



The CenterCap Group is a boutique, real estate focused investment bank providing strategic advisory, capital raising, and consulting related services to public and private sector companies and fund managers across the real estate industry.

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CCG PERSPECTIVES

The Importance of Succession Planning

By Deborah Smith

Given many firms in the real estate space recently have taken on the task of addressing succession planning, it seems like an opportune time to encourage those who have put the task on the backburner to change their priorities. We talk with senior executives of fund managers and operating companies and one thing is clear – they are focused on growth, their investors, their P&L, their employees, and not what happens if they aren't there anymore. They see succession planning like writing a will – a task for the day after tomorrow. A day that never comes. What we tell our clients is that implementing a succession plan is critical to a firm's long-term success, value and longevity. It is particularly vital for companies where its' current successes and/or value is critically tied to one or a handful of individuals.

The real estate sector is characterized by personal relationships, reputations, credibility-tied individual investing prowess, and entrepreneurs who have created significant wealth from their efforts, street smarts and commitment to risk in the chase for reward. They have been successful at it. Unsurprisingly then, the owner(s), iconic senior executives' or founders' contributions may be intricately entwined with the value and future of the firm, the strength of its relationships with clients, investors, employees as well as its position in the industry.

From a capital raising perspective, succession planning is increasingly becoming a big deal to the investor universe and some would argue investors are an important driver to the dialogue around succession planning considerations. Indeed, succession planning, profit sharing and incentive questions are increasingly becoming common for fund managers as part of LP due diligence.

Succession planning is a complicated event rather than a single event. It takes time to formulate and likely more time to implement. A succession plan should be drafted to gradually transition ownership and leadership to the next generation of managers. Depending on the size and structure of the firm, it can take years to effectively implement a succession plan. It's critical to understand which employees are fit and ready to be elevated when key senior executives leave. If companies are concerned about today's readiness of the next layer of people to move upwards in the organization, then it behooves current senior management to start thinking about what is required to improve readiness - investing time, effort, resources into identified managers – or alternatively, it might be necessary to entertain hiring outside talent and/or pursuing corporate strategic alternatives.

Without a well-established plan in place, any number of issues can run unchecked. A sudden vacancy can throw a business and its employees into a potentially devastating maelstrom of uncertainty. Skills may leave with long-term leaders if a handoff isn't begun early. Internal power struggles may ensue without a proper plan established, clients may suffer from a dip in standards or unmet expectations, and investors and partners may view the long-term sustainability of your company in jeopardy and act accordingly.

So where do you start? A succession plan should address both planned and unplanned departures. Blackstone, KKR and Carlyle all set in play organized well-structured succession plans over the past two years that detailed management transitions and timing. On the other hand, Angelo Gordon was rocked by the death of global head of real estate, Keith Barket, in 2010. In 2016, following the death of John Angelo, its co-founder, the company announced succession planning initiatives. On the other hand, in 2016, Composition Capital was hit hard by the sudden death of its founder Erwin Stouthamer, and the company was eventually wound down in 2017. Having known Erwin personally, our firm was similarly devastated by his death.

One of the first steps of a good succession plan may be to undertake a business valuation exercise. Understanding what the company is worth helps provide a framework to determine the company's best option(s) when it comes to a successful transition. Each firm has its own unique circumstances when it comes to determining the enterprise value of their business. The next step a company should take is to clarify their goals and determine its priorities. What's important to them. Companies have to decide what they want for their future. Then they need to decide how to go about executing in the event of senior leader retirement(s), or in the event of unforeseen circumstances. They have to choose a reasonable time frame and identify the events or opportunities that might accelerate or delay their timing. Once a clear existing strategy goal for the firm is set, then the company has to determine what transition strategy best suits the company. Viewing your managers through a critical eye is necessary and appropriate. Do you

have inside talent that can take on the pursuing the long term goals of the company? Can they step up into broader roles than currently performing? If not, why not. Exploring broader strategic alternatives may be a worthwhile exercise as well. Such an exercise will likely be valuable in exploring paths of growth for the company (some unchartered but viable) but also forge a thought process as to direction and vision the company.

There is no one shoe fits all solution. But next time you are enjoying a quiet moment and can plunge into deep thoughts, it would behoove you to think about whether your company would be able to carry on without you, or any particular senior executive(s), at any time without materially impacting the business, its clients, its investors and its employees. You may not like the answers. If not, this is the exact time you need to recognize succession planning should be elevated in your list of daily priorities.