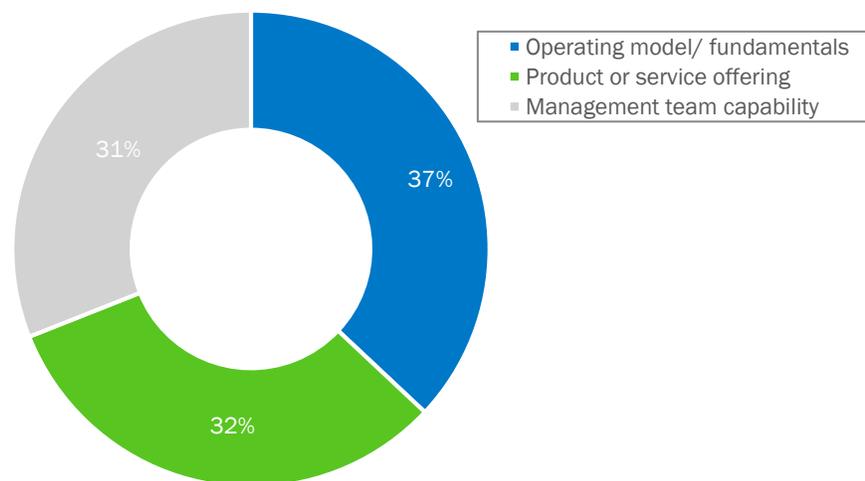


## Valitas Insights: Management Diligence – The Power of a Leadership Blueprint

There are a number of factors that PE investors consider when analyzing a potential acquisition target. However, according to a recent report, [A View from Both Sides – How PE firms and sellers can form wise partnerships](#), firms perform rigorous due diligence on two of the most significant factors, operations and product offering, but treat the third factor, management team capability, more casually. We spoke with Richard Davis, Ph.D., CEO of Kilberry, a leadership advisory firm, and one of the authors of the report, who provided insights into why this occurs, and how rigorous management due diligence can drive future value creation.

**Figure 1: What is the contribution of each in the success of a private equity deal**



Dr. Davis suggests that PE investors should set aside fixed notions of what constitutes a successful leader and management team. “Different attributes are better suited for different goals,” he says. “For example, a value creation strategy based on cost-cutting versus one driven by global expansion will require different leadership attributes.” To most effectively assess management strength for a specific target, Dr. Davis recommends taking the following steps to develop a leadership blueprint:

- (1) Develop a clear understanding of the investment thesis for a specific deal.
- (2) Determine what the target management team will need to do to operationalize the investment thesis.
- (3) Identify the leadership attributes necessary to achieve this.

Management due diligence often falls later in the due diligence process, at a stage when a PE firm is already attached to a specific deal. For that reason, Dr. Davis emphasizes the benefits of using an external assessment of management capabilities, rather than the more casual and commonly utilized personal interview and/or spending time with target management.



Dr. Davis's view is supported by the Nobel-winning work of Israeli psychologists, Daniel Kahneman and Amos Tversky, who believed that "crucial decisions are made, today as thousands of years ago, in terms of...intuitive guesses and preferences" and decision makers are not aware of their own biases. External assessors provide a scientific and unbiased view when assessing management characteristics relative to a proposed investment thesis. In addition, removing the emotional attachment to a deal, and the influence of sunk time and effort allows for a more accurate conclusion. External specialists are utilized when performing other areas of due diligence – for example, the accounting firm that conducts a quality of earnings analysis to validate a target's financial performance. Bringing in an external assessor to evaluate management team bench strength provides a similar benefit.

In addition to assessing management suitability, a leadership blueprint allows PE investors to identify the value creation inherent in developing a management team's potential. "Rather than perfect [fit], we look for value creation opportunities amongst the current management team, someone that can grow," says Dr. Davis. "The ability to diagnose issues and prescribe remedies early in the process increases the probability of a successful investment without replacing the leadership team."

There is certainly no single cookie-cutter approach to analyzing a management team. Rather, leveraging the science of human characteristic analysis against a leadership framework provides value-added diligence to a process. As Dr. Davis emphasizes, "It is not just judging and evaluating [a management team], but applying rigour in evaluating someone's ability to do what you want to be done. Not just judging someone's character, but using the information to take action."

*Dr. Richard Davis is President/CEO of Kilberry, a firm of management psychologists that provides assessment and development services to investors, CEO's, and key corporate leaders. He has extensive experience advising CEO's, including those leading Fortune 100 companies or otherwise in the public eye. Richard is licensed as an Industrial/Organizational Psychologist by the College of Psychologists of Ontario. He received his M.A. at Boston University, and his Ph.D. at York University.*

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