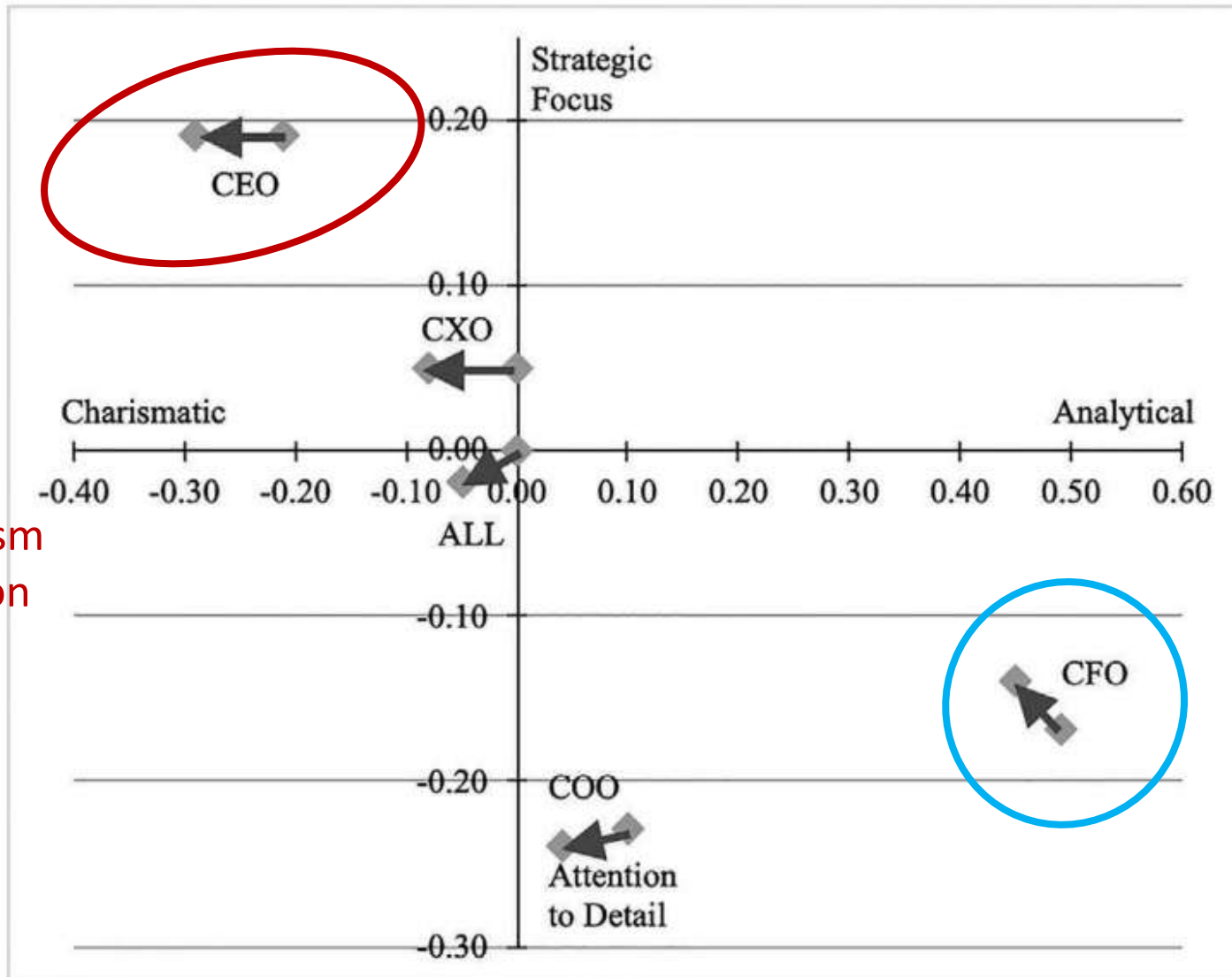


fast
high standards
proactive
holds people
accountable

Teamwork
listening skills
open criticism
persuasion
consensus

4 Factors: Creative, Strategic & Charismatic

Panel B: Factor 3 (Charisma vs. Analytic) and Factor 4 (Strategic vs. Managerial)



Enthusiasm
Persuasion
Proactive
Fast

Who gets hired?

CEO candidates have more general ability, greater execution, great charisma, strategic perspective.

These factors predict future CEOs.

Guidance for becoming a CEO. You can modulate your abilities.

But, who gets hired?

General ability + interpersonal skills are more likely to be hired.
However interpersonal skills are unrelated to performance.

Boards overweight interpersonal skills at the expense of execution.

Setting the right Pay to hire CEOs

What are the factors behind pay contracts? Radical rise of Ceo pay.

- **Technological change** associated with pay increases and gap.
 - Willing to pay for the ability to recognize and invest in new technology. (Frydman, Papanikolau 2019).
 - Toyota choosing to develop Prius just as electric batteries became efficient.
- Interaction btw boards (set pay contracts) and shareholders (approve). **How much voice should you give your shareholders?**
 - Say-on-Pay leads to + 5% market value and long-term profits.
 - Limited affects on level of pay. Serves as a disciplining device. (Cuñat, Giné, Guadalupe 2016)
- Structure of Pay. How are CEOs **incentives related to performance?**
 - less performance sensitive incentives depending on the competitive context. (Anton, Ederer, Giné, Schmalz 2023)

In Summ

Two main behavioral styles. Managers or Leaders.

Match is key. **Most value is in the Match** not the candidate alone.

CEOs have **distinct abilities** from other top Executives.

4 factors, that can be developed.

Be aware of **hiring biases**: overweight interpersonal at the expense of execution.

Pay: firms will pay for **ability to invest in new tech** (AI & decarbonization)

Boards need to interact more w/investors when setting pay.

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Thank you!

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