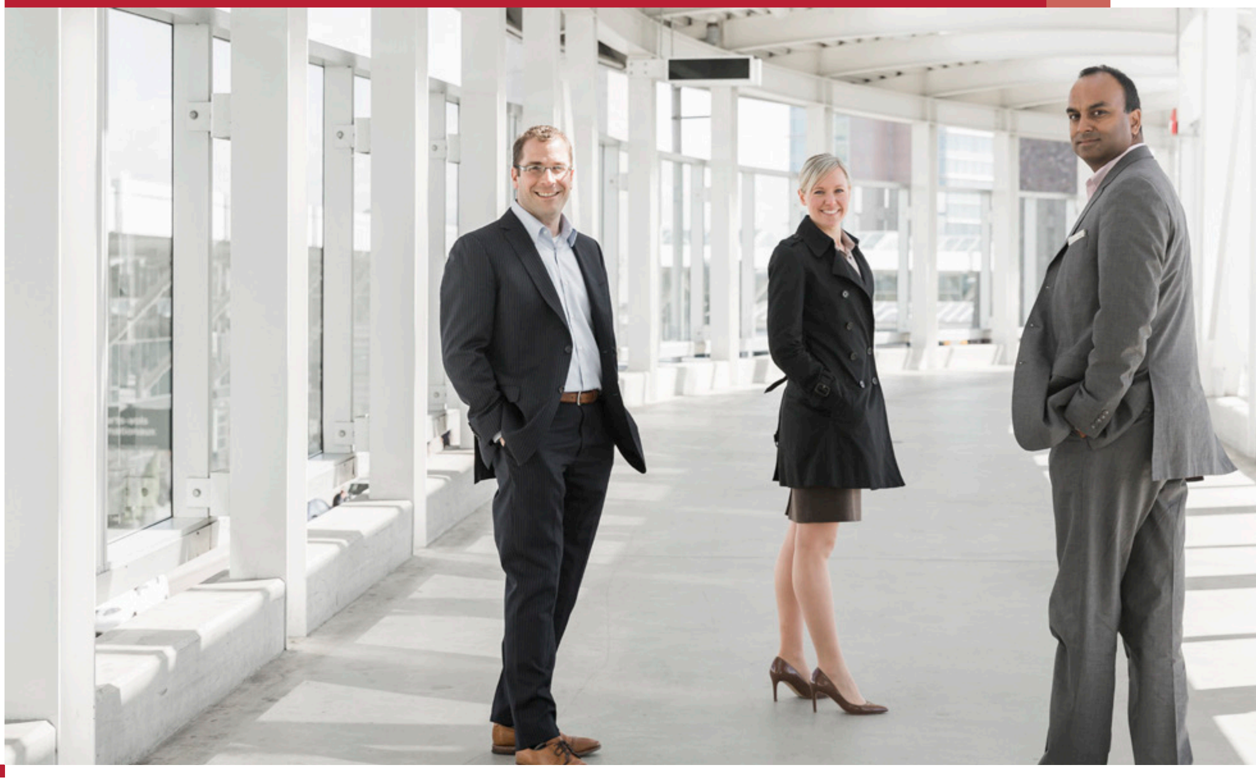
Communications Review / March 2017
Insights for telecom, cable, satellite, and Internet executives

CEO succession in telcos: high turnover and dismissal rates reflect the industry's hunger for consumer-savvy leadership from outside



Communications operators across the world are facing a growing competitive threat from over-the-top (OTT) entrants – just one of many challenges to their future profitability and even viability. In response, telcos are focusing on reducing complexity and using simplification to manage costs down, while at the same time striving to reinvent their businesses with the customer – and digital technologies – at the core. But how is this transformation affecting telcos' choice of leadership? Exclusive research conducted by Strategy&, PwC's strategy consulting business, confirms that communications operators change – and fire – their CEOs more often than companies in other industries. They are also more likely to seek and recruit their new CEOs from outside their own organisations. In this article, we examine what these previously unidentified patterns mean for operators, their boards, and their leadership succession plans.

Today's global telecoms industry faces myriad challenges that are all too familiar to executives across the sector. To name but a few, they include saturated markets, rapid rises in network traffic, creeping commoditisation, intensifying competition from aggressive over-the-top (OTT) entrants, increasingly demanding customers, and an inconsistent and fragmented regulatory environment.

For many telco operators across the world, the combined result of these issues has been stagnating growth and profitability, and uncertainty over where to find new paths to growth. While some are making progress, others appear to be floundering. What's clear is that the choices and actions taken in the next few years will probably determine the fate of the industry.

The industry imperative: time to refocus on customers

As operators strive to rise to the challenges confronting them, they have struggled to monetise the flood of data running over their networks, constraining their ability to invest in further network upgrades. At the same time, their services have become increasingly commoditised, pushing them towards the status of a dumb pipe, as the OTT players have continued to grow their dominance and capture the lion's share of value from telcos' network investments.

How has this situation come about? To date, many carriers have tried to be all things to many people – and have often failed to excel at any of them. To fight back effectively, they must first take a hard look at their own positions within their markets, and then make the tough strategic choices needed to maximise the value of their own specific situations.

These choices will be around complexity reduction, simplification, digitisation and new go-to-market models – all targeted at achieving greater customer-centricity and much closer customer intimacy. This will mean operators moving away from their traditional engineering-led focus on building and operating networks, and towards a culture and mind-set based primarily on understanding and delivering what their customers want.

Gauging the impacts on CEO succession

As the competitive threat for the OTT players grows, operators across the world have no time to lose in executing this profound change in their purpose, structure and culture. It's a shift that brings major implication across the business – from strategy to operations to talent and more. Rarely has any major global industry faced a need for such a radical, sweeping and business-critical transformation at such high pace.

Nowhere is the resulting pressure greater than at the top of the organisation, with the CEO – the hot-seat where the buck ultimately stops. So, against this background, we decided to take a close look at how the patterns of CEO succession and departure in the communications industry compare with those in other sectors.

To investigate the telecoms industry's treatment of its CEOs, we drew on a global research study that PwC's strategy consulting arm, Strategy&, has conducted every year since 2000: *The Strategy& annual CEO success study*. The background, goals and methodology of this study are summarised in the accompanying information panel.

We've taken the cross-industry findings from the research and conducted a deep-dive into the findings from the telecoms industry. We've then compared this drill-down with the results for other sectors. As we'll describe, the findings from this comparison are both surprising and provocative, casting a fascinating new light on how the industry is responding to its challenges.

The Strategy& annual CEO success study

For sixteen years, Strategy&'s annual research has been assessing what companies look for when it's time to choose a new leader. The study analyses CEO successions at the world's 2,500 largest public companies, collecting over 50 data points about each CEO. The results are released annually through a global launch every April with a feature article in Strategy+Business magazine, generating intense client interest and high-profile media coverage.

The study has examined more than 240 successions within the telco industry over the past twelve years. These have now been analysed in detail in multiple dimensions, and the results compared with those from other sectors.

An industry that stands apart on multiple dimensions

So, what did our analysis tell us? Essentially that, on virtually every metric we looked at – including CEO turnover rate, dismissal rate, and tendency to recruit new CEOs from outside the organisation – telecoms operators score higher than virtually every other sector. And it's self-evident that this divergence from the norm reflects the unique and growing pressures that the industry faces.

Starting with the frequency with which companies change their CEO, we found telecom services providers have exhibited the highest CEO turnover rate of any industry over the past five years, with an average of one in four telcos appointing a new CEO every year (see Figure 1). It's interesting that the second highest rate is in the energy sector, which has also seen profound disruption in recent years, albeit driven by very different factors. It's equally intriguing that the IT industry – a sector with which telecoms is often bracketed – has the lowest turnover rate.

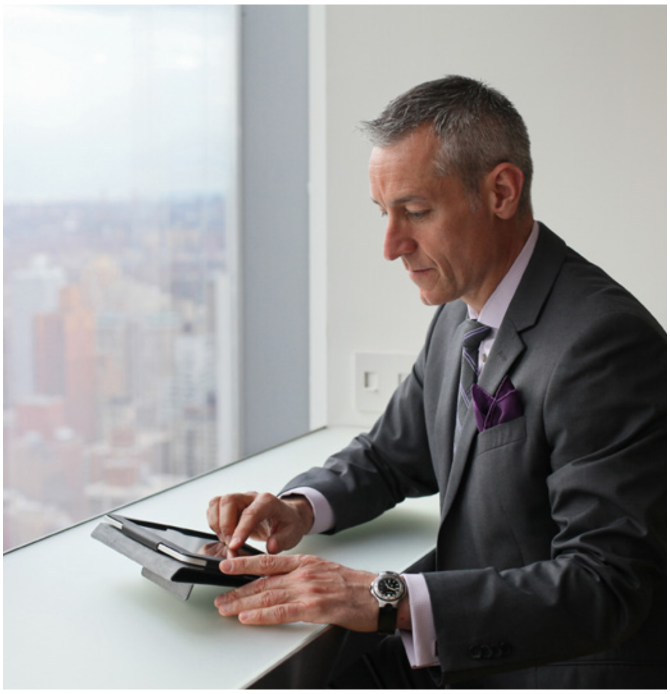
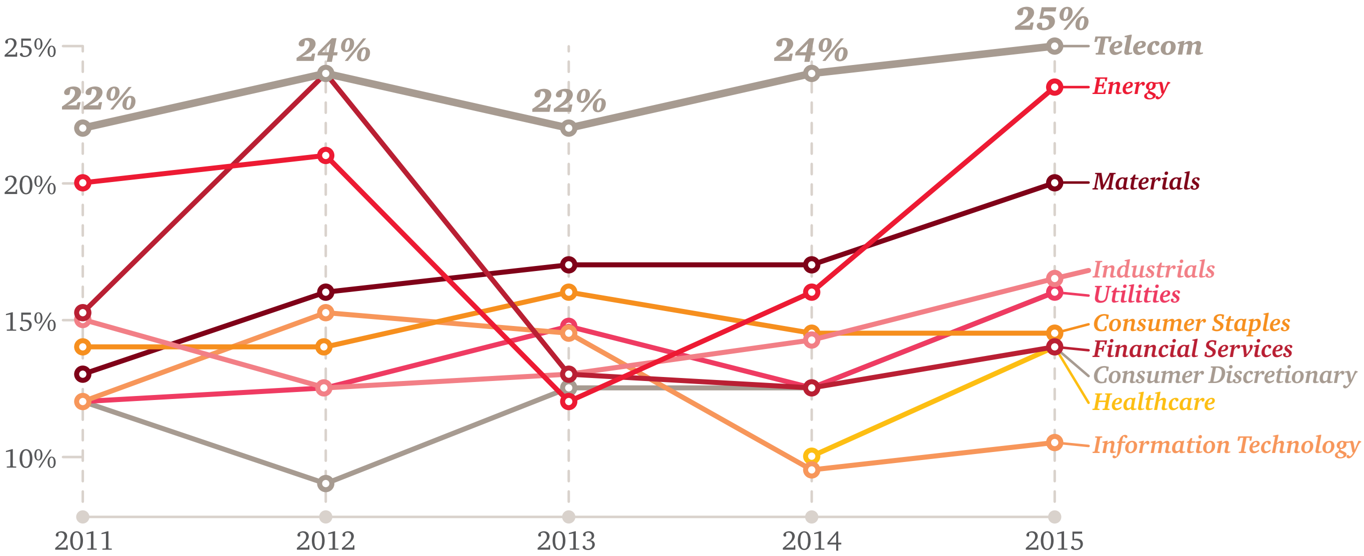


Figure 1: CEO turnover rate by industry

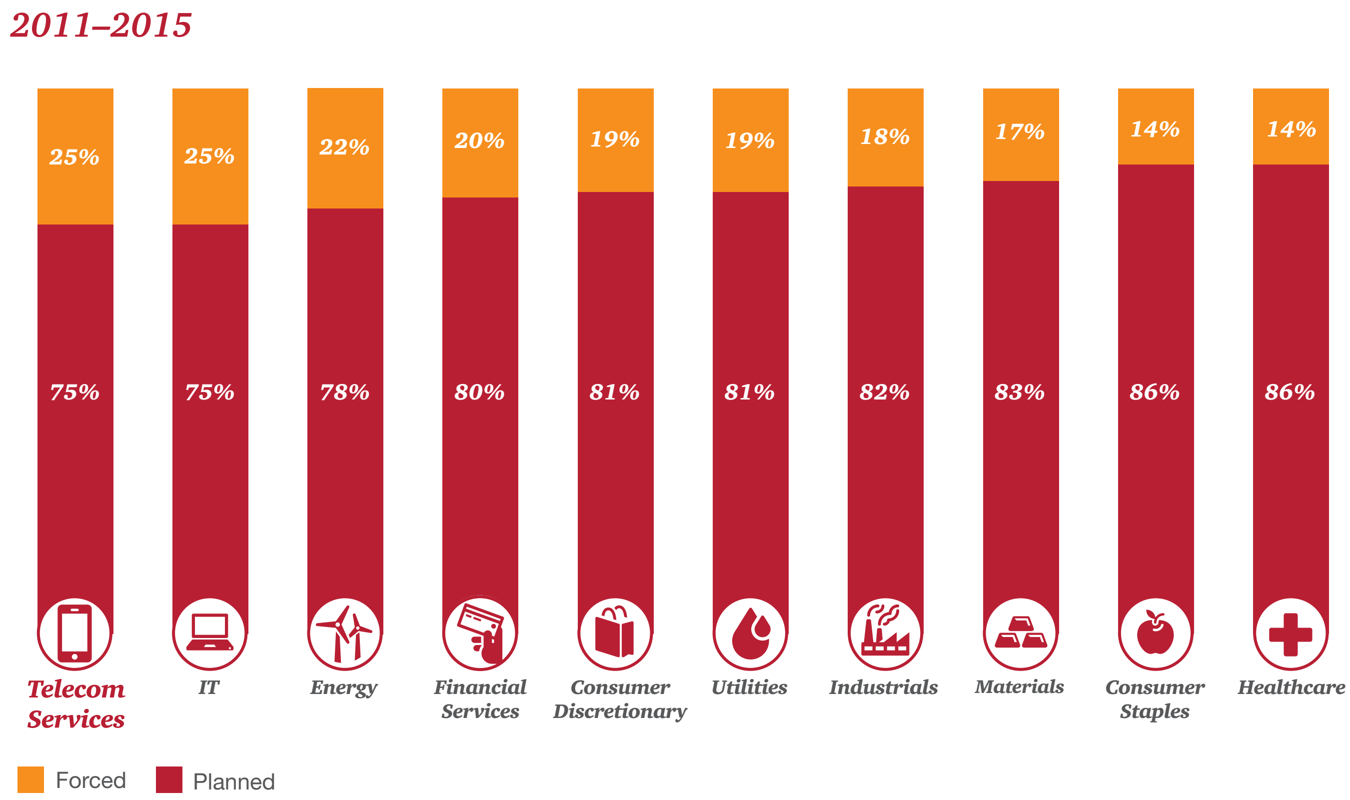
2011–2015 CEO turnover events as a percentage of top 2,500 public companies in each industry



Source: Strategy& 2015 CEO Success Study

Turning to *why* CEO turnovers take place, telecoms once again stands out from the crowd. As Figure 2 shows, communications operators are equal first with IT companies in terms of their proportion of forced – as opposed to planned – CEO turnovers, with fully one in four departing CEOs having been fired. At the other end of the spectrum is healthcare, where just 14% of CEOs end their tenure by being forced to leave.

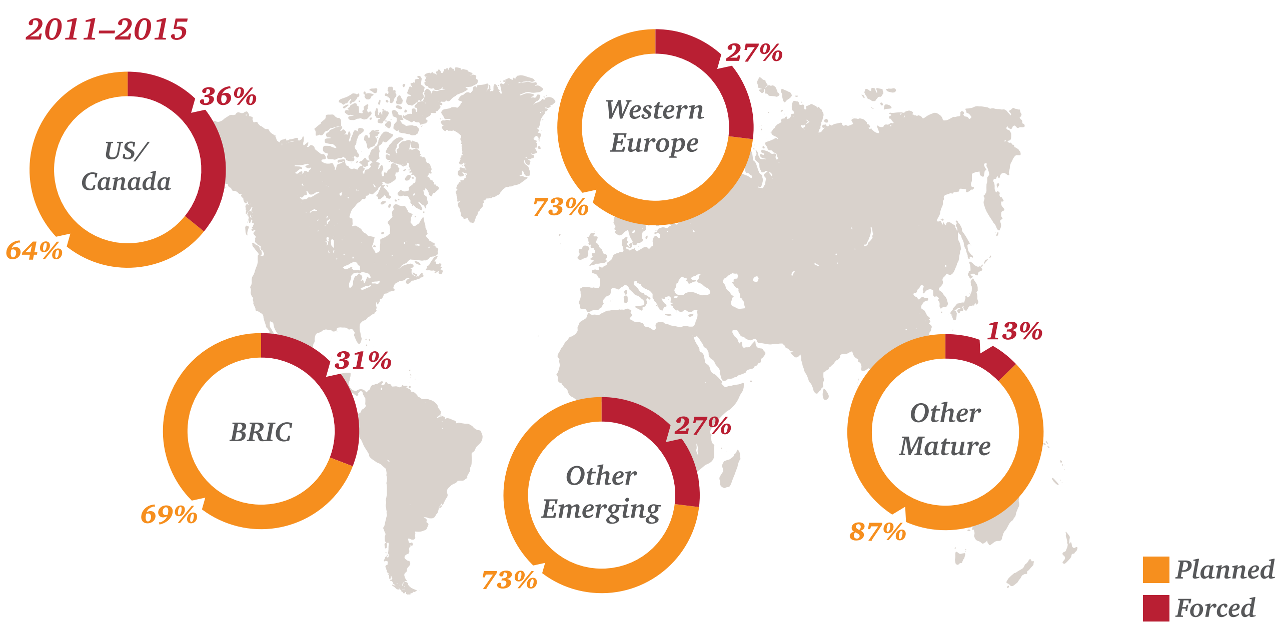
Figure 2: CEO turnover type by industry



Source: Strategy& 2015 CEO Success Study

An analysis of CEO turnover type by region reveals further insights. As Figure 3 shows, the tendency to fire CEOs is greater in the most mature markets such as North America, where the telecoms market is often saturated and growth harder to find.

Figure 3: Telecom services CEO turnover type by region



Source: Strategy& 2015 CEO Success Study

Defending or destroying shareholder value?

In replacing their CEOs – whether through forced or planned succession – telecom operators' boards are clearly looking to protect and grow shareholder value. So, are they succeeding? Unfortunately, our research suggests not.

Using the calculation method described in the accompanying information panel, we assessed the median Total Shareholder Return (TSR) from one year before to one year after each succession. We found that planned CEO successions have a relative market-adjusted median TSR of -4% over the subsequent two years, while forced CEO successions have a median TSR of -13.5%. For the average company among the world's 2,500 largest listed corporations, this relative TSR difference translates to a significant loss in shareholder value. Given that telecom operators' CEO succession pattern is skewed more towards firing CEOs than in other industries, this insight is critical for them.

All CEO transitions are difficult – and even in planned ones, the uncertainty created causes company performance to suffer. Managers ask themselves if the strategy will change and if they will still be needed. Momentum slows, and this is reflected in the negative relative shareholder value development. In forced succession situations, the dismissal of the CEO is often the consequence of many things not being healthy in the company. In many of these forced situations, boards should have addressed the fundamental issues earlier and avoided finding themselves in a situation where the CEO needs to be let go.

Looking outside the industry for experienced consumer-focused leadership

A further observation that appears to correlate well with our research findings is that many CEOs and executives who grew up in the telecoms industry may now be facing significant challenges in adapting their leadership style and organisational structures to today's new and highly dynamic environment.

These challenges reflect the need for telcos to transform their operating model from an infrastructure-centric to a digital- and client-service centric business model. To compete effectively with the new digitally-enabled, customer-focused entrants, they must also recalibrate their businesses to achieve shorter time-to-market cycles, higher degrees of digitization, and more effective and responsive customisation of their products and services to the needs of customers.

Put simply, communications operators now need to put the customers at the heart of their business for the first time. New insights and inspiration can play an important role in helping to achieve this – and for this reason many telco boards are responding by reaching for executives from outside the organisation, with experience of leading customer-centric businesses.

Calculating the impact of CEO turnover on shareholder returns

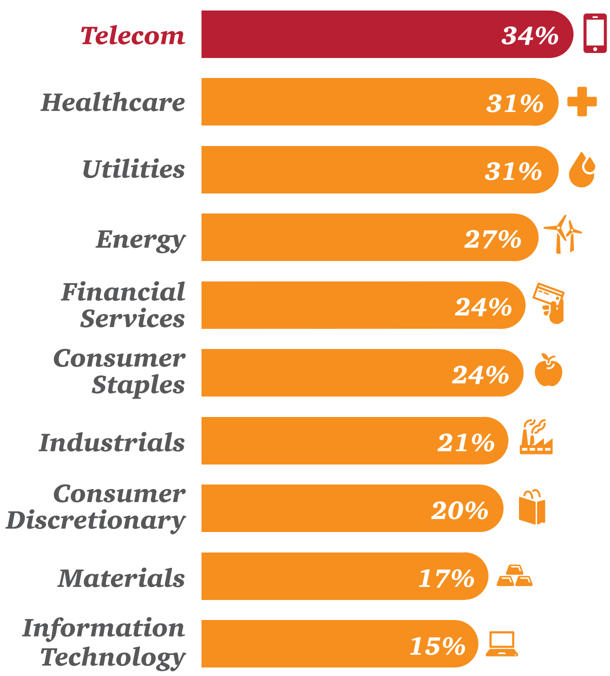
To quantify the effects of a change of CEO on total shareholder return (TSR), we segmented the CEOs into forced and planned successions. For each company, we then computed the relative market adjusted TSR for the one-year period leading up to the succession date and for the immediate one year period following it. Numbers were subsequently aggregated to create aggregated data for forced and planned departures.

For companies with CEO turnovers over a three-year period, we then calculated the median TSR relative to market adjusted indices in the year leading up to the turnover. For those with planned turnovers we found the variance was -0.5%, and for companies with forced turnovers, -13%. In the year following the turnover it was -3.5% for companies with planned turnovers and -0.6% for those with forced turnovers.

As Figure 4 shows, 38% of incoming CEOs joining telecoms companies over the past four years were outsiders, the highest of any sector. Again, it's interesting to note that IT is at the other extreme – with only 15% of incoming CEOs during the same period being outsiders.

Figure 4: Percentage of incoming outsider CEOs by industry

2011–2015



Source: Strategy& 2015 CEO Success Study

Benefits and risks of bringing in a new CEO from outside

For any telco, recruiting a CEO from outside the organisation brings its own advantages and risks. On the positive side, if the company needs to change radically to cope with an increasingly digitalised operating environment, an external candidate who has already gone through a similar process may be a better choice. Another benefit is that outsiders are not burdened with legacy biases and commitments within the current organisation, meaning it may be easier for them to take an objective view about what company needs to do, and make sweeping changes to execute it.

In terms of risks, an outside CEO may lack the internal networks and knowledge to exert influence effectively and survive in the role – especially if they're not given the right support. Hiring an outsider can also hurt the talent pipeline through two immediate knock-on effects. First, aspiring executives who were passed over for the CEO position may decide to leave. And second, the new CEO may want to bring their own people. In combination, these developments can create gaps in the executive ranks.

If the new externally-recruited CEO doesn't work out, companies often find they have to go outside again, because the people filling the top executive roles have not yet had time to prove their skills and leadership. So, while bringing in new skills is an important benefit of hiring from outside, companies must also ensure they continue to build the required skills inside the company in order to generate a robust succession pipeline of leadership talent.

Benefits and risks of bringing in a new CEO from outside

As telecoms companies navigate the transition from asset-intensive to consumer-intensive business models, our research underlines that many CEOs – especially those who have grown up in the industry – face significant challenges in adapting to today's dynamic environment. As a result, more companies are looking for CEOs from outside the organisation.

While this may appear a logical response, it isn't necessarily the best one. In PwC's view, companies can prepare themselves more effectively by implementing robust succession planning processes at the topmost levels of the company – not only for the CEO role – that constantly evaluate both internal and external candidates, in the context of the current and future business environment the firm faces or will face. Such an approach gives the company the best possible chance of making the optimal strategic choice for its own specific business, and then of ensuring that this choice is successful going forward.

In light of this, we would suggest that telecoms companies' boards ask themselves three key questions about their CEO succession process:

Does the board really "own" the succession process?

At many companies, the succession narrative largely revolves around the current CEO. However, what's best for the sitting CEO may not always be best for the development of potential successors. The board should find ways to make CEO succession planning a routine, recurring, and candid topic of discussion.

Is the company truly proactive about developing future generations of CEOs?

Boards should treat CEO succession as a process that will be years in the making, not as a decision made in a knee-jerk fashion over the course of a week or two. Almost two-thirds of internal CEO appointments have spent 12 years or more climbing up the corporate hierarchy.

Is the succession planning backwards-looking or forward-looking?

Boards tend to choose candidates who have thrived under the business model the company has pursued in the past. True, these candidates may have been standouts in that context. But changes in the industry, in markets, or in technologies may point to a need for different competencies and experience in the future.

In their drive to transform for today's increasingly digitally-driven and customer-focused environment, a number of telecoms operators – especially in mature markets – are expanding dramatically into new areas outside their traditional network business. Such moves help to reduce the reliance on returns generated from investments in networks, while also expanding the range of skills they'll need in future, demanding a rebalancing towards more creative talent.

In basic terms, our research shows that – in today's fast-changing marketplace – telecom operators across the world are more likely than companies in most other industries to recruit a CEO from outside. The aim, quite rightly, is to reshape and re-orientate the business towards a greater focus on customers. However, while leadership skills from outside may be attractive, telcos mustn't lose sight of the need to keep developing and drawing on the wealth of talent they already have within their organisations.

About the authors

Christine Rupp

Christine is a Partner with PwC
Strategy& Germany.

Christine can be reached at

christine.rupp@strategyand.de.pwc.com

Per-Ola Karlsson

Per-Ola is a Partner with PwC
Strategy& UAE.

Per-Ola can be reached at

per-ola.karlsson@strategyand.ae.pwc.com

Spencer Herbst

Spencer is a Manager with PwC US.

Spencer can be reached at

spencer.herbst@pwc.com

Thomas Aichberger

Thomas is a Principal with PwC
Strategy& in Austria.

Thomas can be reached at

thomas.aichberger@strategyand.at.pwc.com

About Strategy&

As part of the PwC network, Strategy& helps clients solve their issues from strategy through to execution. We do that by combining our strategy consulting expertise with the vast capabilities of the network, to help you movie your business forward with confidence.