

Private Equity
International

Operating Partners Forum New York 2021

20-21 October 2021

Interactive Working Groups:
**Connecting operating partners in
specific areas of interest**

PEI

The Operating Partners Working Groups

The Operating Partners Interactive Working Groups brought together operating partners at our New York forum to discuss specific areas of value creation in intimate groups.

With the help of our partners, we have produced this report on the sessions at the event.

Thank you to our sponsors and all those that took part in such fruitful discussions.

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Interactive Working Group

Deep dive discussion for operating partners only:

Writing the next chapter of the value creation playbook



Host: **John Annakin**
Director
RSM

Key concepts that surfaced from the following topics:

Value creation planning

- The consensus of the group was there is no universal approach to value creation planning; however, it should start during the due diligence phase when key themes around opportunities can be flagged
- Most participants said they focus on creating highly detailed value creation plans using a phased approach versus a 100-day plan, which focuses on tactical execution of priority activities
- There was agreement around portfolio companies taking ownership of value creation, which makes it critical they receive the plan early and keep it updated
- In terms of how value creation planning may evolve, the group's post-pandemic prediction is there will be an acceleration of widespread digital transformation
 - Some participants expressed seeing heavier usage of and good value being derived from low-code/no-code development platforms;

and they also cited change management and organizational culture as important considerations for successful implementation

Performance measurement

- The question was raised if private equity firms are using objectives and key results (OKRs), and if so, through what performance management systems? It was noted that limited usage of OKRs can pose challenges during implementation, at least initially
- The conversation then turned to management by objectives (MBOs) and how to translate qualitative measures into quantitative metrics
- There was also an expressed interest by the group to know if firms are measuring employee engagement, and some participants said they did for all levels of management

Post-transaction integration

- The conversation started with a brief discussion around the importance of pricing, go-to-market (GTM) strategy and ecommerce

- There were broad responses to an inquiry about whether firms are underwriting synergies
- When asked if M&A is considered part of a value creation plan, participants gave differing responses based on the size and scale of their companies
 - Larger companies tended to have dedicated integration teams, while smaller companies expressed wanting more support, such as their need for financial consolidation tools

Environmental, social and governance (ESG)

- The dialogue around ESG centered on its growing importance in private equity transactions, including considerations around investor/ LP requirements, with some participants stating ESG is sometime a gating issue while others mandate it.
- The consensus was that ESG has become a priority and that compliance departments are being implemented as a result
- The conversation ended with a brainstorm session about linking ESG programs to positive EBITDA outcomes—e.g., the benefits of energy efficiency, and leveraging supply chain to gain competitive advantage—with the takeaway being that companies need help connecting the dots

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Interactive Working Group

Deep dive discussion for operating partners only:

Working with CEOs—dos and don'ts



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The working group engaged in a lively discussion and shared war stories of CEO relationships gone wrong and then explored what it takes to set that most important relationship up for success.

Priorities

While the investment thesis is usually clear to the deal and operating team, we often assume that the CEO has fully absorbed and is aligned with the value creation plan. Like “two ships passing in the night,” the CEO and the investors might be looking at the same goal but have very different interpretations of how to get there or what it will take. It is helpful to invest time upfront and share the investment thesis with the CEO and management team so they understand the vision. Your natural inclination might be to dive deep and start tackling priorities one after another. However, taking a step back to formally onboard the CEO onto the platform and build the alignment on a near and longer-term definition of success is the most critical step in the first days of the investment.

Who

The magic will happen only if you have the right person in the role. Many shared war stories of instances where they had that nagging gut feeling that the CEO might not work out and yet didn't act fast enough on it. As the group agreed, people issues are nothing like wine - they do not age well. Betting on the right person is the most important lever to accelerate value creation. Once you have the CEO in the seat, you should project confidence and make them feel safe even if they make a mistake: You have to let them know you will back them until you don't. And while the person might have the right skillset, we tend to underestimate their motivation to fully own the next stage of the journey, so making sure they are not only aligned but also committed becomes an important conversation to have. It is critical to tease out potential points of misalignment with their career path or personal life situation ahead of getting them in the role.



Relationships

Every success story and productive CEO relationship has one ingredient in common and that is trust. However, operating partners are seen as the extension of the deal team which makes it hard for the CEO to openly share what is top of mind. Trust has to be earned, and making implicit explicit is one way of getting there faster. Participants shared the importance of being clear with the CEO when it's okay to have a discrete 'between friends' discussion versus explicitly indicating what information will be shared back with the investor team. The group also highlighted the importance of overinvesting in social time, even if on screen, and showing the passion and curiosity about the business. As the saying goes: "People don't care how much you know, until they know how much you care."

CEO Leadership Behaviors

The group was curious to discuss the traits and competencies that successful CEOs have in common. We explored four leadership behaviors drawing on ghSMART researching based on over 1,700 CEO assessments conducted over 25 years: 1) The ability to make decisions fast with imperfect information; 2) Adaptability to change the course when external and internal trends change, 3) Engaging for impact not likeability 4) Delivering reliably and consistently.



Interactive Working Group

Deep dive discussion for operating partners only:

Putting ESG at the heart of your business strategy in the new sustainable economy



Host:

Donald Reed

Managing Director, Finance
Transformation

PwC

The discussion revolved around the following topics:

How does your firm think about ESG, and what specific areas within E, S, and G are covered?

- Several participants noted that their firm was transitioning from an ESG mentality based on compliance with LPs interests and requirements on ESG to one of value creation through ESG.
- Most described this transition as still “partial”
- One participant asked whether PE firms were doing a disservice by thinking about ESG solely in terms of value creation
- As an alternative, this participant said that his firm simply puts ESG as a broad topic on the agenda of portfolio company boards to assure that it's on the company's
- Out sourced ESG due diligence as separate diligence workstream vs
- ESG integrated into quality of earning, commercial, tax, HR, etc.
- General feeling that the value of stand alone ESG due diligence is low and diminishing.
- One participant made the point to distinguish ESG due diligence from environmental liability diligence which is critical for particular assets
- One participant outlined three distinct value objectives in due diligence:
 - Avoiding red flags
 - Avoiding value erosion from ESG sources
 - Capitalizing on ESG opportunities as a source of growth
- Appropriate ESG due diligence sets the stage for operating improvement plan including ESG and metrics

ESG due diligence best practices

- The conversation focused on comparing:

What is the role of the operating partner in driving ESG initiatives?

- Agenda setting: one participant noted that his firm focuses on putting ESG and diversity, equity and inclusion on the agenda of the boards of their portfolio companies in a largely unstructured way annually to
- Likewise, another participant noted that the most valuable aspect of ESG for an operating partner is the debrief after diligence with the CEO about how ESG played in the due diligence and should play in the operating improvement plan
- Integral to operating improvement plan
 - Cost out: Right sizing an carve out. Footprint reduction and energy efficiency. Include energy & GHG hot spot analysis in footprint reduction
 - Geographic expansion
 - Roll up: ESG best practices

Mapping out and engaging with all key stakeholders on ESG

- The group agreed that the ESG stakeholder are distributed across multiple functions at portfolio companies
- The group also suggested convening multiple functional groups at portfolio companies including consistently:
 - Facilities
 - Environmentally Health & Safety
 - Compliance
 - Investor Relations
 - Human Resources – human capital development and DEI
 - Leads of lines of business and geography
 - Communications
 - Legal

We ran out of time before turning to these two additional topics:

- How are ESG based KPIs and metrics being used?
- Private equity's ESG journey: what comes next?

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