How Andreessen Horowitz Evaluates CEOs

by Ben Horowitz

storytelling

> *“I mean damn, did you even see the test*
> *You got D’s, motherf*$@%&, D’s! Rosie Perez”*
> *—Kanye West, Good Morning*

No position in a company is more important than the CEO and, as a result, no job gets more scrutiny. Sadly, little of this analysis benefits CEOs as most of the discussions happen behind their backs. This post is a step in the opposite direction. By describing how Andreessen

Horowitz evaluates CEOs, I am at the same time describing what I think the job of the CEO is. Here are the key questions we ask:

1. Does the CEO know what to do?

2. Can the CEO get the company to do what she knows?

3. Did the CEO achieve the desired results against an appropriate set of objectives?

1. Does the CEO know what to do?

One should interpret this question as broadly as possible. Does the CEO know what to do in all matters all of the time? This includes matters of personnel, matters of financing, matters of product strategy, matters of goal sizing, matters of marketing. At a macro level, does the CEO set the right strategy for the company and know its implications in every detail of the company?

I evaluate two distinct facets of knowing what to do:

Strategy—At Andreessen Horowitz, we like to say that in good companies, the *story* and the *strategy* are the same thing. As a result, the proper output of all the strategic work is *the story*.
Decision making—At the detailed level, the output of *knowing what to do* is *the speed and quality of the CEO's decisions*.

The Strategy and the Story

The CEO must set the context that every employee operates within. This context gives meaning to the specific work that people do, aligns interests, enables decision-making and provides motivation. Well-structured goals and objectives contribute to the context, but they do not provide the whole story. More to the point, goals and objectives are not *the story*. The story of the company goes beyond quarterly or annual goals and gets to the hardcore question of *why*? *Why* should I join this company? *Why* should I be excited to work here? *Why* should I buy your product? *Why* should I invest in the company? *Why* is the world better off as a result of this company's existence?

When a company clearly articulates its story, the context for everyone—employees, partners, customers, investors, and the press—becomes clear: When a company fails to tell its story, you hear phrases like:

"These reporters don't get it."

"Who is responsible for the strategy in this company?"

"We have great technology, but need marketing help."

The CEO doesn't have to be the creator of the vision. Nor does she have to be the creator of the story. But she must be the keeper of the vision and the story. As such, the CEO ensures that the company story is clear and compelling.

The story is not the mission statement; the story does not have to be succinct. It is the story. Companies can take as long as they need to tell it, but they must tell it and it must be compelling. A company without a story is a usually a company without a strategy.

Want to see a great company story? Read Jeff Bezos' 3-page letter he wrote to shareholders in 1997. In telling Amazon's story in this extended from—not as mission statement, not as a tagline—Jeff got all the people who mattered on the same page about what Amazon was about.

Decision Making

Some employees make products, some make sales; the CEO makes decisions. Therefore, a CEO can most accurately be measured by the speed and quality of those decisions. Great decisions come from CEOs who display an elite combination of intelligence, logic, and courage.

Courage is particularly important, because every decision that a CEO makes is based on incomplete information. In fact, at the time of the decision, the CEO will generally have less than 10% of the information typically present in the ensuing Harvard Business School case study. As a result, the CEO must have the courage to bet the company on a direction even though she does not know if the direction is right. The most difficult decisions (and often the most important) are difficult precisely because they will be deeply unpopular with the CEO's most important constituencies (employees, investors, and customers).

In my personal experience, the best decision that I made in my career—the decision to sell the Loudcloud business to EDS and become Opsware the software company—would have lost by landslide had I put it to vote with my employees, my investors, or my customers.

As CEO, there is never enough time to gather all information needed to make a decision. The CEO must make hundreds of decisions big and small in the course of a typical week. The CEO cannot simply stop all other activities to gather comprehensive data and do exhaustive analysis make that single decision. Knowing this, the CEO must be continuously and systematically gathering knowledge in their day-to-day activities so that they will have as much information as possible when the decision point presents itself.

In order to prepare to make any decision, the CEO must systematically acquire the knowledge of everything that might impact any decision that she might make. Questions such as:

What are the competitors likely to do?

What's possible technically and in what time frame?

What are the true capabilities of the organization and how can you maximize them?

How much financial risk does this imply?

What will the issues be given your current product architecture?

Will the employees be energized or despondent about this promotion?

Great CEOs build exceptional strategies for gathering the required information continuously. They embed their quest for intelligence into all of their daily actions from staff meetings to customer meetings to 1:1s. Winning strategies are built on comprehensive knowledge gathered in every interaction the CEO has with an employee, a customer, a partner, an investor, and so on.

2. Can the CEO get the company to do what she knows?

If the CEO paints a compelling vision and makes fast, high quality decisions, can she then get the company to execute on her vision and decisions? The first ingredient in being able to do this is leadership as I outlined in a previous post Notes on Leadership.

In addition, executing well requires a broad set of operational skills. The larger the organization, the more elaborate the requisite skill set.

In order for a company to execute a broad set of decisions and initiatives, it must:

Have the capacity to do so – In other words, the company must contain the necessary talent in the right positions to execute the strategy.

Be a place where every employees can get things accomplished – the employees must be motivated, communication must be strong, the amount of common knowledge must be vast, and the context must be clear.

Is the CEO building a world-class team?

The CEO is responsible for the executive team plus the fundamental interview and hiring processes for all employees. She must make sure that the company sources the best candidates and that the screening processes yield the candidates with the right combination of talent and skills. Ensuring the quality of the team is a core part of running the company. Great CEOs constantly assess whether or not they are building the best team.

The output of this capability is the quality of the team. It's important to note that team quality is tightly tied to the specific needs of the company in the challenges that it faces at the point in time that it faces them. As a result, it's quite possible that the executive team changes several times, but the team a) is high quality the entire way and b) there is no attrition problem.

Is it is easy for employees to contribute to the mission?

The second part of the evaluation determines whether or not the CEO can effectively run the company. To test this, I like to ask this question: "how easy is it for any given individual contributor to get their job done?"

In well-run organizations, people can focus on their work (as opposed to politics and bureaucratic procedures) and have confidence that if they get their work done, good things will happen for both the company and them personally. By contrast, in a poor organization, people spend much of their time fighting organizational boundaries and broken processes.

While quite easy to describe, building a well-run organization requires a high level of skill. The skills required range from organizational design to performance management. They involve the incentive structure and the communication architecture that drives and enables every individual employee. When a CEO "fails to scale," it's usually along this dimension. In practice, very few CEOs get an "A" on this particular test.

Netflix's CEO Reed Hastings put great effort into designing a system that enables employees to be maximally effective. His presentation on this design is called Reference Guide on our Freedom and Responsibility Culture. It walks through what Netflix values in their employees, how they screen for those values during the interview process, how they reinforce those values, and how they scale this system as the number of employees grows.

3. Results against objectives

When measuring results against objectives, start by making sure the objectives are correct. CEOs who excel at board management can "succeed" by setting objectives artificially low. Great CEOs who fail to pay attention to board management can "fail" by setting objectives too high. Early in a company's development, objectives can be particularly misleading as nobody really knows the true size of the opportunity. Therefore, the first task in accurately measuring results is setting objectives correctly.

We also try to keep in mind that the size and nature of the opportunity varies quite a bit across companies. Hoping that VMWare can be as capital light as SolarWinds or trying to get Yelp to grow as fast as Twitter doesn't make sense and can be quite destructive. CEOs should be evaluated against their company's opportunity – not somebody else's company. Let me share a funny story which illustrates a CEO really owning delivering against results. This story is from Robin Li, CEO of Baidu. He shares that on the day of Baidu's IPO—usually one of an entrepreneur's most exhilirating days of his entire life—he sat at his desk terrified. Why? Listen to how Robin owned delivering results:

> *In 2004, we raised our last round of VC money led by Draper Fisher Jurvetson…and Google, one of our great colleagues. Then a year later, in 2005, the company went public. The ideal price was $27 [the stock's initial offer price] and it closed on the first day at $122. It was great with us for many of the Baidu employees and for all of the Baidu investors. It was a very miserable thing for me because when I decided to take the company public, I was only prepared to deliver financial results that match the price of $27 or maybe a little higher, $30, $40. But I was really shocked to see that the price went to $122 on the first day. So that meant I needed to deliver real results that matches an expectation much, much higher than what I had prepared to do. But in any case, I thought I had no choice. So I put my head down and focused on operation, focused on technology, focused on the user's experience, and I delivered.*

Once we've taken all of this into account, we see that black box results are a *lagging* indicator. And as they say in the mutual fund prospectuses, "past performance is no guarantee of future performance." The white box CEO evaluation criteria—"does the CEO know what to do?" and "can the CEO get the company to do it?"—will do a much better job of predicting the future.

Closing Thought

CEO evaluation need not be a byzantine, unstated art. All people, including CEOs, will perform better on a test if they know the questions ahead of time.

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