

The Market for CEOs: Evidence From Private Equity

Based on BFI Working Paper 2023-13, “[The Market for CEOs: Evidence From Private Equity](#),” by Paul A. Gompers, Harvard University; Steven N. Kaplan, Chicago Booth; and Vladimir Mukharlyamov, Georgetown University

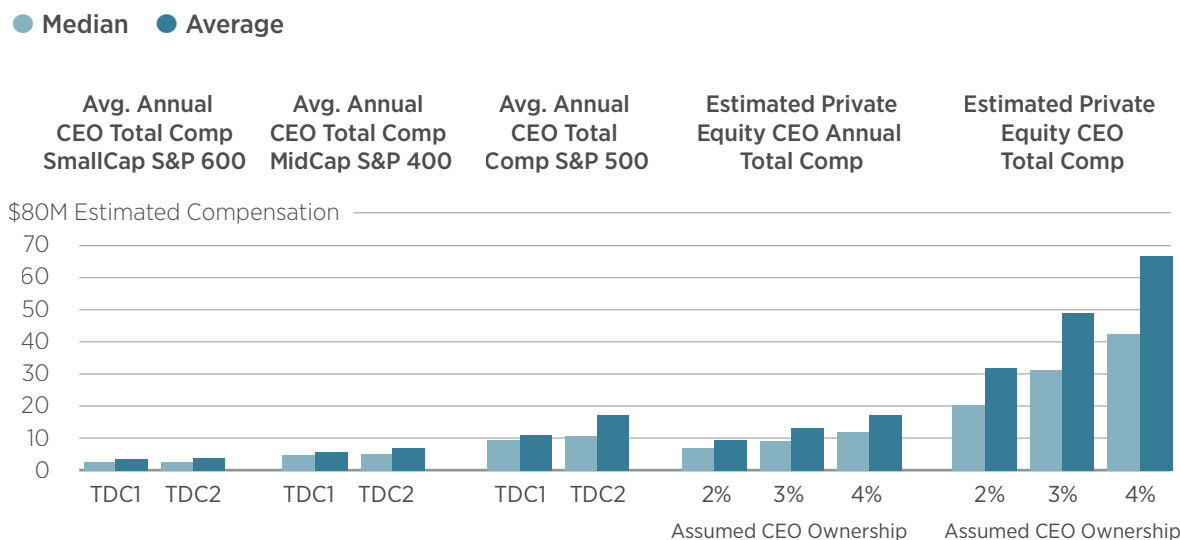
While most new CEOs of public companies are internal promotions, this new work finds that more than 75% of the new CEOs are external hires, with 67% being complete outsiders.

While research has long examined the market for CEOs and executive mobility in public companies, the market for CEOs in private equity funded companies is less understood. This paper addresses that gap by studying the market for CEOs among larger US companies (enterprise value greater than \$1 billion) purchased by private equity firms between 2010 and 2016. These are primarily leveraged buyout transactions, meaning that a significant

amount of borrowed money was used in the acquisition (the authors use private equity and buyout interchangeably).

This research is more than an academic exercise, as the private equity industry has grown increasingly important in recent decades. From 2017 to 2021, for example, over 30,000 private equity deals (buyouts and add-on acquisitions) were completed with a total value exceeding \$4

Figure 1 • CEO Compensation Estimates



Note: This figure displays cash compensation and incentive assumptions together with the performance results to estimate total equity compensation and annual total compensation under different fully diluted equity assumptions. TDC1 relates to expected compensation while TDC2 is realized compensation.

trillion, representing a market capitalization of more than 10% of the S&P 500. Further, these buyouts have greatly influenced the market for CEOs, including how they are selected and compensated. In addition, these buyouts have performed well: The average private equity fund formed between 2010 and 2016 outperformed the S&P 500 by a cumulative 22% and an annualized 5%.

The authors find the following:

- In large leveraged buyouts between 2010 and 2016, 71% of those companies hire new CEOs, and of those, more than 75% are external hires with 67% being complete outsiders. In contrast, among public companies, 72% of new CEOs are internal promotions.
- The outside CEOs hired during buyouts are, in order, raided executives who were previously not in a CEO position (representing more than half of the CEOs), unattached managers, followed by raided CEOs.
- Of the external hires, 67% were recently at a public company and 32% at an S&P 500 company, with nearly 50% having some previous experience at an S&P 500 company.
- Regarding compensation, the authors find that buyout CEOs earn appreciably more than CEOs of similarly sized public companies and only slightly less than CEOs of much larger S&P 500 companies, suggesting that externally hired CEOs perform well.

These findings lead the authors to consider the following implications for the market for CEOs and top executives:

- That top executives move from public companies to private equity funded companies at competitive compensation levels suggests that the broader market for CEOs is active and that, at least for private equity funded portfolio companies, firm-specific human capital is relatively unimportant.
- That the externally hired CEOs have previous experience in the same or related industries strongly suggests that industry-specific skills, rather than firm-specific skills, are important.
- The results for, and inferences from, publicly owned companies do not generalize to all companies.

Finally, the authors are left with a puzzle: Why are results so different for private equity funded companies and those companies in the S&P 500? Please see the working paper for a more detailed discussion, but possible answers suggest that the typical S&P 500 company has many talented executives from which to choose; that appointing outsider CEOs is value maximizing for private equity funded companies; and that, other things equal, the costs of getting a CEO candidate to move to a new firm, including moving costs and risk aversion costs, may bias firms toward hiring internal candidates.

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