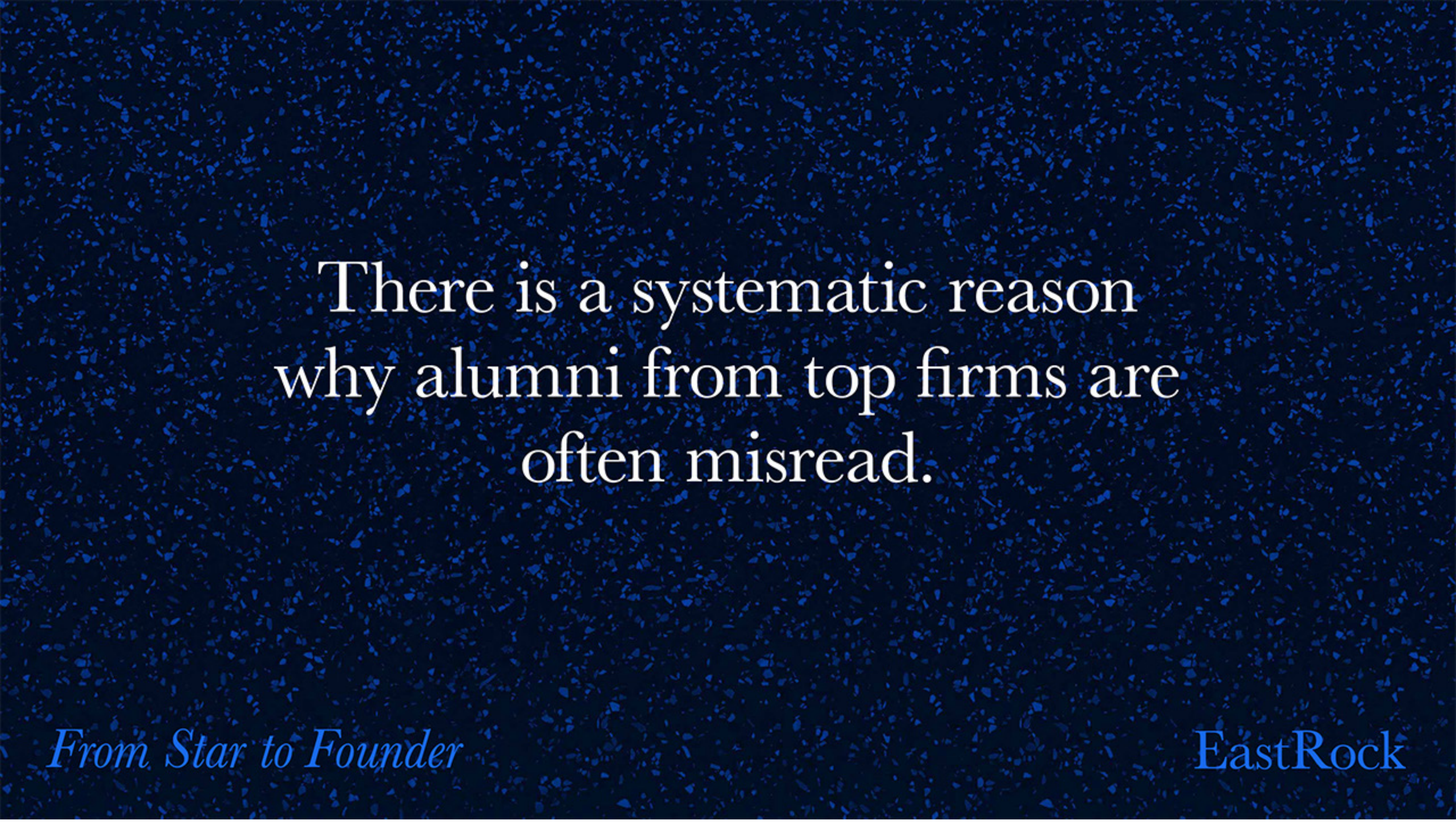

When Stars Shine – and When They Don't: Part 1

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IN MY LAST POST I talked about investment firm founders as a group of insiders who were largely prepped at one of a few training grounds.

In this post, I'd like to raise two caveats:

1. Predicting founder success is not easy – but it is worth it (Remember that manager returns are often highest in the early years)

2. Predicting the success of founders from "blue-chip" companies like Blackstone, Bain Capital and Goldman Sachs is MORE DIFFICULT than assessing outlier talent from many other organizations.

For observers of investment firm formation over the last 15 years, perhaps caveat # 2 is not a surprise. We have all read about spinouts from blue-chip firms that have failed to really launch. Or worse — we've seen some suffer large losses and even blow up. (No, I'm not going to name names. ☺) Anecdotes aside, there is a systematic reason why alumni from top firms are often misread. More on that below.

At East Rock, we focus on identifying and supporting investment firm founders as they make the transition from star employees at large firms to leaders of new ones. As such, a key question we regularly face about a potential founder is: "Was their past success due to them, or was it 'the container?'"

This question is difficult not just for potential allocators but even for founders themselves. And for founders, their entire careers are at stake, so they better get it right!

For a data-driven analysis of this topic, I highly recommend the book Chasing Stars: The Myth of Talent and the Portability of Performance by Harvard Business School Professor Boris Groysberg. I was recently introduced to Professor Groysberg and was pleased to meet a kindred spirit focused on the question of "was it the person or the container?"

Professor Groysberg's book starts with the clever insight that the market for equity research analysts offers a valuable data set to study the portability of talent. The movement of equity research analysts is easy to track from one firm to another, and the subsequent increase or decrease in performance is easy to measure via change in Institutional Investor (II) ratings.

The big headline from Groysberg's book: Although 85% of the equity research analysts he interviewed believed their skills were highly portable, the job performance of star equity analysts who switched employers, on average, plunged sharply and continued to suffer for at least five years after moving to new firms when compared to similar stars who stayed put.

Groysberg emphasizes that the analysts themselves were unable to predict this outcome: "Individuals who are stars in the workplace have a strong and persistent—and potentially career-damaging—tendency to undervalue the importance to their success of their employers' capabilities and resources—and their own practiced ability to make use of these resources."

But there are exceptions!

1. Women's talent seems to be more portable than men's: "In exploring the reasons for women's portable performance, we found that female analysts deliberately and strategically cultivated portable (i.e., external) relationships, resources, and sources of information, and also thought more strategically about the repercussions of moving than did their male counterparts."

2. Teams are more portable than individuals: "We found that stars who changed firms along with teammates experienced no decline in either short- or long-term performance."

3. Some containers are easier to leave unscathed: "Stars from certain investment

> banks suffered no performance penalty when they moved. These banks were those that viewed themselves as offering, in effect, an organizational umbrella for individual analysts' entrepreneurial franchises."

Turning back to the classic breeding grounds of Blackstone et al., Groysberg gives us a hint as to why founders from these places are so hard to assess. In his study, the equity research analysts whose performance suffered most after moves were those who went from top-quality firms to lesser-quality firms. The natural conclusion: the better the container around them, the more likely that it really mattered, and that losing it really hurt.

So, what can be done to better predict founder success? We'll cover that in my next post.

NEWSLETTER
From Star to Founder
Insights from partnering with exceptional investment managers as they launch and build new firms

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