KEYNOTE INTERVIEW

# Tailoring the value-creation playbook

*Adjusting value-creation plans to suit the needs of specific industries and deal types can help maximise the impact of operational improvements, say Montagu's Tim Cochrane and Claudia Paniker Rumeu*

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**Q Is the current macroeconomic environment impacting the value-creation playbook?**

**Tim Cochrane:** We are witnessing a period of ongoing inflationary pressure and some slowdown in economic activity, although GDP growth is probably more robust than we expected. As a firm, we invest in must-have businesses, primarily B2B, providing must-have products. That means we are not that exposed to raw material nor energy inflation; instead, it is wage cost increases that have the biggest impact on our portfolio.

In the last 18 months we have been focused on managing that inflationary pressure and working with portfolio companies to create product extensions that drive more value for clients and customers.

We have found our businesses have huge potential to increase their offering to customers and to monetise that value through price increases above inflation, so we have seen margin expansion across the portfolio.

In addition to addressing wage increases, we have been doing a lot of work around the talent agenda across the portfolio. That involves looking at how we ensure all companies are spending enough time thinking about employee satisfaction, addressing key employee needs and building more loyalty to reduce unwanted attrition. We also have a strong focus on attracting senior talent, and we continue to find people excited about the opportunity and wanting to work in our portfolio.

Alongside addressing inflation and talent, the other big lever we have been focused on is M&A.

**Q With add-ons such a dominant feature of the PE market today, what are the essential elements to successful integration?**

**Claudia Paniker Rumeu:** We are very focused on M&A, and clearly bolt-ons are becoming a dominant feature of value creation. We have seen a five-fold increase in add-on acquisitions undertaken by our portfolio companies over the past few years and this trend is accelerating.

In terms of integration, having a disciplined approach is key. We find it helpful to start that process early and articulate a clear value-creation plan that drives what needs to be integrated, when and how. Nothing is more important than people when it comes to getting integration right, which means bringing them on the journey and incentivising them correctly.

**TC:** The reduction in venture capital funding and the drop-off from some of the high valuation expectations that were around 18 months ago mean this is a ripe market for bolt-on M&A. People are more willing to accept conversations around valuations that make sense. Plus, the slowdown in the market for primary deals has increased appetite on both sides.

**Q How are GPs developing value-creation plans to suit specific deal types, such as carve-outs?**

**TC:** From our perspective, when it comes to value-creation plans, there are several important areas to work through. We start at onboarding, ensuring companies meet a standard 'Foundations for Good Governance', including in relation to ESG and financing requirements. Next, we turn to a light-touch assessment of the functions in the business, looking at, for example, whether HR systems are set up for the hiring required and whether the IT systems are where we want them to be for our growth plans.

**Q What makes for an effective integration plan between different industry sectors or businesses?**

**CPR:** Where you need to be on an integration spectrum varies greatly by industry and subsector. As an example, our portfolio company Galileo, a leading global higher education business, tends to keep its schools independent to retain their academic identity but provide core central support, rather than going down a full integration route.

More generally, we typically integrate tuck-in or scale deals more fully and at pace to secure the value. Whereas for deals where the rationale is to acquire strategic adjacencies – for example, where it is often critical to retain intellectual capital – we may take a slower and more hybrid approach.

**TC:** We want to extract as much synergy as possible, particularly in scale deals within smaller industries or product markets, and a lot of that will involve cost take-out and integration in areas such as sales force. In a scope deal, meanwhile, there may be some back-office synergies, but typically you integrate less because there are different sales forces.

With fast-growing founder-led businesses, the question is how you create the right incentives for the founder. In roll-ups of funeral chains or eye clinics, for example, we find that having the founders on board as shareholders rather than employees is important. It is a blend of addressing cost synergies and maintaining the excitement and entrepreneurship of the key individuals, which may mean less integration to give those founders all the opportunity you can to deliver their ambitious growth plans. You can structure the deal with meaningful earn-outs so founders can benefit and in return we integrate less and hold them more accountable.

Then we get to strategy and commercial diagnostics. This leads to what we call the full potential plan, where we seek to understand the opportunities and size of the growth levers available to us, and align management and the board around the plan. The next step is setting KPIs for the first four or five years.

We expect to do all these things for most deals, but the order and duration of each step will vary. More than half the deals we do are carve-outs, typically coming out of large multinational companies with management that has never run a stand-alone, leveraged business before. There, we need to spend more time on how the business is going to work as a standalone entity, addressing gaps in IT, HR and elsewhere.

On the other hand, if we invest in a secondary deal, which we do less often, we can usually onboard the business faster because it has already spent a few years under private equity ownership. If we know the business is fit for purpose, there is a lighter touch on commercial modelling and we may move to the strategy stage more quickly.

## Q What are LPs expecting managers to prioritise in their operating teams today?

**TC:** Fundamentally, LPs want to hear that the decisions we have made around setting up our operating partner team are consistent with our firm's strategy.

The sorts of deals you do and the levers you use to create value will impact how you structure your operating team. We invest in must-have businesses in the mid-market across Europe and the US and, as mentioned, more than half of the deals we do are carve-outs from multinationals. This means the operating partner team we need has several requirements.

First, we have a strong carve-out capability because we need someone who can sit in on those early conversations with the head of M&A at the seller and the business unit head and reassure them that we can deliver. You need to build up a bench of experts to do that. Having undertaken 28 carve-outs since 2002, Montagu has this experience.

Second, we have found that what the CEO and his or her team really value is a set of generalist or specialist partners that can come and act as mentors to them across the key value levers. They don't necessarily want large groups of consultants arriving because typically they cannot handle that level of support and they do not have the data required to keep those people busy.

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>
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We have a small group of partners that can work with the CEO across a broad range of issues, typically former CEOs or general managers that have done it before. Plus, we have a range of specialist partners who can go in and spend time with the relevant department heads, whether that be M&A, marketing, finance, or technology, to help drive forward those agendas. LPs are reassured by alignment across how we originate, what deals we do and how we deliver value.

**CPR:** LPs recognise that M&A is an attractive value lever and see the opportunity in the current environment. The majority of our portfolio companies operate in markets with high potential for M&A, but they may not have done many deals or have a full set of M&A capabilities. Our ability to bring a rigorous and repeatable model to sourcing, execution and integration to accelerate M&A is appreciated.

## Q What will value-creation teams be focused on going into 2024 and beyond?

**TC:** Some of the things that are more important now than they were 18 months ago relate to helping companies through the economic environment. How do you think about the increased cybersecurity risk across the portfolio? How are you thinking about maximising value opportunities around ESG, and what support are you giving to companies to pursue their priorities there? How do you think about emerging opportunities around artificial intelligence?

We have a strong team in-house that focuses on ESG, as do most of our peers, and that team can help companies work through a range of governance, environmental and social issues. In our case, that is mainly carbon reduction targets, diversity and inclusion, and setting up the right governance in terms of structures, committees and policies.

Another big focus is going to be AI and cybersecurity, where there is a debate about the right way to provide that support to portfolio companies. The tension there is that having someone in-house provides benefits, but the market is moving so quickly that there are challenges around staying current. We have a range of third-party firms that we work with on a regular basis on this, as well as some in-house resource.

The fundamentals will remain the same for us, which means the biggest value levers we talk to CEOs about will continue to be creating commercial excellence, extracting better pricing, expanding into new geographies, particularly in the US, through both organic growth and M&A. That will also include exploring new products, embracing technology and data to improve processes and provide a better experience for customers, supporting talent in the business, and leveraging ESG to create stronger sustainable businesses. ■

Tim Cochrane is a partner and head of the Full Potential Partners team at Montagu and Claudia Paniker Rumeu is a partner at Montagu FPP