Private Equity International

Operating Partners Forum
New York 2020

October 14 - 15 | Convene 117 West 46th

Six trends in value creation

From analytics to zero-based budgeting, PEI's A-Z shows value creation is a golden thread running through the investment cycle.

PEI

Six trends in value creation

1 IT STARTS WITH A VISION

A vision is essential. It is the guiding light that clarifies a business's financial goals and strategic objectives and determines the selection of value creation initiatives that will deliver them.

Having a vision "is a key part of being a good leader of a company and CEO", says Olof Faxander, head of the operational team at Nordic Capital. "If management and the entire organisation understand the overall vision and direction, everything is much clearer." Then, as "reality hits", it is easier to make decisions and the business can adapt its strategy, he adds.

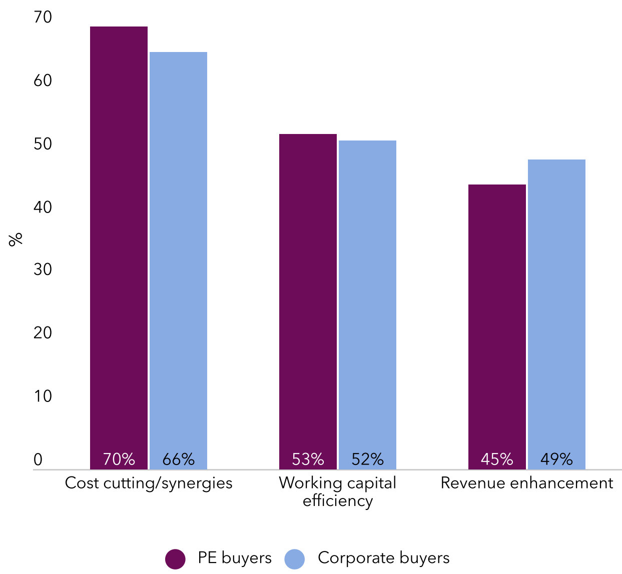
"Having a visionary approach and leadership courage to hire the right people and give them the right tools and authority to make changes, means you have happier staff and better staff retention, and people go through the change curve quicker," says David Olsson, partner at advisors Beyond the Deal. "If you want to create value, productivity is the key. Getting everyone working smarter as opposed to just faster – that is going to increase the intrinsic value of your business." And that starts with honing a vision, even before the deal is signed.

2 PRE-DEAL IS CRITICAL

Embarking on the value creation journey on day one of ownership is too late. In a hotly competitive market where buyers are paying soaring multiples, GPs must use all the time they have available to find all the avenues of growth available at a target business. Increasingly, operating partners are involved in the initial sift of deals in the pipeline. Then, during diligence, the portfolio or value creation team can be found digging into the detail to identify potential value creation drivers. They also have a role to play in contributing to the ultimate investment decision. Their expertise helps GPs decide whether the price is worth paying, or indeed if the value creation levers are so strong it is worth paying even more. "Deal due diligence is not simply about creating a picture of the company at one point in time," says Friederich von Hurter, partner M&A integration at PwC Germany. "It now means collecting and interpreting numbers and providing advisory services to create and implement a future-proof plan."

CRITICAL LEVERAGE

Percentage of deals in which value was realised by lever



Source: PwC, 2018 survey of 100 PE executives and 600 corporate M&A executives

3 GOOD PEOPLE ARE ESSENTIAL

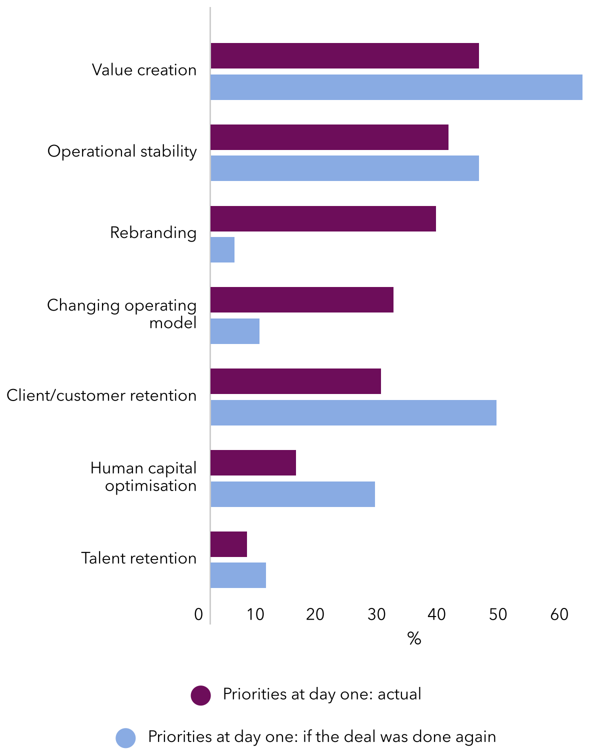
Although it is often difficult to place a specific monetary value on initiatives related to people, such as chief executive succession planning or refreshing organisational culture, GPs increasingly realise the benefits of getting people issues right; and the damage to value creation potential of getting them wrong. "If you don't enable things to go well around people, you can't achieve good financial outcomes," says Dawn Marriott, partner at Hg, where she heads the portfolio team. "Understanding the people dynamics and the organisational structure are very important to driving change and future value.

"You could have an average product and a world class team and I think you could still get a world class outcome."

ECI investment director Duncan Ramsay agrees: "Staff retention, satisfaction and engagement is proving to be an ever more important and difficult challenge. Our experience is that there is a strong correlation between the strength of a business's culture and its success." This requires finding the right people with the right talent and skills and supporting and incentivising them, Marriott notes, adding the firm is spending more time on people issues than it was five years ago. The other area where Hg's focus has intensified is data and automation, she adds.

TOP PRIORITIES

Value creation is a key day one priority for dealmakers



Source: PwC, survey of 100 PE executives

4 DIGITISATION IS EVERYWHERE

Digital disruption and transformation have permeated every business sector, presenting risks and opportunities GPs cannot ignore. "Digitisation is impacting all the businesses we work with – whether it is helping them pivot to direct digital marketing and communication with clients; or using data within a business for greater insight and efficiency; or using or developing software to improve performance or to sell as a product," says Gareth Whiley, managing partner at Silverfleet Capital.

So, where do you start? "Understanding the digital maturity of a company and relative threats to position from competitors and potential market disrupters is the first step in delivering successful digital transformation," says James Prebble, director at Palladium Digital. He adds that insights from digital due diligence can be used "in post-transaction planning to enable investors to accelerate value creation. Because of the scalability and immediacy of digital change, digitisation should be viewed as a strategic imperative for all private equity firms".

"Digitisation is an important lever for organic growth and productivity," says Alain Vourch, partner at Charterhouse Capital Partners, which is encouraging its portfolio companies to step up their investment in digital marketing and other tools to drive productivity, and also to ensure they have the right level of digital expertise.

This might mean hiring a chief digital officer, putting in place data infrastructure and analytics or upgrading cybersecurity. "It's a big item during our onboarding phase," says Vourch.

5 DATA AND ANALYTICS TOP THE AGENDA

Closely tied to digitisation is the potential for data and analytics to power value creation.

Often, these two sources of additional business insight are left untapped by entrepreneurial business owners who are unaware the data (and its potential) exists, or, have not had time or capabilities to unearth it.

"We believe the opportunity to create value through data is now greater than it has ever been before," says ECI's Ramsay. "The volume of data generated globally continues to double every two or three years, with the capacity to store this data rocketing and the associated costs of that plummeting."

Prebble adds: "Today's best performing companies are utilising data and supporting technologies to drive operational excellence, sales and marketing efficiencies and improved customer experience, generating significant returns for their investors."

It is also critical to the deal process itself. Data allow a GP to "understand proof points or opportunities to do better", says Marriott.

"Whether we are focused on a potential investment or we are looking at how we help a company run itself better, the data team are extensively involved," she says.

6 BEING RESPONSIBLE IS A MUST

"If you want to talk about trends, ESG is one of the strongest right now to drive long-term value," says Faxander. Consideration of environmental, social and governance impacts and risks filters throughout the value creation process, from assessing a deal to improving governance and operational best practice to positioning a business at exit for potential buyers.

An example of ESG's reach is GP focus on improving ESG within the supply chain. "Private equity is leading the way in bringing this [attention to ESG in procurement] to small to mid-size growing companies," says James Bousher, senior manager operations performance at consultants Ayming.

"For them the focus has never been ESG. It's been growing the company. Private equity's influence is stabilising and will allow them to focus on reassessing the value stream risk element and the social good and positive externalities."

Martin Calderbank, managing partner at Agilitas Private Equity, adds: "When done properly, investing responsibly can aid the defensibility of a portfolio and be a powerful value creation tool.

"There are different ways of achieving this, but at Agilitas we do it by only backing companies where positive societal or planetary purpose and shareholder value are fundamentally aligned."