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## How high-growth company CEOs tap the power of private equity

Private equity (PE) has become a resource for a growing number of founder-led businesses seeking stronger, more sustainable growth. Today, the private equity investing model has become an integral part of the economy – for example; there are nearly 8,000 US PE-owned companies, which contrasts with less than 5,000 public companies. With a track record of outperformance, PE continues to attract more and more capital from a broadening array of investors. Globally and across strategies, PE assets under management (AUM) stands at over US\$5 trillion, according to Preqin.

### Why consider private equity?

Partnering with a PE group is especially attractive for founders of lower and middle market companies that aim for transformational, not incremental growth. As minority or majority investors, GPs invest alongside their portfolio company management teams to create a real culture of partnership that is necessary to drive collaboration and execution on an agreed upon growth plan.

A growing number of private equity groups specialize in taking young, growing companies to the next level and doing so quickly – over a three- to six-year investment window. As active and engaged investors, they bring:

- ▶ Not only capital, but specialized industry expertise and experience
- ▶ Generally, a large network of specialists, including operating partners who are often ex-CEOs

Management teams collaborating with PE firms gain access to value-add capabilities across functional areas such as:

- ▶ Business development
- ▶ M&A
- ▶ Product road-mapping
- ▶ IT
- ▶ Recruiting to drive organic and inorganic growth

Founder-operators who work with PE firms especially appreciate the ability of their PE partners to bring a fresh mindset to evaluating their companies and its growth opportunities. “It is important to have a partner that has a broader view of what is possible for your company, and it really expands the opportunity,” notes Jeff Eastman, CEO of Alchemy Systems, whose firm was angel-backed and then acquired by a PE company. As serial investors of growth companies, PE firms look at thousands of firms every year to become highly experienced builders of businesses.

### PE as a source of growth capital globally

#### Typical company target size

US\$5m–\$200m in revenue (lower and middle market).

#### Hands-on owners

According to the 2019 EY *Global Private Equity Divestment Study*, over 80% of GPs report they interact, at minimum, monthly with portfolio companies to drive value.

#### Active buyers

PE deals represented nearly 20% of global deal values in 2018, according to Dealogic. PE deals represented 15% of US deal values in 2018.

#### Assets under management of PE groups

US\$3.3 trillion globally including US\$1.8 trillion for US-based funds.

#### Total value of US PE deals

Value rose 11% to US\$249b as of 30 June 2019, from the same period a year earlier.

#### Dry powder

US\$758 billion in uninvested capital for PE worldwide with the US accounting for \$459 billion.

#### A seller's market

There are more than 7,000 GPs globally, with over 5,000 in the US according to PEI.

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One of the things I take most pride in is that we have made about 20 millionaires over that course of Alchemy’s journey.

Jeff Eastman  
CEO of Alchemy Systems

## The importance of finding the right fit

According to seasoned PE-backed CEOs, one of the most critical criteria to look for in a prospective PE partner is alignment of vision, investment thesis, and values to keep everyone rowing in the same direction. This alignment is also critical for stimulating productive collaboration where all the partners are passionate about building the business and can communicate freely and frankly. The right PE partner can also help founders achieve their personal goal - whether it's a fair financial return, maintaining the legacy of the business, or looking after key stakeholders.

As many PE groups are highly engaged, hands-on investors, they tend to interact frequently with the management team. Consequently, "it is really important that there is a personal fit" between the partners, emphasized by John Fraher, CEO of Adare Pharmaceuticals who has worked three times with PE. Ultimately, owner-operators want to work with those individuals whose judgments they can trust, who they are able to talk with openly and transparently, and who they are able to work with through the inevitable rough patches.

Ultimately, finding the right PE partner involves:

- ▶ In-depth due diligence, similar to what GPs practice in evaluating their prospective portfolio company targets
- ▶ Learning how different PE groups think about debt and equity, which may be informative of their investment style and culture
- ▶ Considering either a negotiated sale or a more formal auction process to broaden the pool of potential PEs

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## Six steps to help you prepare for private equity

1. Start the process early
  2. Get help, specifically financial and legal expertise
  3. Identify your objectives for your company and yourself
  4. Decide what type of sales process you need - formal auction or informal negotiated sale?
  5. Interview, reference-check, and socialize with PE groups
  6. Make sure the private equity firm you move forward with is aligned with your company's vision, investment thesis, and values
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## Summary

CEOs of PE portfolio companies realize that the model works, but that it may not be for everyone. Having benefited personally, financially, and professionally, a growing number of these CEOs have gone on to become serial CEOs and operating partners for PE groups. This is a testament of PE's strong partnership and business-building capacity.

## Lessons and challenges

CEOs of PE portfolio companies who have built successful partnerships and achieved accelerated growth are in agreement that one of the most important lessons is to be clear upfront about your goals and vision for the company.

Early on, one of the biggest challenges founders face is the time commitment in running a full-blown sales process while managing the business. Having a CEO sit through management presentations and due diligence meetings over a four- to six-month period can be highly distracting and potentially paralyze a firm's operations. Thus, it becomes imperative to prepare early: decide what your goals are, get the right team behind you, and map out the most efficient process.

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**The most important thing is to start with what is your vision, what are you trying to accomplish, and then look for partners whose vision is aligned with yours.**

**Joe Fluet**  
CEO of MAG Aerospace

When a PE partner comes on board, founders may face a challenging transition as they shift from their role as owner-operator to co-owner, CEO. These roles tend to involve different mindsets, skillsets, and responsibilities. A founder who built his or her business on risk-taking may now have an owner that is more risk-averse and will place execution responsibility squarely on the CEO's shoulders. Navigating these management team-GP dynamics highlights the importance of transparent and candid communications and basing the partnership on mutual trust.

A common regret CEOs have with their relationship with PE firms is not pushing hard enough to get more capital upfront and putting it to work early. And PE investors may agree that this is an opportunity missed. Besides boosting confidence in the management team, making strategic investments earlier may be more likely to lead to growth before the PE holding period ends. Entrepreneurs who have boot-strapped their operations and are worried about dilution, naturally may be hesitant to request capital. This point also highlights the importance in keeping aware of the exit window. In the later stages of a portfolio company's life a PE firm will be focused more on executing on exit strategies and less on putting more money to work.

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