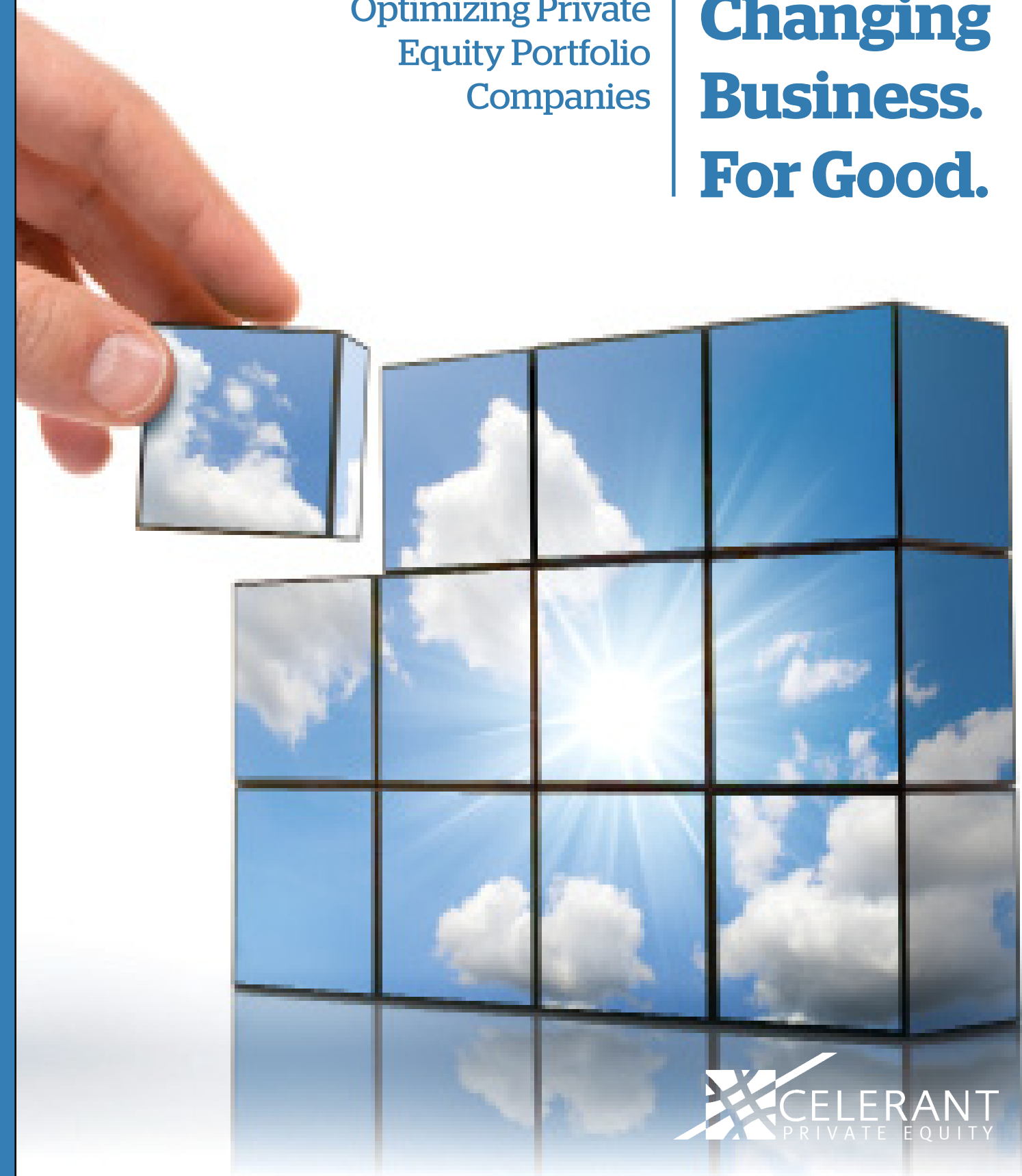


Four Tenets for
Optimizing Private
Equity Portfolio
Companies

**Changing
Business.
For Good.**



Global Headquarters

72 Lower Mortlake Road
Richmond, Surrey TW92JY
United Kingdom
+44 20 8338 5000

Private Equity Headquarters

435 Devon Park Drive
Wayne, PA 19087
United States
+1 781 674 0400

For more information on Celerant's Private Equity practice:
privateequity@celerantconsulting.com

celerantconsulting.com



In today's private equity market the pressure to perform is increasing as the multiples paid on additions to investment portfolios rise. Building value in a portfolio company, preparing a platform for growth and developing attractive exit strategy options still come down to basic principles: planning, flawless execution, and communications. These principles must be applied relentlessly to optimize value, beginning in the early stages of due diligence and continuing throughout the portfolio company ownership cycle. Acquiring firms or entities that do not focus immediately and consistently on opportunities for continuous improvement and implementing optimized processes are fighting against themselves. Status quo performance is sub-optimal and when the time comes to expand organically or structurally, pre-existing inefficiencies will become roadblocks for growth.

Optimizing the total value created from an acquisition or merger is paramount. The endgame, however, can only be achieved if the company's strategy is carefully laid out and understood by all parties. Acquisitions undertaken without clear direction create confusion and a rudderless work environment that can derail the best of plans and set the stage for a merger stunted by cultural clashes. As Robert F. Bruner, dean of the Darden Graduate School of Business at the University of Virginia notes in Chief Executive Magazine, "CEOs tend to think that integration merely consists of connecting the IT pipelines, getting the cash to flow in the right direction and consolidating the accounting systems, but that is just the start. Integration is about building a joint vision and strategy of the combined company, and creating a set of norms about how decisions will be reached."¹

When a portfolio company is shaped to demonstrate profitable growth and year over year returns not only is present value optimized, the exit strategy opportunities for Private Equity become more abundant and attractive. The foundations of these outcomes are built by adhering to four basic tenets for change.

Tenet #1: Change begins before the close

Value creation starts with a detailed understanding of the organization's structure, personnel, and areas of strength and improvement. The vision must be clear, and the action plan fully developed before control is sealed by the private equity team.

If aggressive preparations are not made, value can be lost from Day One. Buyers must approach the planning process by going beyond the typical CIM review and financial due diligence to get an inside look at future operations. They should visit company sites personally, assess conditions, and base conclusions on carefully gathered external data. The process must prepare them for the tough decisions ahead while laying the foundation for detailed operational assessments and action plans in the first 100 days of ownership.

With this process at their backs, teams can confidently send out a Day One communication that enlivens the staff, enrolls them in the vision, and ignites positive momentum. Participants benefit from clear and actionable pronouncements about objectives broken down into functional areas. Teams should feel supported by the full weight of the organization as they undertake change, whether that means a minor alteration to a department's IT system or a major overhaul of a production facility.

This thorough setting of the stage and preliminary communications need to be in play prior to the close, and acquirers, management teams, and external advisors must collaborate continuously to ensure they are moving in lockstep.

Tenet #2: Accelerate Value Creation

The first 100 Days are the window for new owners to exert authority and make changes that demonstrate confidence, enthusiasm, and alignment with the vision.

The planning and pronouncement process offers important guidance, but without immediate, decisive action it will be nearly impossible to enroll the organization. Those 100 days, then, are the critical timeframe in which assumed synergies must be proven while redundancies and operational inefficiencies are identified, evaluated and eliminated.

The urgency is justified. Too often, new portfolio ownership takes gradual hold of an organization, and as a result employees hold fast to their heritage, routines and behaviors. Hitting the accelerator on Day One helps avoid this pitfall.

When it comes to mergers, establishing a united front from the start is crucial. Otherwise, resistance to change - especially from a cultural perspective - can spell disaster. The industry is rife with examples.

Take what is now viewed as one of the most significant failures of corporate merger integration, the purchasing of AOL by Time Warner. In 2000, the \$360bn merger was positioned to change the landscape of communications and yet after 10 brief years, the two companies separated. The collapse of the merger is a direct result of the companies' failure to truly integrate their cultures and services.

Tenet #3: Change must be designed to last

Flawless execution is a daunting term, but it is a necessity as a new organization undertakes a transformation initiative. Execution must be performed with precision, and progress confirmed repeatedly with open communication, management controls, and monitoring that keeps tabs on the many balls in play.

Most importantly, the pursuit of flawless execution is not geared toward "not getting it wrong." It is instead an approach that allows teams to make corrections quickly and directly when things invariably do go awry. Organizations are built around the most unreliable of resources - people - and plans will inevitably be scrambled as they unfold. Missteps need to be anticipated and teams should be empowered to assess the situation and take action.

When the organization is moving in the right direction with the right processes in place, the work is not yet done. Implementation teams have an obligation to make their work endure; there is no room to leave employees with new roles and responsibilities with no idea how to sustain momentum.

Managers should be taught how to use the reporting and monitoring tools, how to analyze progress and be accountable for their and their teams' actions. With a personal stake and the enthusiasm that comes with truly owning their new roles, these key ambassadors will adopt the tools as part of the new culture and operations of an improved enterprise. Robust management systems and motivated people are the foundations of a performance culture, with continuous improvement built into the DNA of the new learning organization.

Tenet #4: Don't just follow the leaders - create a strong team

The most comprehensive planning, keen communications, and expert implementation will have little impact without the right leadership team at the helm.

The personality of the CEO and its team in particular have to be carefully considered; it is crucial to have those roles filled by people who can paint visions, communicate, and plan accordingly.

In less cautious times, a premium was placed on high profile individuals to headline large acquisitions, regardless of their personal fit with the company. Today, organizational targets are refined and more strategic. Specialty funds seek out acquisitions that fit a specific profile for geography, size, and the nature of business; this laser focus has spawned better awareness of industries, company-specific needs, and the tools necessary to get the job done.

In his book "Good to Great", Jim Collins defines the criteria for successful company leadership. "Level 5 Leaders" are not the charismatic and erratic Lee Iacocca's of this world, and not the driven but risk-taking managers such as Jeffrey Skilling at Enron. True leaders of change that deliver sustained value and consistent performance develop commitment to a shared vision for success and talent throughout an organization.

The greatest Level 5 leaders of our time are largely low profile. Darwin E Smith at Kimberley Clark, Bill Allen at Boeing, and William McKnight at 3M each managed the transformation of companies that have not only become leading global corporations, but have also delivered sustained value over decades. Private Equity firms must focus on the appointment of executives who will manage change, lead teams and make the strategic plan come to life. This has to be for the short, medium and long term.

As private equity firms source deals and develop growth strategies, value creation for each portfolio company comes down to ideas and execution. Extensive planning and training provides the confidence needed to get the job done and the insight to know what is likely to work before the deal closes.

Of course, after a year has passed and organizations reflect on their progress, the leading stakeholders are already moving towards next steps. For them, the refined organization they created should now stand as a foundation for further acquisitions, with a team that has been through significant change and knows how to create value. This battle-tested structure is the real victory; it is the most dynamic ingredient to generating fast, sustainable value and a platform for further growth.