

## Great Founders – Highly Prized but Poorly Understood

### 62% of Start-Ups Fail due to Founding Team Conflict<sup>1</sup>

The human aspect of an investment is most important. It is well known that most start-ups will fail. It is less well known that most start-ups fail because of conflict between the founding team.

At Concentric, this has bothered us for some time. With unprecedented sums going into venture capital investments, we have been continually surprised to find little serious work on what makes a successful founder or founding team.

The venture capital industry has been so focused on understanding what good technology looks like, they've perhaps forgotten what good human beings look like. And this is bizarre because in a world that changes so fast and where so much is not under your control, who you hire and work with is one of the few things that is.

Last year we partnered with Karim Jalbout – head of Egon Zehnder's European technology practice – to assemble a group of industry experts including founders, investors, recruiters and HR consultants.

The aim was to understand and find consensus from a range of perspectives on exactly what makes a founder 'good' and what practical tools are at our disposal to help us identify positive or negative traits during our investment due diligence process.

#### 1. 'Everyone has a plan until they get punched in the mouth' – Mike Tyson

#### *The inside view – founders about founders*

Being an entrepreneur is mostly hustle, overwhelming stress, a lot of false dawns and the occasional bout of vindication. With something like 90%<sup>2</sup> of all start-ups failing, it takes a special sort of person to lead the company that is part of the 10%.

At Concentric, we see first-hand how tough it can be and our founders concurred. Without resilience and proper motivation for the task at hand, a founder simply won't last long. The ability to handle rejection from investors, disappointment from customers and dissatisfaction from employees takes its toll on anyone and is the first thing they look to weed out in potential business partners. The question they constantly ask themselves and evaluate in senior members of their team is – why are they doing this? Are they still hungry and do they have the personal ambition to see out the fight?

A degree of humility is also important. Good founders, from our founder's perspective, continually asked themselves if they were the right person for the job and how they could improve themselves whilst also making sure to listen to the people around them. Perhaps predictably, arrogance was universally disavowed, with all (but one) commenting on how the 'loudest voice in the room' is often not the most important or sensible. Founders must exercise good judgement in listening to the right people at the right time.

But good judgement is a tricky thing. How is it developed? The answer it seems is partly through experience as second time founders were particularly preferred, regardless of whether they had succeeded or not. It was the learnings from that experience that counted. And that ability or willingness to learn was another crucial theme that ran throughout our session. Building a start-up is a journey and the most successful start-ups navigate their way through constantly changing market and competitive pressures. As the great warrior poet Mike Tyson said, just in other words - flexibility of thought under extreme pressure, and a willingness to continually learn are vital traits for those participating in the ring, or indeed building a company.

But what use is learning if;

- 1) The information being learnt is irrelevant
- 2) The founders are unable to action that information?

1. <http://fundersandfounders.com/startup-dirty-laundry-conflicts-that-kill-partnerships/>

2. <https://www.forbes.com/sites/neilpatel/2015/01/16/90-of-startups-will-fail-heres-what-you-need-to-know-about-the-10/#684d36be6679>

Well it seems very little. Founders are continually bombarded with information and must be able to sift out the nonsense, absorb information that is relevant and then action it over a suitable timeframe. To do so requires real conviction and a pro-active mindset that not many people possess. Fortunately, tech founders are a unique breed and the nature of them seems to select for those who are action biased.

Not always though. Our founders reflected upon the balance between curiosity and ability to take decisions within a realistic time frame. 'Paralysis to analysis' they said, could be a real problem for some. Some of the best founders (and indeed investors) were the ones who had an insatiable curiosity and constantly asked themselves why their environment was the way it was. It often led them to design superior solutions. The clichéd 'out of the box' thinking though was useless if not combined with the ability to prioritise effectively and then ruthlessly execute.

As we've alluded to throughout, entrepreneurs and founders are under pressure from every angle and they must be able to deal with that pressure effectively and turn it into something productive. Our founders remarked upon how they are constantly working to manage their stakeholders and use their disparate skills to the benefit of the business. It was vital, they said, to remain accountable and transparent with key stakeholders, especially investors. Attempting to bury bad news seldom worked out well in the long run as it undermined vital relationships. Honesty really is the best policy.

Time and changing cultural attitudes have also played a role in what makes a successful founder today. Many of our founders and 'hybrids' (investors and founders) pointed to how cultural attitudes have changed over time. They pointed out that approaches to management have changed and that the typical 'autocratic' style no longer works. A high level of emotional intelligence is now required.

### *Cultural mash-up*

There is no such thing as a 'good' culture. There are popular ones and there are trending ones, but the only bad one is one that is too diluted, one that doesn't stand for anything. Building a culture that stands for something important, in the eye of its employees at least, is the remit of the founders.

Founders are normally the key factor in shaping company culture. Whilst what constitutes good company culture is outside the remit of this note, we did note some observations over how founders have had to change over the years to adapt to the changing nature of work and changing societal expectations of the working environment.

The first was that the old 'autocratic' style of leadership is no longer welcome. Founders are expected to take their team on a journey by for example, explaining the thought processes behind key decisions. It is no longer good enough to simply dictate next steps. Most importantly though perhaps, founders should serve to unite all employees behind a common purpose. This is of course easier said than done as it's about having a compelling vision in the first place, being able to communicate it and then recruiting those with whom that vision resonates strongly. At an early stage business, it's impossible to overstate how important this is, according to our assembled founders. Without true believers, employee attrition quickly becomes a problem.

### *The Outside View – Investors on Founders*

Investors are not important. They may think they are, but really, they're peripheral at best and shouldn't forget it. Or so the investors present told us. They were all aware that the founders were the superstars, they bear the burden of responsibility and investors are there to support and advise. But of course, investors are also there to identify which founders are capable of making venture-sized returns. It goes without saying these sorts of people are not found everywhere, like Unicorns. So, what did our assembled investors think was important when assessing founders?

Much like our founders, it wasn't arrogance. Overall, we found our investors wanted to invest in people they liked and felt like they could work with. After all, VC investors are in it for the long run and especially for those that are active, working very closely with their founders for a considerable period of time is a given. Indeed one of our investors stated they would simply not invest in founders with personality flaws, but were ok with founders with developmental gaps.

And developmental gaps are not always a sign of a lack of experience. It takes maturity to put long term gain over short term profit and founders investing in self-development as well as surrounding themselves with an experienced and diversified advisory team were commended by the investors present.

Motivation was also critical it seems. Investors wanted to understand why a founder embarked on the company building path and be sure they were doing it for the right reasons. And those 'right' reasons can be diverse. Surprisingly, they didn't have to be financial with some of our investors citing how some entrepreneurs were motivated by the social impact a business might have or the value it brought to the wider ecosystem. Part of what they looked to gain was simply confidence in a founder's ability to weather a storm. Echoing the thoughts of our founders, building a tech business for venture sized returns is tough and when things start to look bleak, which founders are going to be the ones to battle on through?

Our hybrids drew from personal experience and reflected upon their time building companies across the globe. Rocket Internet for instance was well renowned for hiring high achievers from the top universities around the world to build out their businesses. In the good times this tactic appeared to work well. When the tide turned and their high salaries could no longer be sustained, so did these employees and to the detriment of the wider organisation.

Like the founders, the investors were looking for those founders who they felt could adapt with the company. A founder will have to take his or her company through economic and business cycles and this clearly requires a multitude of different

skills. Interestingly, this requires giving up control of certain functions at the appropriate time and considering most founders have a paternal relationship with their businesses, the psychological shift required here is not to be underestimated.

That begs the question though, why do entrepreneurs who do not possess these traits get funding? One theory mooted on the day blamed society's current obsession with celebrity culture. Perhaps inexperienced investors are led to invest in people who mimic those we see on the TV – the loud, the brash, the coarse. That said, one investor in the room claimed there was a place for 'a\*\*\*\*\*s' as they can often mitigate groupthink, just perhaps not as lead founder.

Another investor sagely noted; he'd rarely been pleasantly surprised by a team once they'd got his money. Those pre-investment meetings are as good as it ever gets. Founders: they'd better be outstanding.

*'I appreciate what you're saying, but ...'*

Also in attendance was Saberr, a technology business focusing on identifying teams likely to be successful. Their hypothesis is that teams matter more than individuals and their proprietary technology has achieved some impressive results. If you want to predict success they posit, you should be looking at the *relationships* between individuals as this is the only statistically proven factor. The key trait to look for in individuals is tolerance, but in particular tolerance toward other people across a range of different factors. If an individual has a strong view on a particular issue, but is tolerant toward other views on that same issue, even if it opposes theirs, then it's likely they'll be able to work effectively with that person. Summed up over a range of factors and across many individuals, you have the basis for understanding if a team will perform well together.

Humans are experts at finding patterns that aren't there. By looking for characteristics of founders at purely the individual level, that's exactly what we're doing. Correlation is not causation and so looking for gender or age norms for example can be misleading. Our partner from

Egon Zehnder passionately agreed. He argued that isolating individuals can be a predictor of success but is rarely conclusive. Really we need to evaluate people in the context of who they're going to be working with.

## 2. The Founder Shopping List

So, it turns out that this note on founders' characteristics is not just about individual founder characteristics. Ideally the founder team is balanced in a way as to complement each other's strengths.

We summarise below the eight most frequently cited personality trait categories below that were considered critical. Of course, they relate as much to the founder team as they do to its individual members.

Its often the case that founders as any other human beings do not score perfectly on all the counts. That of course in itself is to be expected, however some of the founder traits were considered to be so fundamental that an investment could not be made without a founder team collectively possessing them.

| Trait                         | Relative importance → |   |   |
|-------------------------------|-----------------------|---|---|
| Resilience & Energy           |                       |   | • |
| Ambition & Motivation         |                       |   | • |
| Ability to convince / sell    |                       |   | • |
| Humility & Self reflection    |                       |   | • |
| Vision                        |                       | • |   |
| Balanced founder teams        |                       | • |   |
| Pro-active                    | •                     |   |   |
| Honest stakeholder management | •                     |   |   |

Excellent. We've identified what a good founder team looks like. But, the question now becomes, how do we identify these people in practice and embed this new way of thinking into an investment process?

## 3. The Concentric Founder Evaluation Process

At Concentric, we've made ensuring we work with the right sort of people as important as evaluating company metrics. In order to identify the right founders and teams, we've embedded questions, tips and tricks designed to filter out those founders who do not share the traits laid out above into every stage of our investment process.

### 1. Preliminary Analysis

- Experienced: Second time founder or operators?
- Referred by Concentric network?

### 2. Deep Dive

- Resilience: >1 founder? Energy level, speed
- Motivation: How much are they paying themselves? Why are they building a business?
- Tolerant: Work with founders, spend time with them and test their thought processes
- Energising: The Zuckerberg Test – would we want to work for this person?
- Maturity: Do they hire people who may threaten them? Particularly in tech
- Sales ability: Elegant sales process. Winner mentality

### 3. DD

- Communication & Vision: Interview each member and ask them what the company stands for, what are its values
- Team: Interviews; look for homogeneity of culture and values but diversity of skills
- Honest: Does the founder say 'invest' or 'spend'? Is the information flow 'open'?
- Judgement: Judgement Index (online tool)
- Tolerance: Saberr team profile
- Agreeable: Meet the other half – a tip from one of our co-investors; Sir Alex Ferguson
- Resilient: Peer referencing - focus on understanding development gaps and put the feedback to the founder to gauge their reaction. Peer referencing is better and ask them 'why' a lot

#### 4. Bonus tests!

If you want to really put your founders through it, give these a go!

- Ask a waiter to bring them the wrong order *twice* in a restaurant and see how they react
- Tell them the feedback from peer interviews was not positive again to test their reaction

#### Parting thoughts

Founders are as diverse as the companies they build. Our job as active investors is to partner with founders, and ideally teams.

Such partnerships come with a lengthy tenor attached – typically longer than an average European marriage. In order to persevere together through this journey of building a business there has to be strong alignment of values, with differing but complimentary skill set across investor and founder teams.

At first glance it may seem onerous, intrusive and perhaps even pretentious to spend so much time detailing and then seeking out certain characteristics of a founder team. However, we learned through painful mistakes that there is no getting out of a venture vessel once it sets sail with you on board.

The fit between an investor and a founder has to go both ways and we look forward to conducting our next deep dive into what makes investors bearable – stay tuned!

#### About Concentric

*Concentric is a technology investment partnership that invests in early-stage European software technology companies.*

*We partner with founders who have built original and scalable products with a proven business-model and a product-market fit.*

*We are substantially invested in the partnership with our entrepreneurs and look to support their growth by deploying both financial as well as human capital.*

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#### About Egon Zehnder

*Egon Zehnder is a global leadership advisory and executive search firm, with 68 offices in 40 countries around the world, including tech hubs London, Palo Alto, Berlin, Paris and Bangalore.*

*Our technology practice partners with large businesses across both B2C & B2B sectors as well as with founders/VCs scaling their early stage companies.*

*We support the appointment of Board, CEO and key functional leadership roles (Technology, Product, People, Marketing and Data/AI) as well as advising teams on culture and the future potential of their leaders.*

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