

## Meeting Takeaways

June 19, 2019

### Private Equity Company Board Strategies for Managing Across Business Cycles



**Panelist**

**James Bland**  
Managing Director,  
Akoya Capital



**Panelist**

**Scott J. Gilbertson**  
Principal,  
Pfungsten Partners



**Panelist**

**William Watkins**  
Managing Director,  
Harris Williams



**Moderator**

**Arthur E. Mertes, Esq.**  
Partner,  
Tucker Ellis LLP

A large turnout of PDA members and guests attended the June 19th program featuring a panel of private equity, investment banking, and corporate finance experts, facilitated by Arthur Mertes, Partner, of Tucker Ellis LLP, discussing the opportunities and challenges facing private equity company boards through the ups and downs of business cycles. Panelists included: Bill Watkins, Managing Director, Harris Williams; Scott Gilbertson, Principal, Pfungsten Partners; and Jim Bland, Managing Director, Akoya Capital. The event was sponsored by Tucker Ellis and PNC Bank.

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The panel covered topics ranging from the opportunities in the current economic environment, managing in a downturn, the role and value of boards for private companies during better and tougher economic climates, as well as how Private Equity firms select and work with private directors for their portfolio companies.

## Opportunities in Current Economic Environment

While a poll of the audience indicated that more than half of the audience expected a recession in the 2020-2021 timeframe, the panel was more sanguine. Consumers continue to drive a sound economy. Election year economies tend to be strong.

Though trade wars and tariffs have raised concerns, mid-high margin companies will be minimally impacted. Many of the companies affected have been demanding action against China to level the playing field, so tend to be supportive of the effort, even if negatively impacted by specific tactics – i.e., “we voted for the guy to do something and he’s doing it.”

On the M&A side, several factors continue to propel activity. The level of capital to invest remains high. Lenders are anxious to lend. With historically high multiples, valuations are good and terms and conditions are favorable, making it a good time to sell, increasing acquisition opportunities. That said, talk of an impending recession has made some investors more cautious, especially toward more cyclical businesses like consumer services.

## Managing During a Downturn

First step is to ensure that, while times are good, capital structures are established to ensure companies can weather the storm. Second is to have a solid team in place. With economic tailwinds, management weaknesses can be glossed over. Other actions include identifying potential to diversify by region or sector and understanding core strengths and opportunities to apply them in areas where other companies are faltering.

## When to Partner with Private Equity

The reason to partner with PE is to get value out of the company, either through cash from the initial investment, a short-term sale or longer-term growth and value creation. Regarding the latter, PE can help a company “grow up” faster. Ultimately, PE firms that buy, hold, and sell are not as successful as those who invest with the purpose to make bigger and better. The fundamental steps a PE firm will take include:

- Ensuring the right capital structure is in place
- Defining/clarifying the strategic direction and value proposition
- Making sure a strong management team is in place. In addition, PE is going to have better access to outside talent – both for potential management team members and for advisors, whether experts in the sector or investment bankers who know the industry well.
- Being data driven and demanding accountability, using scorecards to clearly set and manage against key performance drivers.

In addition, PE is more likely to make the capital expenditures that individual owners are more likely to delay due to being cash poor or risk averse, kicking the can down the road to the point where they can’t invest. As an example, one solution to tight labor market is automation, which requires cap ex – put off too long and the hole gets too deep to dig out of.

## Role of the Board at Private Companies

PE can also encourage/require a formal board with independent directors to deliver these benefits:

- Coaching and mentoring the CEO
- Sector expertise not bound by the blinders of the company’s culture, history, and biases
- Perspectives from other industries
- Networks with outside talent, either as potential managers or advisors

Good board candidates will ideally have strong industry expertise, skills in coaching vs. directing, and prior board experience. A final note is that the establishment of a board needn’t be dependent on size – one of its key payoffs is to help smaller companies grow bigger more quickly.

## Key to Success: Managing Human Capital

One of the biggest challenges is finding the right people for the right situations. Key pieces of advice:

- Post-acquisition, retaining good people is critical. In addition to setting up lines of communication and including in go-forward planning, it’s important to give them skin in the game in the form of equity, shadow options, etc.
- Essential to act quickly if you don’t have the right person in the job. Once you know, lingering is like letting a tumor grow within the organization.
- As part of the scorecard, use human capital metrics – e.g., voluntary turnover, employee engagement assessments
- Develop informal sound board within the company to keep finger on pulse around engagement, morale, and issues.