The CFO's Last Mile: Building Towards Success as CEO

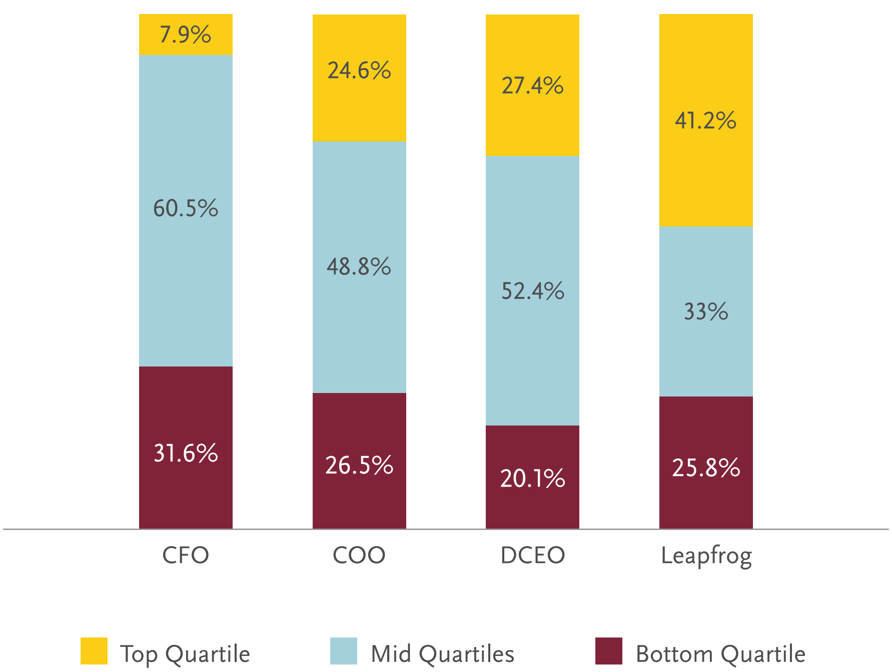
CFOs' unique vantage point into the business often positions them as viable CEO successors. And, in fact, roughly one in 10 new S&P 500 CEOs come from the chief financial officer role. Yet, despite the obvious advantages of their background, promoted CFOs face the toughest odds to outperform as CEO. Our study suggests that CFOs need to adopt a significant shift in focus as they get promoted to CEO: matching financial prudence with a growth orientation for the business.

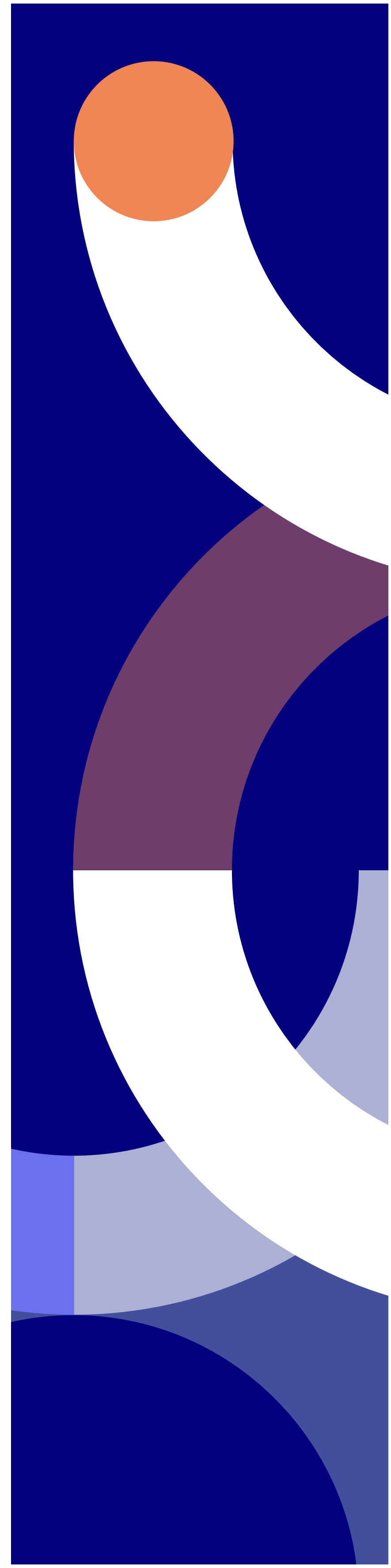
As part of Spencer Stuart's CEO Life Cycle research, we studied more than 1,300 CEO transitions to predict the probability of success in the top job based on a CEO's last role. Our analysis finds that only 8 percent of CFOs-turned-CEOs steered their companies to the top-quartile of performance (Exhibit 1). By contrast, "leapfrog" CEOs — those promoted from two or more levels down — and divisional CEOs had far higher odds of outperformance.

What explains the difference in performance? It turns out that promoted CFOs outperform their peers on the dimension of the business they are already most familiar with. On average, they achieve higher levels of profitability during their early CEO years yet lag their peers in top-line growth. To bend the odds of CEO success in their favor, promoted CFOs need to equally lean into the less familiar: driving growth.

We dug deeper into the data and spoke with successful CEOs who rose from the finance path to understand how CFOs aspiring to CEO can leverage the strengths of their experience and beat the odds to excel as CEO.

EXHIBIT 1: REPRESENTATION IN TOP AND BOTTOM PERFORMACE QUARTILES BY BACKGROUND





The benefits and limits of financial conservatism

CFOs would seem to have a natural advantage when becoming CEO. They typically are the right hand of the CEO and close partner in defining and executing the strategic objectives of the business. They bring a company-wide perspective and deep knowledge of the financial levers for value creation. They have an empirical mindset and hard data approach that can clarify issues and illuminate risks. Finally, boards and investors have seen them up close and feel comfortable with them.

Over many years in the finance function CFOs cultivate financial conservatism, an important asset in their oversight of the company. Embedded in the structure and logic of the balance sheet, they instill financial discipline, prudent stewardship and a clear-eyed view about potential risk. Often outside of the CFO's purview are more risk-prone responsibilities, such as innovation, revenue and growth.

We see this in our data. CEOs promoted from the CFO role on average are slower to drive top-line growth than CEOs from other backgrounds, especially in the first years of their tenure (see exhibit 2 below). As they mature in the role, they progressively narrow the gap. By contrast, we see the opposite effect on profitability (see exhibit 3 below). Former CFOs produce stronger operating margins than peers during their first years of tenure.

EXHIBIT 2: CEO PERFORMANCE — AVERAGE REVENUE GROWTH (YEAR OVER YEAR, WINSORIZED, S&P 500 CEOs)

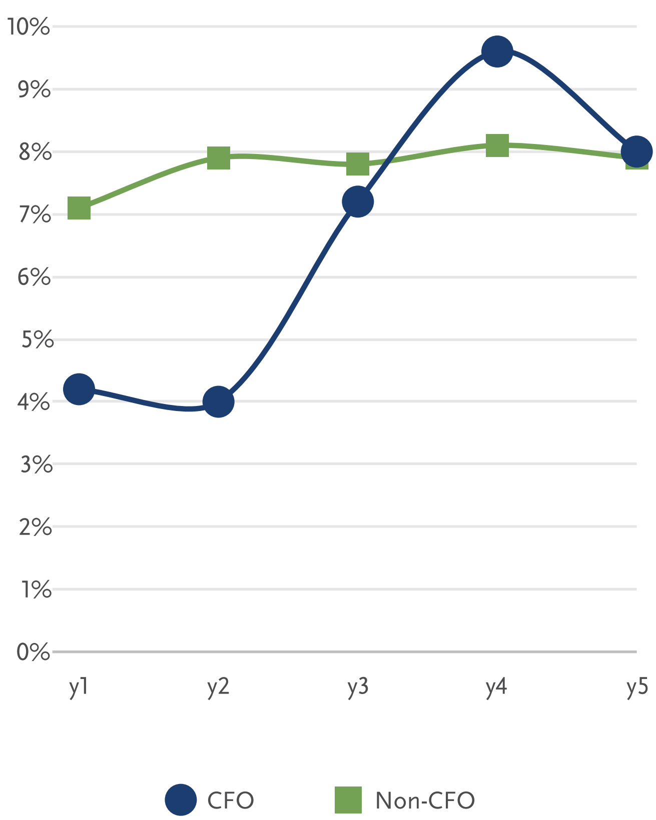
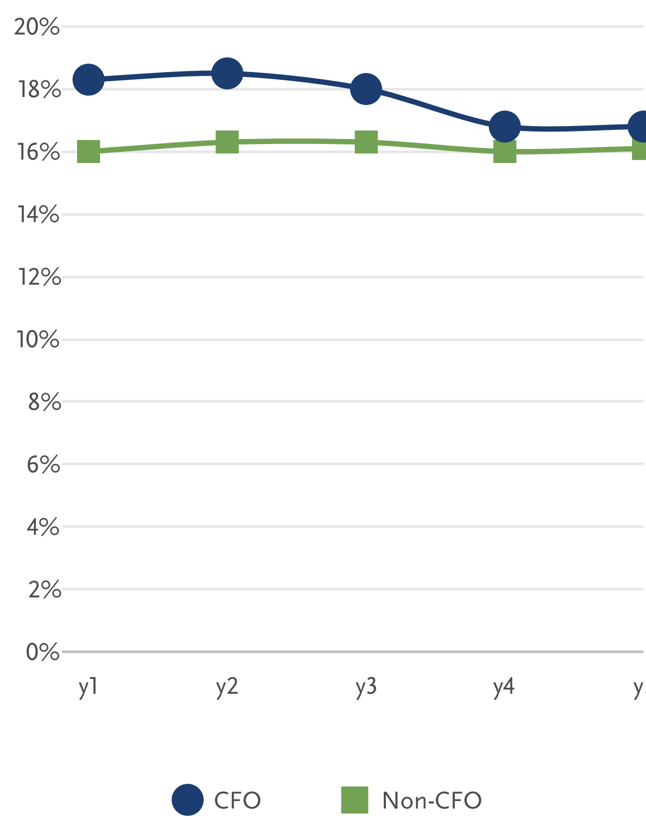
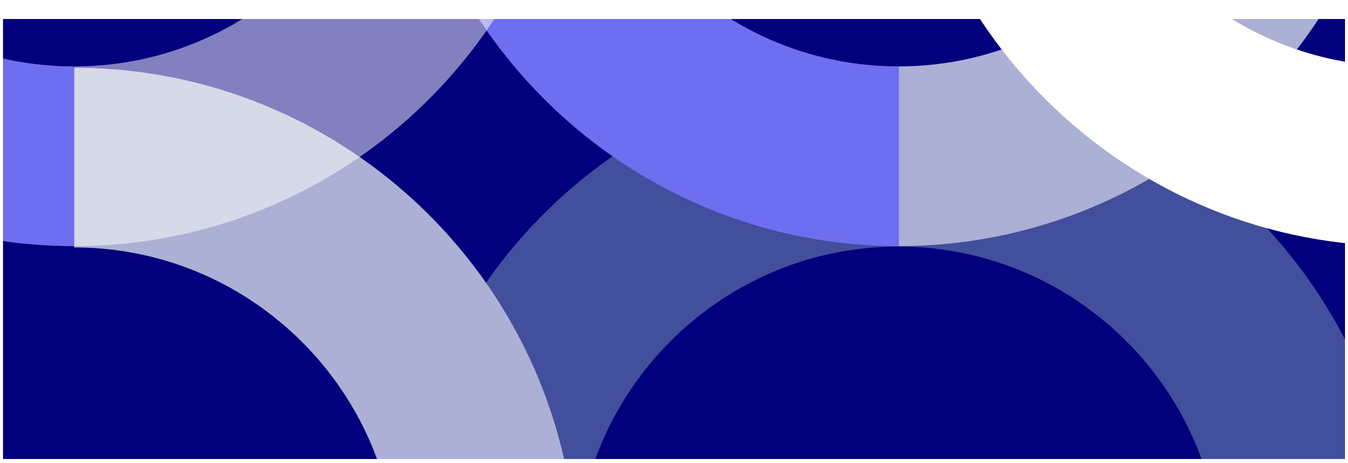


EXHIBIT 3: CEO PERFORMANCE — AVERAGE EARNINGS BEFORE INTEREST AND TAXES (EBIT MARGIN, WINSORIZED, S&P 500 CEOs)





Slower top-line growth comes at a cost. We modeled revenue growth for promoted CFOs and their peers over the first five years of a CEO's tenure for a company with revenue of $11 billion, the median revenue in our sample. Companies led by former CFOs are at risk to generate nearly $1 billion less in revenue due to lower growth during the early years.[1] During the same period CFO promotes generate a total of $374 million in additional operating income compared to their peers. While such profitability growth is impressive, it appears that investors value the focus on generating future sales over the ability to find synergies in the short term.

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As one former CFO-turned-successful CEO observed, "Where CFOs are most comfortable is in the cost end of the business, not driving the top line. They may not be close enough to sales and marketing as they should be. A lot of times people want to save their way to prosperity by focusing on costs and efficiency instead of driving the top line."

A CFO's attention to the bottom line provides a counterbalance to the optimism and growth focus of the CEO. Such a partnership creates healthy tension, with the CFO freeing up the CEO to realize their vision by ensuring that plans are grounded in reality and risks are understood. Once CEO, too much pragmatism and financial conservatism become a liability. To succeed as CEO, former CFOs must tamp down instincts honed during years in the finance function and adopt a new mindset — one focused on innovation, growth and possibilities. They must think and act in completely new ways. "What got you here won't get you there" has never rung truer.

How successful CFOs accelerated into the role

An executive's "modus operandi is a proxy of what they have been exposed to."[2] Becoming a successful CEO requires a significant shift in said modus operandi. The good news is CFOs can begin putting in place the building blocks for this shift well before becoming CEO. Here's what finance leaders can do.

1 We examined several possible reasons for these differences, none satisfactorily explaining the difference. On average, CFO promotes led slightly smaller companies than peers, and, while they were represented in all major industry sectors, they were more likely to be found in financial services, industrials and real estate. We also explored whether promoted CFOs were more likely to be selected for challenged companies, but our data did not reveal meaningful differences in the shareholder returns over the previous three years between the companies that chose a CFO as their next CEO and those who did not.

2 James L. March (1991) "Exploration and Exploitation in Organizational Learning,"

Build commercial muscle

CFOs who are successful as CEOs shift their focus to growth. They reorient their thinking away from the idea that "capital is scarce" to the idea that "opportunities are scarce." In addition to preserving cash flow and finding synergies, they chase the biggest opportunity and choose which alternatives to forgo to maximize stakeholder returns. Backing innovation efforts, market expansions or acquisitions that increase return on capital may be new territory for former CFOs, but they are critical drivers for the sustained success of the business.

Many CFOs who outperformed as CEOs gained P&L responsibility at some point during their careers. Others found alternative ways to develop commercial prowess. One promoted CFO says he adopted the commercial mindsets and behaviors he observed from watching customer-facing leaders he worked with during his career. "Someone coming up through marketing or another more creative route is much more focused on the consumer and the pain point that needs to be solved," he said. Another successful CFO-turned-CEO credits his experience working in multiple industries. "Making those moves, you are forced to learn the front end far earlier and in greater detail than you normally would. Otherwise, you can't understand the business." Spending as much time as possible with customers is another way to hone a commercial perspective. Getting out into the stores and partnering with other business leaders to identify and capitalize on commercial opportunities will help many CFOs develop a stronger growth focus.

Tap into vision in decision-making and communication

Great CEOs have vision. "They are storytellers," one director explains. "You have to have a vision and be able to bring people along. Without the ability to breathe excitement into the organization, it's very hard to be successful."

There are many ways finance leaders can hone their ability to speak with passion about the vision for the business. One former CFO and successful CEO, for example, expanded her purview, stretching herself to become a leader and strategic thinker in technology. Sponsoring innovation, overseeing investments, helping to define success, and understanding the benefits of technology only enhanced her CEO readiness.

Successful CEOs also are effective at communicating their vision for the business, often engaging the organization by tying objectives to a larger purpose. Finance leaders can enhance their ability to communicate with vision by shifting their perspective beyond shareholders to include stakeholders and providing a big-picture perspective before diving into the details. As one promoted CFO explains, "When you're CFO, you spend all your time convincing Wall Street and everybody around you that you're the smartest person in the room. When you're CEO, you've already been appointed smartest one in the room. You don't have to convince anybody anymore. You need to convince them that you have a vision of what's going on in the future."

Know when to take off your "finance leader" hat to build connections with your peers

Most CFOs feel tremendous pressure to serve as the financial conscience of the business. But when CFOs always play that role, it can keep them from interacting with peers in ways that help them learn and build influence. Taking off the finance enforcer hat requires vulnerability. One former CFO-turned-CEO advises CFOs to ask for help when they need it. "At every place I've been, there were a couple of people who really made me better," he says. "You have to be able to admit that they know more than you do. You have to be willing to say, 'I've got a thimble full of knowledge about a particular area. I need you to help me.'" By knowing when to serve as financial conscience and when to focus on helping make others successful, CFOs become more adept at holding multiple perspectives at once.

Have the courage to develop successors

Since 94 percent of the CFOs appointed CEO were promoted from the inside, it's paramount to invest in developing a successor. Developing a strong team and a trusted successor frees CFOs to elevate and expand their focus with the comfort that the finances are well-managed. In turn, that confidence and expanded scope help the board and others see the CFO in a new light. CFOs who became successful CEOs are strong people developers, regularly coaching their teams and providing opportunities for team members to learn and develop. When finance leaders invest in the professional growth of their people, they also tend to develop a delegation mindset that will serve them well as CEO. As one CEO advises, "It's very easy to spend time in the CFO lane as a new CEO, as opposed to appointing someone really competent who can do what you used to do, so that as CEO you can put your energy disproportionately other places."

Find a coach

A coach can help leaders develop new capabilities and enhance their overall effectiveness. Coaches — whether an external executive coach, the current CEO, a board member or other — can help identify specific objectives and actions to help leaders achieve their goals, aligning developmental needs with the ability to create value for the organization. One CEO relied on a coach to work on toning down his natural inclination to lead with facts and figures. Over a period of time, they worked on balancing the rational with the emotional to capture the hearts and minds of the audience. Focusing more on the "why" in communications helped the CEO to improve the level of engagement in the organization. Coaches help leaders define what success looks like, uncover blindspots, illuminate how certain actions or communications are perceived by others, support relationship-building and hold leaders accountable for making progress. Change takes time, so working with a coach should be viewed as practice, with the coach providing guidance and reinforcing behaviors over time.

Conclusion

Data is not destiny. By understanding the mindsets, capabilities and priorities of the most successful CEOs, CFOs can begin preparing themselves for long-term success. Pushing themselves to broaden their knowledge of the business, increase their growth orientation and develop their people leadership skills will improve their performance as CFO and increase the odds that they will emerge as top-performing CEO.

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