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Insights

CEOs' experiences of a primary buyout

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Skillcapital has strong relationships with leading Private Equity (PE) investors who are interested in what key factors management teams consider when choosing which investor to work with. From the opposite perspective, management teams are interested in what it is really like to experience an MBO.

To provide some insight on this topic, Skillcapital recently hosted a panel discussion with three PE CEOs to discuss their experiences of leading a primary buyout. Our panel consisted of:

- A current chairman who, as a CEO, led a large-cap PE-backed MBO
- A CEO who led an MBO with his current investor, a UK mid-market PE fund
- A current CEO who led an MBO, and was part of another PE deal which he took through to IPO

Here we share some of their insights into the buyout process, focusing on their considerations when selecting a new investor.

CEOs look to the personalities and characteristics of individual investors when choosing a financial sponsor, rather than choosing a PE firm or brand name. In particular, they value an individual's ability to **"deliver the firm"** – to bring the combined expertise, network and resources of a PE investor to bear – toward helping a business to grow.

What are the main factors in choosing which private equity fund to work with?

The CEOs noted that, most importantly, it's **the current owners that choose a new investor** – be they the incumbent CEO, another private owner, or a large corporate divesting part of its business. This may purely come down to the price an investor is willing to pay, or the structure of the deal.

Beyond this, the **chemistry between the CEO and the lead investor** is paramount. Given the need for a close working relationship between the CEO and PE investor – which is needed throughout the lifetime of a deal – the importance of **mutual trust, a shared approach and open communication** cannot be overstated.

Put simply, **"if the chemistry isn't right, you won't deliver on the deal."** One CEO commented: "there are definitely periods when, as a CEO, you are uncomfortable. Having a trusted relationship with your investor is key".

Shared approaches can be as idiosyncratic as the relationship between the CEO and their investor. One of the CEOs, working in a highly data-driven business, preferred one particular investor whose analytical and numbers driven style chimed with his own. In short, they spoke the same language.

"...first and foremost, it's the current owners that choose a new investor – be it the CEO themselves, another private owner, or a large corporate divesting part of its business".

What qualities do you look for in an investor?

"You need a partner who can deliver the firm". Regardless of the size of the transaction, what is key is someone who "has responsibility. Decisions get taken and things just get done". One of our CEOs was dealing with a large carve out from a corporate. He said that having a senior investment partner meant that "it turned into a more straight-forward process than he had expected".

Another key quality was the ability to listen: one of our panellists said that the PE firm he chose was the one who was best able to articulate the business and their strategy.

Our CEOs agreed that frustrations can quickly escalate when dealing with an investor who either cannot deliver, or is one of many in a hierarchy. As such, the "layers" of professionals within the fund, and the **quality and depth of the entire team** is an important consideration when selecting a fund to work with.

Another key quality was the ability to listen: one of our panellists said that the firm he chose was the one who was best able to articulate the business and their strategy. "They were also very honest in saying the main thing they would bring to the table was money". However the CEO had assurances that "the investor would stay involved with the business throughout the whole process".

In our experience it important that the individuals who will be managing the investment going forwards are also part of the deal team. If the lead investor will continue being the main point of contact then this is ideal, but understandably not always possible. Any changes to individuals in the fund overseeing the business throughout the time of the investment should ideally be done gradually, such that there is continuity of trust and empathy.

Who advises you on process and looks out for your interests?

This can vary according to the size of the deal. Two of our panellists were CEOs of large cap investee companies. They were in agreement that there was a need for advisors to management when the transaction was highly complex. One of our CEOs who came from a large corporate commented: "it can be a complete mystery regarding terminology. A huge amount of hand-holding is needed".

However, **the more experienced the CEO, the more confident they became in their own judgement.** One panellist said "when you do it again, you have more experience, you have a bigger network, you can reference more and you have more ability to decide what motivates you and what your drivers are".

Do you know which private equity firms to speak to before taking any formal advice?

Again, a question of the CEO's experience. "The first time I did the process we met 20+ funds. We knew who we did and didn't think we could work with. Whether or not you are proactive or just have an idea, **you really need to think about the type of investor, their experience and then their reputation. As CEOs we talk a lot to each other,** and I found this valuable especially in discussing fund reputation".

On the same note, another panellist discussed how the response they received from the NDA showed a lot about the firm's approach: "the response we had to our NDA was very interesting...some signed straight way, they got it and **understood. Some refused point blank. One fund sent us 15 pages of amendments to our three page document. We found this exercise very telling about what they would be like to work with".**

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Another panellist said "you don't pick firms, you pick people. I pick the person I will be working with first, then I look at the firm and their culture. Ultimately we have to judge the individual and analyse if we feel we can trust them".

Is the buyout M&A process your most challenging experience to date?

There was agreement among our panel that the buyout was less challenging than they had expected and that **the CEO's key role was to keep focused on the business during the buyout process.** When asked if the buyout was their most challenging experience to date, one panellist commented "Not for me. You are making big decisions. It's quite stressful, but that comes with the job. **I actually enjoyed the process and it gave me a buzz**". Another said "Not my most challenging experience, no. However there are a lot of emotions involved and you have to keep on top of those or else it can become wearing".

Conclusions

- The CEO can have varying levels of influence in choosing an investment partner, however, they are central to the process
- The CEO has to achieve a fine balance between managing the buyout process and managing the business
- When looking for an investment partner, a crucial factor for CEOs is their personal "fit" with the lead investor
- CEOs also cite the PE firms reputation and experience, although this is cited as less important than their personal chemistry with the lead investor
- CEOs also have their own peer network, and those that have experienced and M&A process do talk to one another to share experiences and offer advice. Often this advice is taken prior to the appointment of advisors to management
- Finally, it is important that the investment partner is an individual who is able to "deliver the firm" and make good on their guarantees and promises.

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Our thanks to the CEOs who provided content for this research.

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