KPMG

Making it count

How PEs / VCs in India manage their portfolio investments

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Foreword

Investor confidence in India continues to remain high. With the Indian economy expected to emerge as the third largest by 2030, investors have earmarked significant capital to actively participate in the India growth story, driven primarily by the sizable market, inherent cost advantage and young talent pool.

Especially in the last 5 years, investors have made multi-billion dollar investments across the growth lifecycle and sectors, with consumer goods, financial services and e-commerce leading the pack. Whilst competing for an asset and successfully concluding a deal is half the battle won, the real challenge is to maximize return on investments, within the stipulated investment horizon. This game has been mastered by investors who bring in deep sector experience and drive strategic initiatives across the portfolio right from the word go. Our analysis of select 300 transactions between CY16 and 20 indicate that returns on private investments have out-performed public markets, across sectors, underpinning the importance of investor led intervention in helping the company enhance its valuation, whilst navigating critical challenges or competitive pressures.

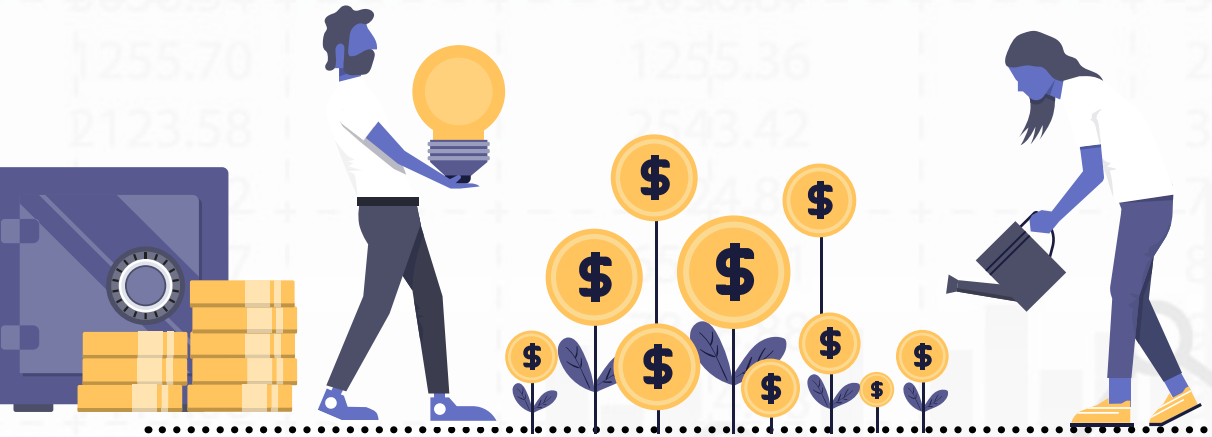
Whilst successful investments that add value to the portfolio, help PEs and VCs differentiate themselves and raise future capital, lack of alignment with founder promoters, management or forced value additions, can be counterproductive and erode investor's brand equity.

In this "Making it count" publication, we have attempted to identify the common themes followed by investors in India to protect and enhance value of their portfolio companies.

We have delved deep and analysed Indian case studies to analyze the key interventions made by the fund houses right from signing off on an investment until its exit.

The 'Value protection' philosophy underlines the importance of plugging leakages identified during the diligence phase, while effectively taking control of the investment, emphasising on the following core areas:

- Taking control on Day 1 – ensuring business as usual post investment
- Identifying and retaining key talent



- Developing a robust finance function – to ensure availability of reliable data and key decision support
- Enhancing the enterprise risk framework to detect, prevent and mitigate risks
- Being cyber secure and having a robust business continuity plan in place.

On the other hand, returns on investment are driven by clear vision and 'Value enhancement' measures such as:

- Streamlining the operating model – Rationalising non-core functions and simplifying processes to optimise costs and free up capital
- Enabling technology as a differentiator – Digitizing the operating processes & customer experience to enhance the company's competitiveness
- Investing in human capital – Upskilling and importing talent to setup the organization for success
- Revamping the Go-to-market strategy – Optimizing the product/ service offerings
- Integrating strategy and business planning – to help improve operational efficiency and provide a seamless experience to customers
- Supercharging business with data and analytics – To help identify levers to unlock and enhance value.

Whilst there is no single play-book for an investor to follow, covering all bases and proactively driving transformation, without antagonizing key stakeholders if more often than not, a recipe for success.

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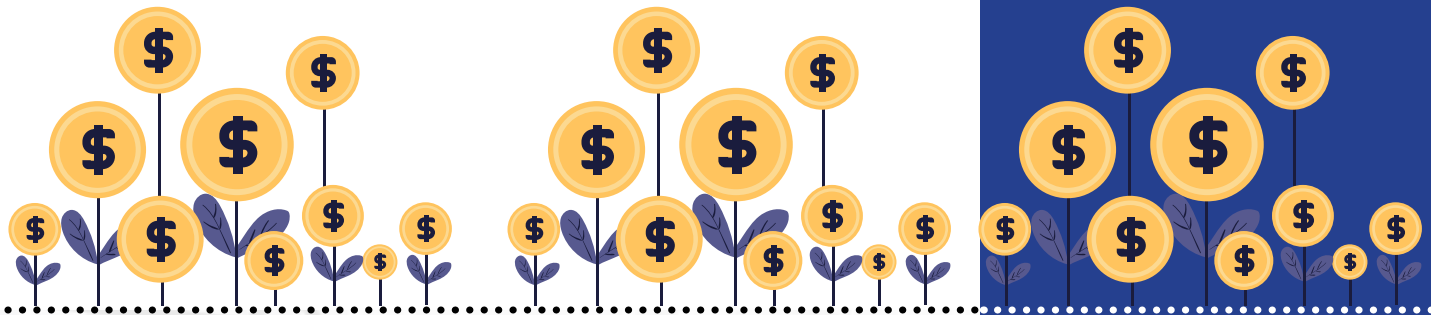


Investing in India

Traditional investment management approaches are no longer adequate to manage the unprecedented market volatility and associated risks, especially in a post-COVID-19 world.

In current market conditions,

every PE investment is a tight rope walk.

India remains an attractive hunting ground for PEs and VCs, with aggregate annual deal values doubling over the past five years

With the global inventory of investable capital expanding to record highs of USD1.2 trillion in CY2018 and given the lackluster growth in the developed markets, investors have earmarked a significant portion of this capital for investment in emerging economies. As per World bank data[1], India and China continue to lead the EM pack along with Egypt, Malaysia and Philippines. In the last decade, India has attracted significant inflow of private capital, across sectors and stages in the growth cycle.

KPMG in India has analyzed PE/VC investments from **CY15 to CY20** covering **c.1900** transactions and observed that:

- Aggregate annual deal value has doubled between CY2015 and CY2019*
- Annual deal count has increased by 60% between CY2016 and CY2019*, partially attributable to attractive valuations of Indian companies and better economic performance of India relative to their EM peers.
- Information Technology (IT) and Consumer Markets (including e-commerce) (CM) and Financial Services (FS) accounted for c.80% of all investments by volume.
- The largest PE investment in CY2020, is an aggregate investment of c.USD21.5 billion and counting, by over 14 fund houses and 3 corporates for c.33% stake in one of the largest telecom companies with extensive digital and retail adjacencies

KPMG in India has also analysed **500 exits**[2] by PE / VC funds between **CY15 to CY20,** and observed that:

- The median holding period of investment has increased from **c. 3.1 years in CY2015 to c. 6.2 years in CY2019, c.100%** increase partially attributable to a **maturing market.** However, to some extent, the increase is also attributable to a lower degree of business confidence arising from macro-economic challenges.
- **CY2019 saw 133 exits, less than half the exits in CY2016.** Analysis of past trends shows that the issue is more cyclical than structural. While some investors are delaying exit plans for stronger market conditions, others are shifting gears from public to private markets for exits.
- Financial services registered multiple large exits in CY2019. Interestingly, the top ten exits in CY 2019 contributed to c. 61% of the total deal exit value[3].

KPMG in India has further analysed a subset of c. 300 exits, which showed that **annualised returns on capital deployed through PE has far exceeded the capital markets returns across sectors.** Barring telecom and utilities, all other exits have **generated median annualised IRR in excess of 29 per cent over the holding period.**

1. World Bank Data as of Dec2020
2. KPMG in India analysis on 500 exit transactions involving c.350 companies with information available in public domain
3. KPMG analysis of top 133 exits in CY2019 with information available in public domain

*CY2020 data has been excluded for trend analyses due to impact of Covid19

Figure 1: PE Investments, by sector, by value, between CY15 – CY20[4]

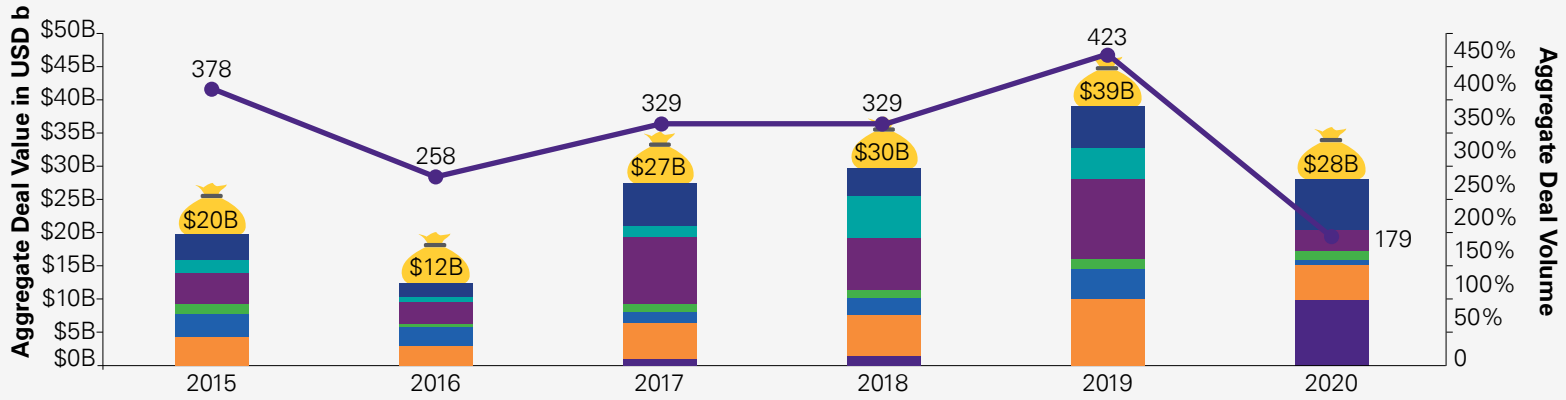
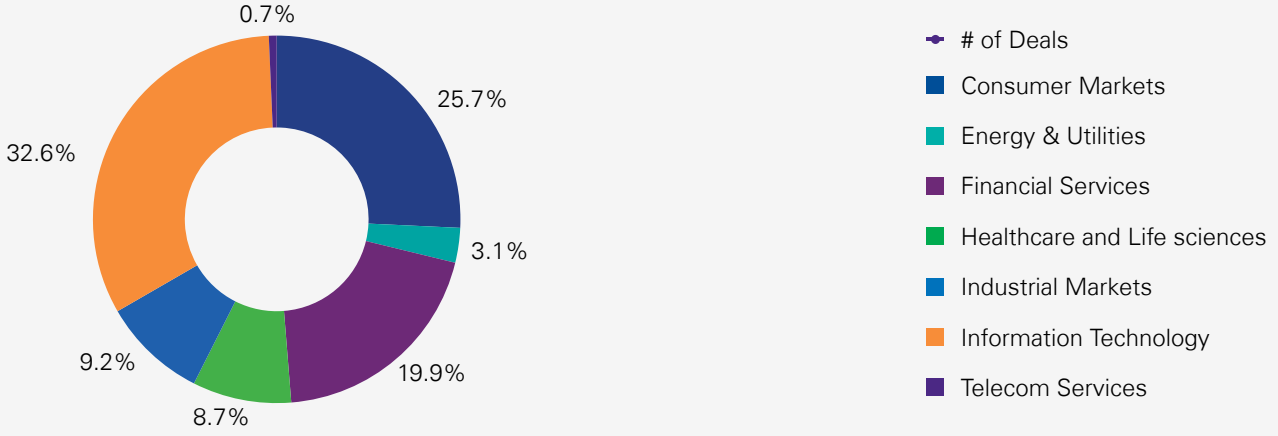
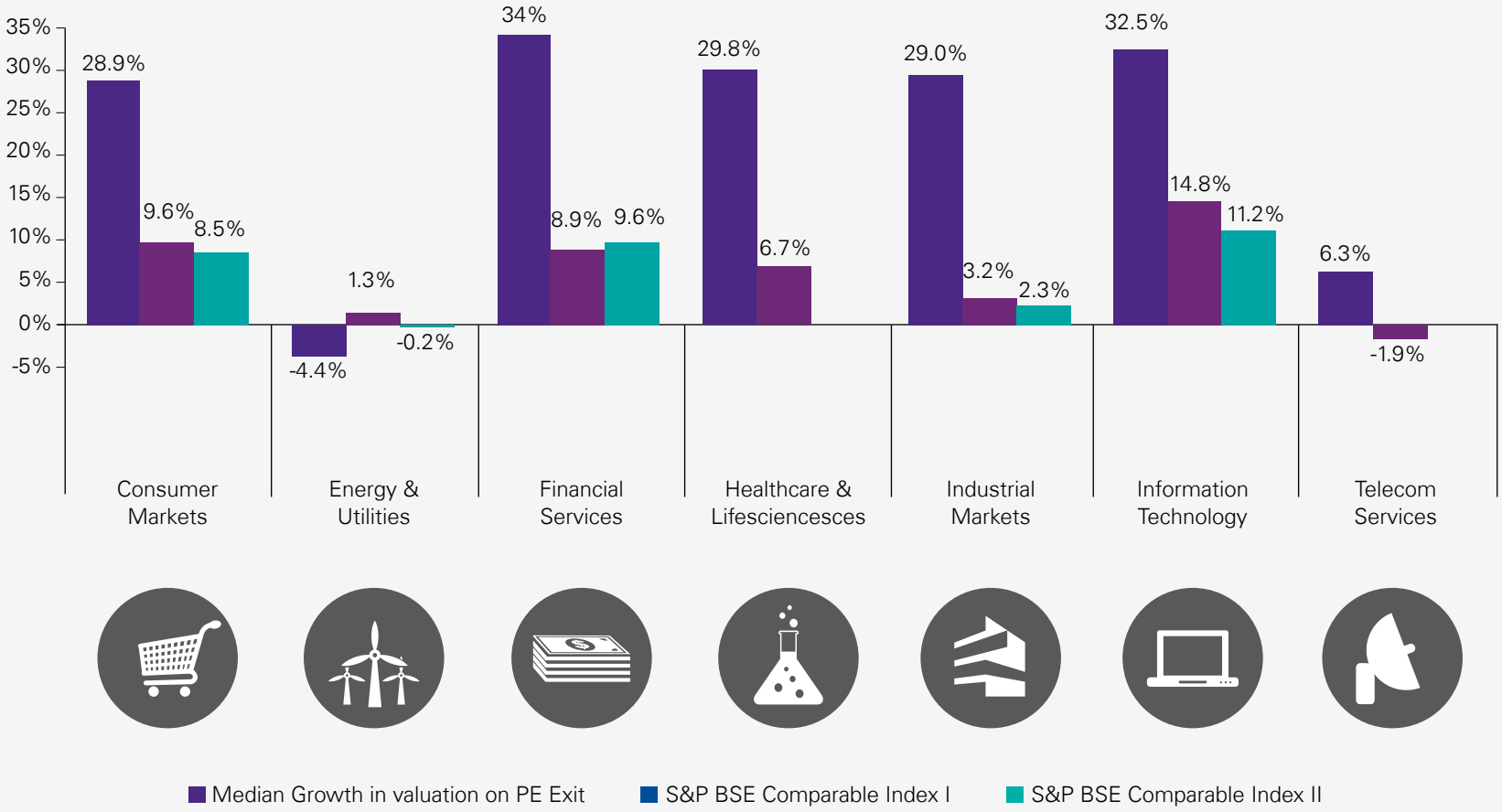


Figure 2: PE Investments, by sector, by volume, between CY15 – CY20[4]



4. VCC Edge ; KPMG in India analysis of 1900 PE and associated investments in c.1,000 companies between CY2015 –CY2020
* While CY20 data has been analysed, the same has been selectively used for drawing inferences and generating insights, due to aberrations on account of COVID19

Figure 3: Annualised Median returns (IRR) of PE Exits vs. Sectoral Indices (CAGR)[6], for subset of c. 300 exits between CY15 – CY20[5]

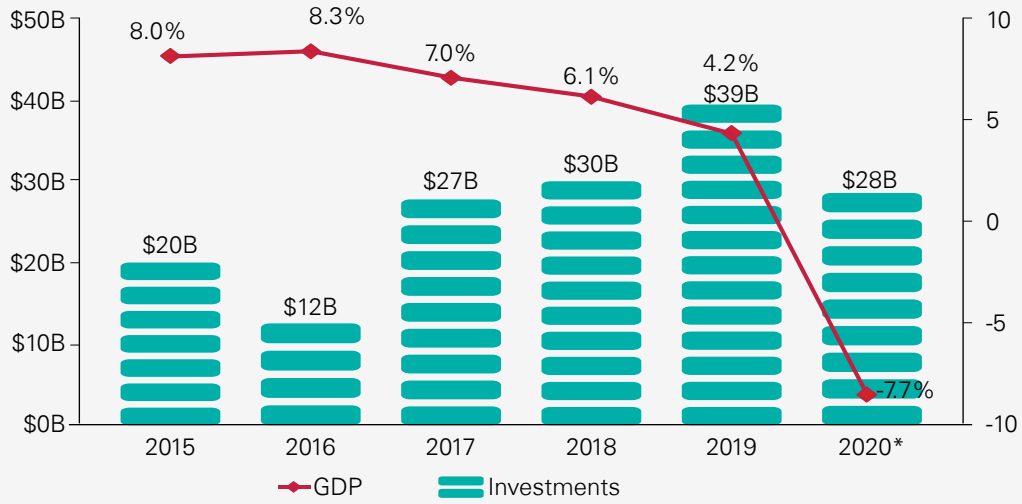


5. Data from VCC Edge, S&P as of 31st December 2020. KPMG in India analysis of c. 300 exit deals by value; (Returns computed based on growth in Enterprise Value across the holding period.)
6. Performance of sectoral indices as on 31 DEC 2020

Two-third of PE investments in India are in mature stage companies, with an increasing preference for buy-out/controlling stake transactions

Despite macroeconomic headwinds, PE/VC investments in India have steadily grown, with funds continuing to actively scout for opportunities across the growth cycle of companies. (Figure 4)

Figure 4 : PE Investment in India vs. GDP[7]



Early stage investments are a leap of faith, considering the absence of established track record and benchmarks

Startup businesses in the early stages are characterised by steep growth curves that generate high returns for the investor. However, these businesses often lack the resources or the professional expertise or the operational flexibility to sustainably scale up their businesses.

VCs step in to support these startups with growth capital, technical expertise, market insights and strategic guidance. This enables them to navigate through volatile and dynamic market conditions.

Of the c.1900 transactions analysed by KPMG in India, 850+ deals were in early stage companies, wherein investors committed c. USD 44billion between CY15 to CY20[8].

7. Source: VCCEdge; 2020 estimates for India's GDP from NSO, Government of India
8. KPMG in India analysis basis 1900 investments by deal-type across CY2015 – CY2020

Investments in mature companies are mostly strategic, with an intent to enhance overall value, leveraging the existing setup[8]

Mature stage investments are often strategic in nature, with the intent to ramp up revenue, rationalise cost structure, strengthen value perception and enhance enterprise valuation, prior to exit.

These investments can be classified into a) financial investments in companies in need of growth capital, or, b) acquisition of controlling stake in companies for a bolt-on or platform play operations.

When PEs pick up financial stakes in mature entities, they may not have enough headroom to bring about transformative changes. However, this does not deter them from sharing best practices and experience with supporting the investee's management.

PEs, acting through their portfolio companies, also look for bolt-on acquisitions to reap combinational and transformational synergies on integration. In mature investees, PEs typically focus on expanding geographic footprint, enhancing asset capacity utilizations, new product developments and refreshing go-to-market strategies, among others. Mature stage companies attracted c. USD 108 billion across 1,000+ deals in the last 6 years[8].

Investing in special situation revolves around interventions to stem further decline and turnaround the asset or finding a strategic fit.

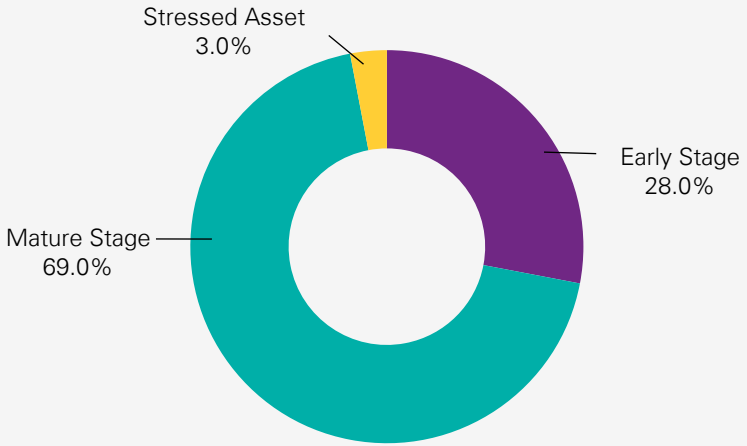
Globally, stressed assets are on the rise due to market uncertainties and demand supply mismatches. Despite sound business models and operations, promising entities become stressed for a variety of reasons that includes policy uncertainty, financial leverage, hyper competition and technological disruptions.

Investing in special situations requires a decisive strategy to turnaround the asset, with an immediate focus on value protection, followed by mid to long-term focus on value enhancement, keeping the promoters involved, where applicable, for seamless transition.

Analysis indicates that c. USD 5 billion of capital was pumped in stressed assets in the last 6 years[8], across real estate, infrastructure, BFSI and industrials.

Typically, PEs look for assets at attractive valuations to infuse cash or settle debts, plug value leakages and stabilise operations.

Figure 5: PE Investments, by sector, by value, between CY15-CY20[8]



8. KPMG in India analysis basis 1900 investments by deal-type across CY2015 – CY2020

Value protection

Given the pace and complexity of deal making, coupled with the shorter due-diligence timeframes, investors at times tend to deprioritise transition planning and value protection,

which directly impacts the ability to realise value post deal.

Though growth remains the long term ambition, PEs must seek to protect value immediately after investment

Often pre-deal interactions and information exchanges tend to be controlled and limited due to promoter apprehensions of sharing sensitive data, resulting in partial visibility. Ground realities of the business, on taking control could be remarkably different.

Therefore, private equities must prioritise transition planning and focus on protecting value immediately post taking control of the investment.

Whilst the need to take control is dependent on the stake purchased and other deal contours, a PE has to invest time in understanding operations and prioritise initiatives in a buy out scenario.

Effective Transition Management

An effective transition management office (TMO) brings all the key focus areas and activities together and helps PEs identify patterns and take swift action to realign the entity on its intended growth path, thereby preventing value leakages and setting the stage for value realisation.

Further, in our experience, deals have a limited time window to realise value, post which organisational inertia sets in and realisation of benefits becomes exponentially harder, if not impossible to realise.

Therefore, it is important to complete taking control and protecting value in a time bound manner.

Figure 6 : Deal transition timeline

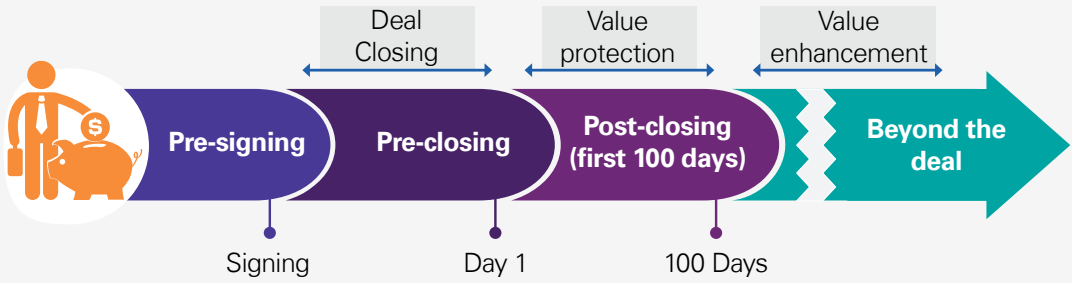
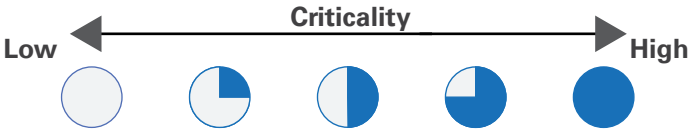


Table 1: Value protection focus areas and criticality by deal type

Economy	Financial Investment	Buyout
Deal closing and taking control of operations		
Retaining talent, reorganising reporting lines - avoid business disruptions		
Secure financial position and improve reliability of financial information		
Enterprise level framework to identify and address risks		
Enhance cyber security and protect data		
Business continuity and disaster recovery planning		



Value protection

Taking over the reins
Ensure seamless transition and target quick wins

Regardless of the nature of investment, a 100-day plan lays down the roadmap for achieving a prioritised set of post investment objectives. It focuses on critical aspects of transition management and helps improve the level of understanding of the investee's operations and business, that may be limited to financial aspects before deal closure. Additionally, in case of buyout deals, Day 0 planning is crucial for business continuity post-closing and takes precedence.

In our experience, many PE funds initiate planning for the first 30 / 60 / 100-day milestones well in advance. They attempt to prioritise findings from the due diligence phase and combine the same with market research or past industry experience.

We have observed that successful transactions, usually follow these best practices, whilst preparing Day 0 and Day 100 plans -

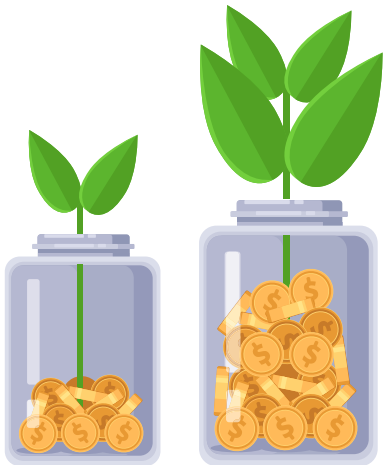
Determine activities to take control of investment on Day 1 – The most critical step in transitioning must commence prior closing, almost immediately after signing. The focus must be on identification of activities required to effectively take control of the investment on Day 1, whist ensuring minimal or nil disruptions to business. These activities must be classified by function, prioritised by impact on business continuity and sequenced to draw a critical path that has to be monitored till closure.

Continuous communication – Direct communication from top and middle management is the most effective means to reduce resistance to change and to avoid confusion. Addressing stakeholder concerns (customers, vendors, employees, government authorities, etc.) goes a long way in garnering their support and comfort for subsequent initiatives.

Transition services agreement (TSA) – When the acquired business is entangled with other sections of the sellers' broader operations, an agreement requiring sellers to provide transition services may be required to maintain business continuity, till such time the business bought out can build its own capabilities and operate on a standalone basis.

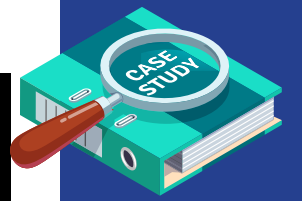
Sellers often provide interim support for areas such as legal, facilities, accounting, IT and other corporate services. Procurement, Distribution and sometimes operations are also provided as transition services. The TSA must be legally binding on both parties and should come into effect on Day 1, have a defined tenure and a clear exit strategy (build inhouse capabilities or outsource).

Operational Diagnostics (post-closing)– In a post deal stage, once access is granted to investee management and employees, a quick assessment needs to be conducted. This not only validates the pre- deal assumptions, but also identifies various operational challenges and risks faced by the investment, that need to be prioritised and addressed. The outcome of the diagnostics often helps the investor and business managers to align short to medium term objectives.



The operational diagnostics can be extended to include a preliminary value enhancement assessment to identify value creation opportunities. These opportunities can be prioritised by ease of achievement and benefit, contributing to long-term strategic and efficiency improvement plans.

Case Study 1 – What could go wrong



Not all information provided by the target may be true and accurate, as has been experienced by a PE who invested in a garment manufacturer. The PE saw their investment value wiped away due to misrepresentation and willful deceit.

Though there are limited mitigating controls to counter frauds, we have increasingly seen PEs perform an operational diligence and corroborate market benchmarks with financial results reported by the company to identify factors that are 'too good to be true'

Pro-tip

If an investment decision has been made, taking into cognizance, certain legacy issues and diligence findings, it is critical to develop a remediation plan post investment and drive execution within a reasonable timetable

- A quick 3 – 4 week assessment of the portfolio company, facilitates better understanding of operations and helps refine the budgeting and MIS reporting practices
- Size up the team by evaluating and building people's and organisation's capabilities.

Value protection

Human element
CEO's most critical transition agenda

In any PE or VC investment, it is critical to connect with the human side of the deal. Several studies across industries and organisations have presented the possible people issues faced as part of M&A deals.

There is a striking similarity in the challenges faced across deals and two of the most critical ones are (i) differing vision and values between PE / VC and portfolio company and (ii) a change in leadership approach and working style.

Other common people issues observed in varying degrees across PE or VC investments are (i) attrition of critical employees, (ii) employees' apprehension to change in culture and working style (iii) uncertainty about personal growth prospects, and (iv) lack of clarity over future course for business.

In order to address such recurring people related issues, investors can focus on:

Change management: An efficient change management strategy addresses the key elements of stakeholder management and culturally aligning the PE and the portfolio company.

People Risk and Impact Management: Regularly assess and monitor morale, confidence and progress of the change approach to tailor change activities accordingly.

Leadership Alignment: This entails nudging the leaders towards a common goal. Align the senior management to follow the same vision, enable them to achieve the overall goal with their specific role and facilitate the decision making.

Talent retention: PEs bring in structure, professionalism and objectivity in decision making through continuous engagement in the portfolio company. People with access to information, vendor- customer relations and knowledge base are critical, and thus, a structured plan to identify and retain talent, to steer the company post-investment well in advance is important.

Stakeholder alignment through clear incentives: Key stakeholders must be aware of their appraisal metrics and related timeframe for performance. The careful definition of a suite of KPIs (including cash-based metrics) should be cascaded down to the functions. In our experience, a simple waterfall of KPIs and incentives drives natural alignment to investors vision and timeline to achieve set objectives.

Figure 7: KPMG in India Analysis of Post deal challenges across all deal types (corporate, PE, strategic, financial)

Pro-tip

- Identify the top 20 managers to be retained prior to closing the deal
- Ensure stakeholder alignment to overall vision by redefining the performance KPIs
- Given limited enforceability of non- compete and GST treatment, it pays to engage and transition relationship with the top 20 clients / customers

Value protection

Day 1 Finance
Gateway to taking effective control of the investment

In many promoter run companies, the finance function is often perceived as a "cost center", with the promoter exercising singular control over cash and decisions.

The finance function is reduced to maintaining book of account and basic banking operations. There is inadequate focus on working capital management or quality of finance reporting. This lack of clarity often impacts valuation or prevents the companies from realising valuable long-term gains.

Following are some of the common themes to gain effective control over the investment.

Working Capital Management: Despite highlighting working capital trends during the diligence, short-term cash flow issues often surface after taking control of the investment. This is commonly attributable to promoter exits, lack of clarity in reporting lines or delegation of authority.

A focused monitoring of cash flows easily addresses some of the initial funding challenges, whilst creating a template to unlock or generate cash through strategic interventions. Quick wins include accelerating collections, implementing payment controls, inventory corrections and renegotiating supplier credit terms.

Medium term interventions include payroll restructuring, controlling capital expenditure, tax structuring and identifying non-performing assets, which can be monetised. Introducing cash KPIs for department heads helps in disseminating working capital accountability in the organisation.

Structural interventions often align transformation activities such as supply chain redesign, asset light logistic models, renegotiation of terms, etc., thereby releasing tied-up capital.

Improve data quality and reporting discipline: Often financial data exists in silos, is tightly controlled and differing versions selectively presented to various stakeholders. This selective disclosure impacts quality of decisions and necessitates multiple reconciliations.

A detailed walkthrough to understand the process of obtaining, storing, processing, and protecting data used in financial reporting is critical to establish a single source of truth, build confidence and rely on the entity's reported performance. This also establishes reporting discipline and ensures timely book closure.

Harmonization of MIS and Reporting framework: In our experience, a planned change in the MIS reporting requirements is imperative to obtaining complete financial control over the investment.

Mapping investor's reporting requirements (including timing, quality and adequacy of reporting) with the investee's reporting systems is essential to identify improvement areas in MIS system and drive change.

End use monitoring: Reviewing cash flows to determine application to intended projects is paramount for the investor. We have observed that a statement of end use of cash, certified by the auditors or other competent professionals, is sought by the investors as a condition subsequent to the deal.

Case Study 2 – What could go wrong

In more than one instance, within two years of its investment, PE funds have initiated legal action against portfolio companies over -

- Loss of valuation as a result of accounting impropriety at a textile company and
- Allegations of forgery and misuse of funds

There is an emergent need to establish robust reporting systems and mitigants, to monitor end quality of reporting and use of funds immediately after investment.

Pro-tip

- Preparation of a 13-week rolling cash flow projection to identify possible leakages and cash requirements
- Benchmarking working capital to industry and macroeconomic indicators
- Relentless focus on improving collections
- Ensure 'single source of truth' to improve reliability of financial information.

Value protection

Enterprise Risk Management
A fit for purpose governance structure

In recent years, there has been an increasing demand for insuring directors' and officers' liabilities, especially for PE professionals - indicating cognizance of historical dormant risks, that may surface at a later point. However, companies need more than just insurance to ring-fence management from such risks.

The best approach is to establish an enterprise risk management framework, focusing on controls, continuous monitoring and adherence. Establishing a framework has its own associated cost and every portfolio investment needs its own fit for purpose framework to yield long term sustainable benefits.

In our experience, frameworks often have diminishing effectiveness in detecting and preventing fraud risks, if not tested and strengthened periodically throughout the investment cycle – i.e. from entry till exit.

Figure 8: Typical components of a robust Enterprise Risk Management framework

Typical challenges faced by an incoming investor

Promoter driven companies seldom accord adequate importance to risk management. Often, businesses are managed by a close-knit group of trusted personnel, bound by family or social relations. In the absence of a structured and standardised operating procedure, managers often rely on their access to promoters, experience and tribal knowledge for decision making.

In such situations, it becomes imperative for investors to conduct background checks on directors, promoters and other KMPs, with specific focus on their reputation and past business interactions in addition to the customary financial analysis prior to investment.

Post investment, especially in companies with a steep growth trajectory, to gain comfort over operations and risk environment, a quick 4 – 6 week controls diagnostic helps identify enterprise risk controls in practice, potential conflicts of interest and other risks.

Common challenges that were observed during a post- investment risk assessment:

Ad-hoc compliance monitoring: Often companies do not have detailed checks and balances, leading to non-compliances, most of which can be easily avoided.

Statutory and Regulatory non compliances often impose penalty and imprisonment of directors and executives for non-compliances.

Identification of an exhaustive list of compliances applicable to the company, with the help of lawyers and license consultants is a good starting point. A one-time exercise for gap identification and corrective action helps in establishing a compliance baseline. A periodic monitoring framework, with regular trainings, audits and surprise checks ensures compliance hygiene is continuous and sustained.

Lack of clarity around segregation of duties (SoD) and delegation of authority (DoA): SoD and DoA need to operate in tandem. Whilst SoD determines controls and avoids conflicts and collusion, DoA establishes necessary checks and balances to mitigate risks. Many companies often ignore these policies and power is concentrated in the hands of a few, leading to fraud risk and may even disrupt business continuity. To establish a robust framework and shift in mindset, the policy implementation needs to be driven from the top.

Lack of well-defined Standard Operating Procedures (SOPs): Often documenting policies, procedures and practices are not considered a necessity. Imbibing a structured SOP not only helps in pursuing growth initiatives, but also assists in fixing responsibility, seamless transition and effective communication.

Lack of awareness of policies and procedures: Employees often lack clarity on many essential policies and procedures, due to infrequent trainings and weak dissemination. Lack of awareness of policies such as prevention of sexual harassment at workplace, whistle blower protection, anti-bribery and corruption, and gifting, could not only lead to apprehensions whilst reporting instances of non-compliance or fraud, but could lead to inadvertent mistakes.

To mitigate this risk, a well-defined incident reporting mechanism should be established, which takes into consideration the following -

- Definition of an incident and when should it be reported?
- To whom should the incident be reported and escalated?
- Safeguards to be practiced to avoid incidents
- Maintaining confidentiality and privacy of whistleblower
- Protocol to deal with and resolve reported incidents?

Pro-tip

- Strengthen Board subcommittees for Governance (Audit, Nomination, Remuneration and CSR) to enhance internal controls through policy implementation
- Continuously engage with promoter and management to cultivate seriousness and discipline about compliance. It requires a shift in mindset from meeting minimum compliance, to that of corporate governance gatekeeper.

Technology and Cyber Security
Is it a risk worth overlooking?

Cyber security risks are frequently overlooked during a transaction, despite the overarching reputation and business continuity threats posed to the investee and investor.

With evolving regulations and increased importance accorded to data protection and privacy, any non- compliance can have widespread consequences. A hospitality sector deal that went on to create one of the largest hotel chains globally is a leading testament to such pitfalls. Hackers had penetrated the target's reservation system undetected two year before the acquisition. Post integration, the hackers used this loophole to steal personal details of more than 300 million guest accounts.

Similarly, a telecom company was exposed to such threat when acquiring one of the largest internet and search-engine companies. Years before the deal, more than a billion user accounts of the target had been compromised and personal information was stolen on two separate occasions. The disclosure of these data breaches by the target also led the acquirer to lower its offer.

Companies with digital operating models and having extensive access to customer data are more susceptible to cyber threats. Investments in such entities mandate the need for a proactive approach to cyber risk assessment at the pre-deal stage and management in the post investment lifecycle.

The latent threat of weak policies, practices or undisclosed breaches before deal closure can not only put an investor at succession risk of breaching disclosure laws, but also have a cascading effect of stiff penalties, brand and reputational damage, loss of customer confidence, lawsuits and more critically business disruptions.

In such situations, the representations and warranties may not be adequate to safeguard the investors. Such risks may also require investors to shell out unplanned amounts post-acquisition to strengthen the cybersecurity framework of the investee in line with prevailing compliance standards.

In our experience, network vulnerability assessments and information security policies are two critical protocols that can be set up to achieve quick wins.

Following are some of the diagnostic studies that every PE should carry out post investment:

IT landscape assessment: This entails a review of the investee's existing software, hardware, infrastructure and IT organisation. It helps identify gaps and determine an implementation priority sequence based on cost benefit analysis of remediation.

Cyber maturity assessment: The objective of this assessment is to gain visibility into the maturity and strength of existing cyber security protocols, identifying gaps vis-à-vis industry standards such as NIST Cyber Security Framework and SANS Top 20 Critical controls, and determining measures to mitigate risks.

Vulnerability Assessment and penetration testing (VAPT): VAPT comprises of simulated controlled attacks on the investee's network infrastructure and/or applications to identify security loopholes, depth and breadth of access that can be gained by malicious attacks. Network architecture review, configuration reviews, code reviews and red team assessments when coupled with VAPT make the assessment comprehensive.

Vendor Governance: For companies with extensive outsourcing, ensuring aspects such as vendor risk profiling, diligent onboarding, periodic audits, and review of contractual agreements is basic to protecting against vendors and third-party suppliers related risks.

Imminent enactment of India's Personal Data Protection bill (PDPB): Inspired by EU's GDPR, India may soon enact PDPB. PDPB compares to GDPR, with penalties of INR 15 crores or 4%[9] of annual global turnover, whichever is higher – for infringements, violation of data processing principles, data transfers to third countries, not respecting data subjects' rights processing of special data categories.

On implementation, investors in IT, internet and consumer sectors need to assess the impact of the draft PDPB, on their investees and estimate the cost of compliance, that may be perceived as an investment into brand and sustainability.

Pro-tip

- An IT Due Diligence and Cyber assessment in the pre deal stage, helps enable investors to modify deal contours and valuation
- Review the customer contracts to incorporate a liability cap clause, linked to cyber incidents and 3rd party data breaches.

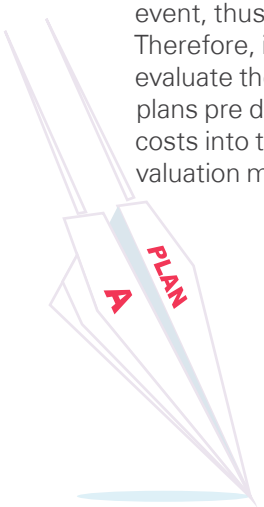
9. India data protection regime – Close to reality? Personal Data Protection Bill 2018, KPMG in India report, August 2018

Business continuity and Disaster recovery planning?

The need for a robust business continuity and disaster response plan has been amplified over the last decade with frequent natural disasters, geo-political tensions and pandemics. The impact of such occurrences on businesses has been magnified due to global reach of supply chains, large scale outsourcing and concentration of specific industries with select countries or regions.

Investors should understand if the investee has a tried and tested disaster recovery plan (DRP) to address any exigency, remediate impacted infrastructure and develop workarounds to facilitate smooth movement of workforce or resources necessary to maintain business continuity.

Absence of a tested DRP or BCP, can take the investee "offline" in case of an adverse event, thus leaving the investors exposed. Therefore, it is critical that the investors evaluate the adequacy of these exigency plans pre deal and factor remediation costs into the investment thesis and valuation models.



Technology and its impact on business continuity

Unlike natural disasters or pandemics, technology failures are relatively common. These events have a higher disruption quotient and impact the brand. The growing reliance of operations on technology, further amplifies the need for entity level exigency plan, especially during change of ownership or control.

We have often observed that authors of the exigency plans are no longer with the company and the current understanding is greatly diluted, documentation scattered, and the intended purpose defeated.

Therefore, investors must drive strengthening of exigency plans by adopting industry best practices and institutionalising periodic review and refreshers.

Alternatively, it could consider diversifying or outsourcing activities to spread and manage the risk.

Dealing with exigencies through a 'Hyper care' approach

Maintaining business continuity, especially during unforeseen events is tough. Management must mobilise the exigency protocols across functions, immediately on becoming aware, to minimise the impact on operations.

Exigency protocols need to be initiated and functions have to switch from a business-as-usual mindset to a new 'hyper care' working methodology. Switching into 'hyper care mode' requires specific considerations:

- Secure senior management commitment to set the right tone
- Establish a collaborative approach to managing operations, since hustling to retain control can be counterproductive
- Prepare daily plans (including regular calls and management updates), to instill the necessary discipline
- Establish single source of truth to avoid disruptions and facilitate seamless decision making
- Lastly, prepare a transition plan to transfer control to business-as-usual, keeping senior management involved to clarify queries and stabilise operations.

Pro-tip

'Hyper care' during business exigencies

- Periodically test robustness of BCP and DRP, through mock drills, at least once a year.
- Dedicate resources to own and review effectiveness of exigency plans. Include reviews in board agenda.
- Grade customer, vendors, suppliers, location and technology infrastructure on the parameter of risk exposure
- Review contracts for adequacy of force majeure and other protective clauses.

Over the years, the financial sponsor community have realized that while choosing the right asset and making the investment is important, the real value creation happens when global best practices are implemented, right professional management is hired and technology/ data is used to drive the business forward. This is what differentiates a good investment from a better investment.

Nitish Poddar
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Deal advisory
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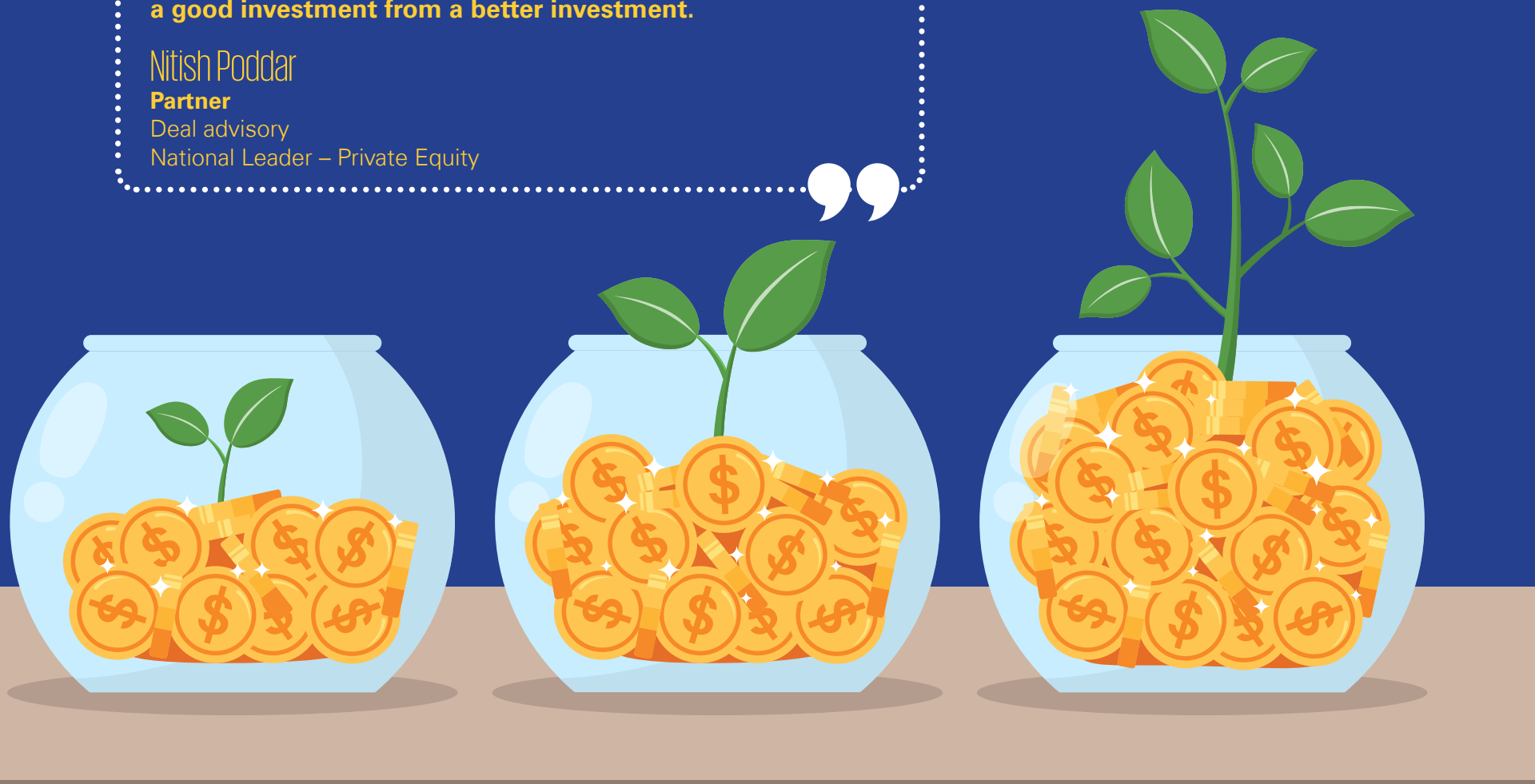


Value enhancement

Clear visualization of ideal future state helps PEs guide management teams to identify and implement specific value enhancement initiatives during the investment period, **thereby expanding scale, capabilities and profitability.**

Successful investments are predicated on a clear vision

A strategic refresh is typically the first item on the Board's agenda post a PE investment. This checkpoint helps redefining or readjusting the business strategy in a competitive landscape, which then defines the future course of the portfolio company. Whilst strategic planning process remains the same in all investment scenarios (majority / buy-out / minority / bolt-on), managing stakeholders' expectations can vastly vary depending on multiple factors.

Value enhancement strategy that is drawn for every portfolio company can be a combination of one or more levers, which should be curated while taking into account multiple factors, such as (i) macroeconomic indicators, (ii) sector dynamics (iii) organisational maturity. Figure 9 – Value enhancement framework showcases, the different aspects of the value enhancement strategy for portfolio investments.

Across the maturity lifecycle of a portfolio company, certain initiatives could be critical towards value enhancement

Figure 9: Strategic spiral of investment

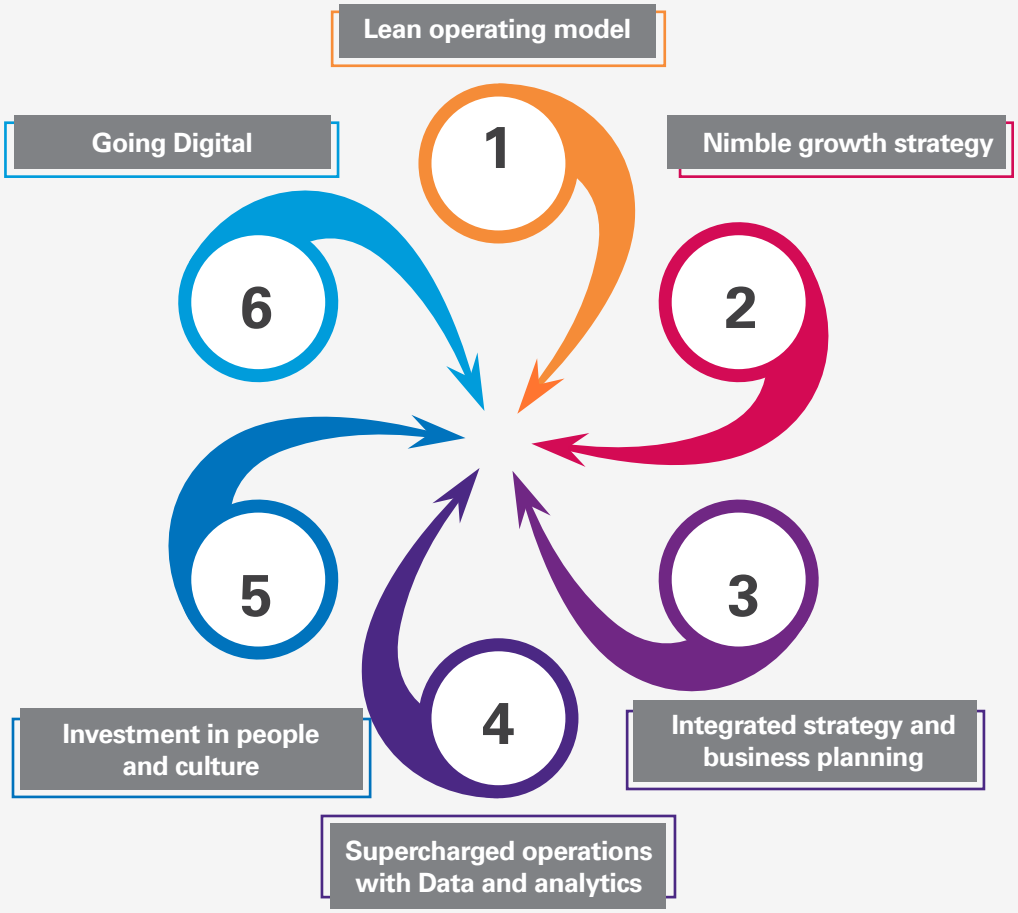
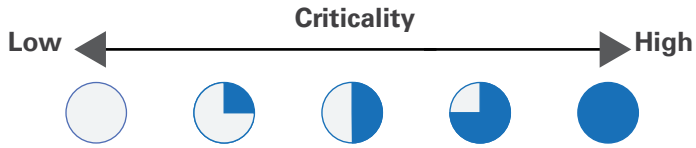


Table 2: Value enhancement focus areas and criticality across maturity cycle

Economy	Early Stage	Mature Stage	Special Situations
Go to market strategy refinement			
Value proposition reinforcement			
Customer and channel integration			
Operational efficiency improvement			
Procurement efficiency enhancement			
Lean operating model design			
Going Digital			
Investment in people and culture			
Integrated business planning			
Data mining, analytics and AI adoption			



Build flexibility and efficiency into your growth strategy and create the right value perception

Interventions can be disruptive…

Despite having a strong vision for growth, companies often fail to differentiate themselves from competition as they lack a robust strategy that is intertwined with operations. In such scenarios, investees can benefit from the PEs experience and strategic viewpoint to enhance value. PEs guide their portfolio companies in prioritising, sequencing and substituting business activities that can lead to greater alignment with growth targets.

A combination of refining the go-to-market strategy, tweaking or optimising the product/ service portfolio, strengthening the brand value across multiple stakeholders can bring out a transformative impact on value, through increased revenue, better customer experience and effective cost controls.

Whilst a coordinated effort can result in significant improvements, some interventions can be disruptive.

Table 3: Typical Go-to-market interventions across investments

	Minority stake	Majority stake	Bolt-on / Platform play
Product	Suggestions on improving the product pipeline	Rationalising product portfolio, product innovation and new segment launch	Recalibrating the combined entity's product portfolio
Price	Guiding on pricing discipline and processes	SKU launches at opportune price points	Pricing improvement through economies of scale
Channels	Proposing sales channels and structured models	Expansion through 3rd party operations/ franchisees while remaining asset light	Harnessing complementary sales capabilities. Cross- selling, geographic re-focus, sales force rationalization
Branding	Brand messaging, re-defining value propositions	Brand repositioning, customer communications leading to brand reinforcement	Customer communications strategy (B2B)

...and yet beneficial in the long run

Continuously evolving market dynamics, changing customer preferences and margin pressures are forcing companies to realign their go-to-market (GTM) strategy on a more frequent basis. Such evolution can help companies stay ahead of the curve.

Portfolio companies can experiment with a combination of these levers to improvise their GTM strategy, with support and guidance from the PEs.

Table 4 - Value enhancement interventions for GTM strategy

Pricing discipline	Channel recalibration	Portfolio expansion
Customer mining	Product innovation	Bolt-on acquisition
Geographic expansion	Brand extension	Sales team activation

Case Study 3 - What went right

Global private equity acquired significant minority stake in a leading Indian dairy products company

Deep industry expertise and support from the investor, helped the company:

- Double its procurement infrastructure, increase production capacity by almost 40%
- Enhanced product portfolio by introducing long shelf life products and a wider selection of SKUs
- Expand into North Indian market with a wider product portfolio
- Implement a formal mechanism for pricing decisions, resulting in improved profitability.

Along with other initiatives, investor guidance resulted in:

- Double revenue and triple EBITDA in 4 years
- Positioned the company well for strategic sale to a global dairy leader.

Case Study 4 - What could go wrong

An online furniture maker backed by multiple funds had to scale back operations due to frequent changes in the go to market strategy from a marketplace model to an inventory led model.

This resulted in the company's inability to compete with other players in the segment, who with a focused strategy, built customer perception and branched into omni channel retail of furniture and allied products.

Go to market requires an in-depth understanding of the market, especially:

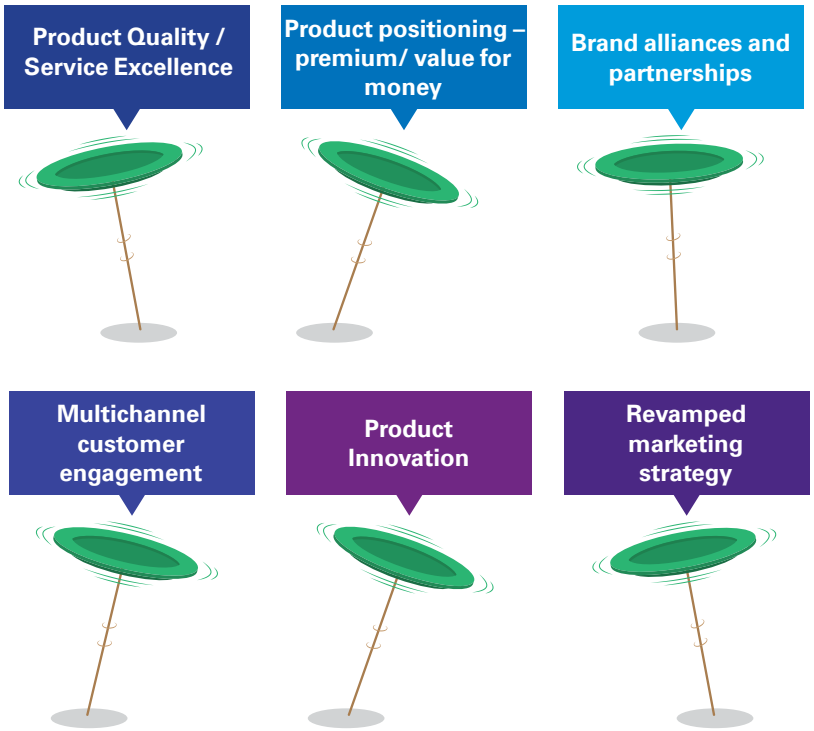
- Market fragmentation and maturity,
- Competition from other players,
- Customer acceptance and
- Technology disruptions.

Creating the right value perception

We are in a disruptive era which is defining the very foundations of consumer behavior. Not just B2C but even B2B companies are recognising the need to continuously engage with customers to retain their mind share. PEs use their experience to guide the portfolio company to develop the right brand with the underlying components of positioning, messaging and corporate citizenship.

It is also not uncommon for portfolio companies to engage in social media to create awareness as part of their brand marketing strategy. A good branding strategy helps enhance customer loyalty or differentiate the product or service, from their competitors. There exist instances where brand positioning has been used as a primary tool to increase market share.

Table 5 - Value enhancement interventions for customer Value perception



Case Study 5 - What went right

VC fund's majority acquisition in India based craft beer and beverages startup

Series of capital infusion together with investor direction led the startup to: acquire breweries in India and transition to domestic brewing, expand the product portfolio and geographies (overseas market), promote the brand in the premium segment to attract young urban consumers, reinvent digital marketing strategies and collaborate with restaurant search and delivery apps launch a platform spanning live music gigs, web series and partnerships with Indian independent music scene to produce original content.

Integrate the channels to provide a seamless experience

Periodic changes to the sales channel mix with a focus on enhancing customer experience, is key for increasing value. To bring about these changes, necessary insights such as product-channel mix and channel-geography mix, can be obtained through data analytics and simulations performed on internal and external customer data. For example, geo-spatial mapping of customer demand can reveal insights around behavioral trends and unmet needs. Channel optimisation has multi-faceted benefits, primary being judicious capital deployment and calibrated inventory levels.

Armed with PEs experience, investees could determine the optimal route to market across products and geographies. This will allow them to tailor the value proposition and commercial programs for each channel and target group. These interventions have a multiplier effect on the company's revenue growth and set the stage for the next level of global expansion. For instance, a portfolio company selling products within a particular region may grow significantly by entering international markets by piggybacking on the network and channels of PE's other portfolio companies. PE firms could guide their investees to enter into strategic relationships with other market players, preferably other portfolio companies.

In a connected world, companies are adopting avenues for digital marketing through online channels, which could possibly turn into the primary outreach channel. It is widely believed that post-COVID scenario could lead to reduced patronage of brick and mortar channels. Companies can tap this opportunity and pursue an expansion plan, which will also help in solving their scalability and profitability conundrum.

While physical retailers are striving for digital presence, pure-play e-commerce brands are aiming for sophisticated omnichannel offerings that blur the line between online and physical experiences. Portfolio companies that have taken initiatives to redefine their channel strategy have helped enable the sales functions to sharpen their focus and increase their reach at the same time, resulting in increase in volume and value of sales conversions.

Table 6 - Illustrative case studies

The story	A hyperlocal player has been guided by its investors to retain technology superiority for seamless operations and swift fulfillment	A ride sharing startup has multiple channels for listing vehicles and has formed strategic alliances to improve customer service and market penetration	A logistics player has transformed last mile delivery by aggregating distributed capacity. The superior customer experience has led to incremental investments and alliances
Sector	**Consumer Internet**	**Ride Sharing**	**Logistics**
Interventions			
Hyperlocal enablement	✓	✓	✓
AI enabled optimisation algorithms	✓		✓
Asset light fulfillment		✓	✓
Spot delivery contracts			✓
Last mile innovation	✓		✓
Distributed warehousing	✓	✓	
Spare capacity aggregation	✓	✓	
Logistics Price discovery			✓

Drive efficiencies through automation

Operational effectiveness holds immense value enhancement potential. Some PEs possess expertise in implementing such interventions across their portfolio companies.

It is essential to develop the right KPIs, customised for every business model and then structure them in alignment with the available data. In today's enterprises, digitization of systems and processes generate enough data that can act as an insights engine.

In our experience, streamlining operations involves interventions across three broad areas – operational efficiency, procurement effectiveness and lean operations, which further constitute of several underlying levers.

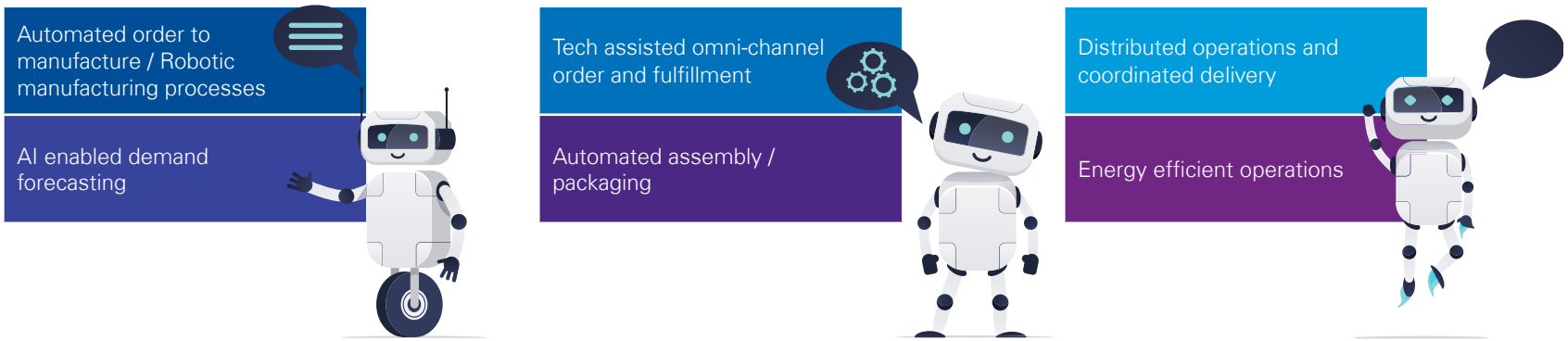
Improve operational efficiency

From robotic order fulfillment, remote monitoring using drones, to efficient energy utilization initiatives, PEs are guiding their portfolio companies to achieve operational superiority.

In the post investment period, some operational issues become immediately apparent, while others surface after thorough investigation. Often, the origin of these issues is only discovered when the impact of not fixing them becomes a draw on operational performance, and then ripples outwards to affect profit margins. The impact of operational efficiencies is amplified in manufacturing or process industries

Further, in the case of bolt-on acquisitions, interventions around capacity optimisation could drive economies of scale in production. Similarly, coordinated distribution could free up working capital. In such cases, technology implementation and automation become cost-effective enablers for growth. Robotic process automation (RPA) based tools have matured and now readily available. These are being increasingly used to automate any manual processes in business processes in finance or HR. RPA is a light-weight technology that sits at the desktop level and does not need integration with existing applications. Moreover, the instances can be scaled up and down based on seasonal demand, with little advance intimation. The elimination of human errors by automation using RPA, nearly pays for the investment.

Table 7 - Value enhancement interventions in operational efficiencies



Value enhancement

Case Study 6 - What went right

A consumer internet company backed by multiple funds has taken up interventions to scale up R&D and upgrade technology to -

- foray into hi-tech production, efficiently scaling up its omni-channel presence without impacting the customer experience
- double production while operating using an asset light model
- use data analytics for demand forecasting to improve inventory turnaround.

Pro-tip

- Several RPA solutions are now available as plug and play tools that can also be used by non-IT professionals
- Energy efficiency measures can lead to significant savings. Enabled by IoT and sensor-controlled circuits, these devices can provide RoI within 12-24 months.

"Trim the fat" from your operating model

Design a lean operating model

Operating models are an aggregation of core activities, systems, processes and equipment that create sustainable value for customers and other stakeholders; and is considered the core engine to operationalise growth strategy.

Continuously evolving customer expectations, increasing competition from peers, and fragmented market structures are forcing companies to rethink their operating model. A lean operating structure and asset-light business model enables companies to disrupt the market with their product innovations, service excellence or pricing structure.

Post investment, one of the first interventions by PEs is to create a leaner operating model through rationalization of non-core functions by simplifying the process or outsourcing functions. Leaner operations help companies optimise costs and free up capital.

Pro-tip

- Dive deep into unit cost economics to check the returns on deployed capital for different service channels and customer touchpoints
- Check applicability of pay as you go platforms for rationalising your investee's non-core functions such as payroll and digital advertising.

A Hands on approach combining operating experience and constant mentoring of portfolio in strategy, governance and capital allocation sets apart the best performing PE's in maximizing value from their investee companies.

Vikram Hosangady
Partner and Head
Client & Markets

Value enhancement

Following are some instances where PE firms have taken specific initiatives (Refer Table 9 - Value enhancement initiatives in operating model) to shift towards a lean operating model, resulting in sustained growth, thereby increasing their valuation.

Table 8 - Illustrative case studies

The story	A hyperlocal player has been guided by its investors to retain technology superiority for seamless operations and swift fulfillment	A ride sharing startup has multiple channels for listing vehicles and has formed strategic alliances to improve customer service and market penetration	A logistics player has transformed last mile delivery by aggregating distributed capacity. The superior customer experience has led to incremental investments and alliances
	Consumer Internet	**Ride sharing**	**Logistics**
Interventions			
Empower customer through self-service	✓	✓	✓
Reduction in unit cost of marketing and service	✓	✓	
Digital enablement	✓	✓	
Asset light market penetration / growth	✓	✓	✓
Customer shift from brick and mortar service	✓		✓
Variable overhead efficiency maximization	✓		✓

Extract value through supply chain optimisation

Supply Chain optimisation

From order creation to shipment to delivery, value enhancement opportunities exist across the procurement lifecycle. Whilst some initiatives require investments, others can be achieved through simple process and controls modifications.

A strong supply chain, with focus on inventory and warehouse management can help unlock substantial value. However, implementation is key and requires coordination across functions such as sales, production, procurements, logistics and finance.

Warehouse and Inventory management

Warehouse optimisation begins with simplification of the distribution process. Adoption of technology and algorithms can help further streamline the process by increasing floor space utilization and picking efficiency.

An optimised warehouse leads to better inventory management, not only unlocking working capital through reduced carrying costs, but also facilitating adoption of industry best practices like Kanban scheduling and Perpetual Inventory Management.

With reliable data, strong forecasts and insights aided by technology (AI, Big Data, etc.,) companies can effectively negotiate prices with vendors.

PEs can further support these initiatives by guiding companies to partner with others for strategic sourcing or alliances.

In case of bolt-on acquisitions, majority of benefits in procurement and supply chain would be contingent on streamlining processes and interlinking the systems.

Logistics optimisation

Lately, technology coupled with policy measures has helped in removing some of the supply chain bottlenecks. Companies have implemented algorithm based vehicle routing to streamline freight movement thereby improving vehicle capacity utilization and fuel consumption patterns. Such solutions have been mainstreamed through high smartphone ownership and access to affordable mobile data.

Similarly, ERP solution providers have also facilitated rapid digitization, for instance leading providers have come up with patches for integrating mobiles, handheld devices and scanner guns for barcodes and RFID chips. This allows direct recording of transactions on ERP and enables real time tracking of goods and consolidated reporting of inventory.

Value enhancement

We have observed some interesting initiatives undertaken by investee companies to enhance their SCM capabilities, with support from PE firms:

- Acquisition of entry level startups that have created innovative logistics solutions
- Strategic partnerships with logistics/ technology focused companies
- Building internal tech enabled tools and platforms to streamline logistics
- Mobile hand-held devices acting as scanners, directly linked to ERPs that have reduced room for error
- Optimise the supply chain network with an objective to increase coverage (geographic, channels, segment).

Table 9: Value enhancement initiatives in logistics

GPS enabled asset tracking	Predictive fleet maintenance (IoT enabled)	Fuel and capacity optimisation (AI enabled)
Relay trucking model	Telematics and real-time communication	Matching supply and demand (AI enabled)
Spot price discovery mechanism	Modularised systems and equipment	Trackable pallets and returnable packaging (AI enabled)

Pro-tip

- Revisit the P2P and O2C process and identify steps that are not aligned to the vendor / customer contracts. Use these points to renegotiate T&C that can provide potential upside
- Benchmark your logistics cost with peers and evaluate cost rationalization opportunities.

Case Study 7 - What went right

Guided by marquee investors, an Indian B2B startup operating in logistics space:

- consolidated the fragmented logistics market by linking shippers to fleet owners and truck drivers
- Invested in AI algorithms to increase automation and improve asset utilization resulting in faster turnaround time
- scaled up operations and strengthened technology.

What could go wrong

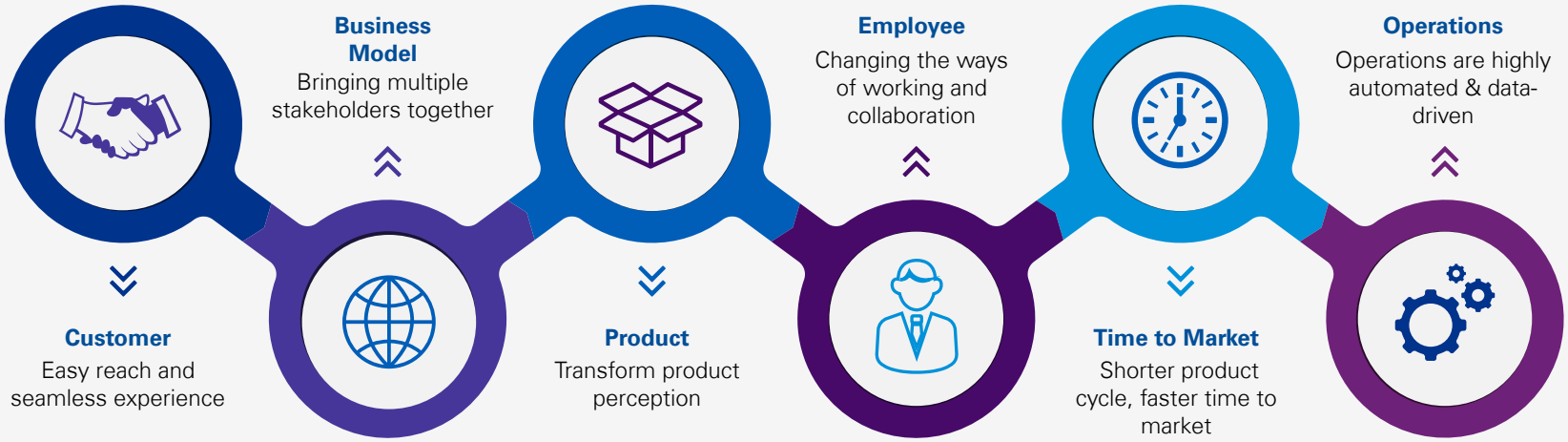
Although supply chain optimisation can enhance value, sometimes forced interventions could have contradicting result, for example:

- Implementing supply chain management systems without in depth understanding of the process or business requirements, could result in mismanaged inventories across locations
- Lack of control over the operating process or excessive outsourcing could be detrimental to product quality and business USP
- Terminating long term legacy supply contracts in an attempt to save costs, could result in supply chain disruptions due to non-alignment with business philosophy and requirement by new suppliers.

Value enhancement

Accelerate digital transformation to deliver in a post-pandemic reality

Figure 10 – Impact of IT across a business' value chain



Information Technology has become imminent for business survival, irrespective of the sector or play. This has been reinforced by the COVID-19 pandemic, which has accelerated companies to adopt remote working and to reach stakeholders virtually. Degree of technology adoption is proving to be a key differentiator among competitors and impacts both cost of service and customer satisfaction.

Technology and digital transformation have graduated from being an enabler to being a differentiator.

Scalability of the current platform

The benefits of technology can be realised across all sectors and workstreams by asking the simple question – "Can we do it better or faster with IT?". Ability of entities to adopt new concepts like AI, blockchain and address data processing demands across locations/ devices to their advantage will shape market leaders of the future. Scalability and agility of IT applications need to be considered as a specific evaluation point for business planning.

Companies are continually exploring digital transformation initiatives, at both front-end and back- end to improve operational efficiency and enhance user experience especially given the needs of today's tech- savvy consumers. It may also be useful to calendarise a review framework to periodically benchmark IT scalability requirements.

Traditional business planning seldom factors in the scalability of IT landscape. Therefore, the CIO should be engaged in business planning, and have a seat at the strategic forums especially where IT is considered as a core business function.

Enterprise Resource Planning (ERP)

Technology landscape serves as a repository/ generator of arguably the most valuable asset of an enterprise - data. Traditional business houses often use multiple applications making data integration a nightmare, if not impossible. The need for PE firms to accelerate growth and profitability calls for a drive to digitising and automating workflows and establish single source of truth.

PE firms and investee companies therefore could look to upgrade to an effective modern ERP system to take immediate control of the business as well as support the future growth objectives of the business.

In house vs. outsource

Large PE funds may also seek to outsource day-to-day IT operations to third party vendors, in order to leverage the scale of operations and increase utilization. However, this may require a case to case analysis of each portfolio company and segregation of activities into core and non-core.

Requirements for real-time data and processing capabilities, confidentiality and associated costs are critical factors to consider while evaluating inhouse vs outsource decisions. Both alternatives have their own unique advantages and shortcomings, however PE firms have to consider the long and short term business needs to make the right decisions.

Figure 11 – IT transformation myths

Myths	Mythbusters
Technology transformation is an IT problem, and has limited impact on business synergy realisation	Synergies accruing due to Technology are often between 30-45% • 10-15% synergies that are due to Technology as a function. This requires a strong understanding of business strategy, roadmap and operating model • 20-30% of business synergies that are enabled by technology. It is essential that the technology team and business team act as per the playbook
Technology transformation can be done on the go, and does not necessitate pre-deal planning	More transformations are undone by poor Technology planning than any other factor • Technology architecture is complex, with entanglements within Technology, as well as business-technology convolutions • Technology landscape itself includes 3 major layers – data, systems and users, and it is critical to prioritise the myriad changes happening across all of these
Technology transformation does not require specialists. IT can be adequately handled by in-house IT team	Less than 15% CIOs have experienced a M&A deal - • During transformations, the in-house IT team is usually overburdened to maintain IT continuity and support the increased number of business requests • Less than 10% of organisations have dedicated personnel for IT integration management, IT communication, application portfolio integration and data harmonization
If Technology transformation is botched up, it can always be managed and fixed on the go	A failed Technology transformation has a reverberating impact far beyond IT • While the IT function may still be able to manage using manual workarounds for a limited period, the ability of businesses to realised planned synergies reduces exponentiality • Deals have a limited window to realise synergies, post which organisational inertia sets in

Pro-tip

- Develop a milestone-based technology roadmap overlapping with short term targets having workstream wise dependencies
- Consider outsourcing commodity IT services. More than the savings, it will free up the internal IT team's bandwidth and allow them to focus on strategic projects.

Value enhancement

Invest in people and culture as "No one size fits all"

Many failed deals can be attributable to people complexities. In a PE transaction, the people risks are perceived to be higher. It is a common apprehension that incoming investor may rationalise teams and dilute the culture.

Irrespective of the post-investment situation, a fit for purpose HR strategy ultimately leads to timely achievement of the investment objectives.

One of the first interventions that PEs make on this front is to onboard professionals onto the management team of the portfolio company. While this singular intervention has a cascading effect, the impact can be compounded with help of other initiatives from the organisation perspective.

Streamline organisation structures – In a post- investment scenario, the business priorities may undergo a course correction on a periodic basis, given the dynamics of market and competition. Review of organisational effectiveness is an important precursor for an effective operating model. Some of the common measures is to check the span of control and nature of reporting relationships and transitioning to a lean management model.

Ensure stakeholder alignment through clear incentives: Careful definition of a suite of KPIs (including cash-based metrics) should be cascaded down to the functions and the incentive program realigned to these KPIs. In our experience, a simple waterfall of KPIs and incentives drives natural alignment to the fund houses' vision and recognition of the sense of urgency.

Benchmark organisation productivity – This provides a direction to the entire workforce and workstream leads, as to expectation of the senior management. Benchmarking with the right set of peers is known to create a sense of competition uniting the entire organisation while ensuring a high level of commitment towards achieving the targeted business goals.

Invest in learning and development (L&D): The true benefit of L&D can be reaped only when the initiatives are specific and strive to not only bridge the skill gap amongst the lower level and mid-management sections but sharpen the leadership skills amongst the senior and executive management.

Focus on transforming the Sales Team through effective engagement: Recruiting the right sales leader depends on the investee's business model and PE's investment strategy. In addition to having the right sales head, the PEs should also pay particular attention to empowering the sales team. Following are some initiatives with high positive impact on profitability.

- Put in place the technology infrastructure to enable the sales team
- Redefine the sales cadence and ethos (such as high value interactions in B2B environment)
- Create and communicate a roadmap on aligning and harmonising the sales processes and tools that support the overarching channel strategy
- Leverage insights to re-adjust the implementation of channel strategy on a real-time basis.

Mentoring the Board: With importance placed on strong management teams by sellers, PE firms must take efforts to deploy the right HR strategies to retain and train key operational and management personnel prior to exit. It is common for PE firms to conduct knowledge sharing sessions within their existing portfolio companies to help management teams improve their operations. One such instance was when a PE firm leveraged its global network and introduced the company's founders to manufacturing facilities in China helping them incorporate some of the best practices followed in China.

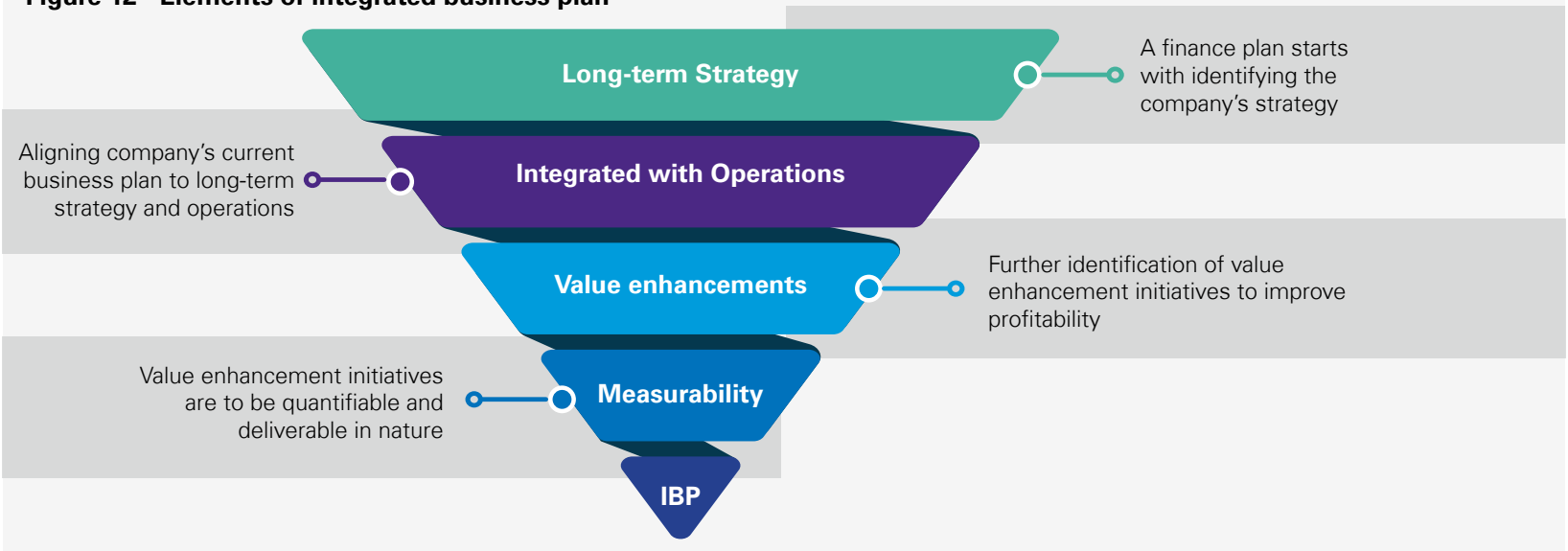
Pro-tip

- Resist the temptation to choose convenience over relevance i.e. ensure that the CxO team are cherry picked based on their relevance rather than availability.
- Refrain from an all-pervasive change in culture of the organisation, rather focus on critical aspects, which are non-negotiable to investor's core philosophy.

Value enhancement

Post deal business planning - Embed five year business strategy in the finance planning process

Figure 12 - Elements of integrated business plan



Integrated business planning (IBP) process can assist in evaluating various scenarios and capture real time insights to better deliver predictable business outcomes.

Among various other concerns related to Indian promoter entities, one that serves as a major hindrance to achievement of strategic objectives is lack of involvement or communication with all workstreams at the planning stages.

Governance processes vulnerable due to overlapping KPIs leading to inefficient planning: Different workstreams work in siloes with individual goals and KPIs. This often leads to misalignment of strategic, financial and operational plans creating confusion about the direction of the entity.

For example, the long-term strategic objective of the business would be to increase the sale of consumer products with focus on advertising spend, whereas the finance function may continue to budget for advertising expenses at the same level (to achieve desired profitability) without taking this into consideration.

Key factors to be considered at the time of integrated business planning for the purpose of goal setting are historic performance (based on data) and benchmarks.

Adopting an integrated business planning approach is the first step PEs take to obtain financial control over the enterprise and communicate its strategic objectives across workstreams. This is critically required to establish and automate a monitoring and reporting framework for the portfolio company and serves as an effective tool for communicating top-down strategic objectives through a common platform.

With the streamlining and automation of business planning and monitoring processes, PEs can spend more time on measurable performance improvement initiatives. While the cliché, "cash is king" is old, it never gets irrelevant. It is among the most common value maximization levers used across PE investments over the years. Often considered as a finance function KPI, in reality, its implementation is interconnected across workstreams and embedded in the day to day operations of the entity.

While most professionals are well aware of the various initiatives across inventory, receivable and payable balances that can be taken to improve working capital, garnering support across all workstreams is among the major roadblocks in its effective implementation. Obtaining senior management buy-ins, including the CFO can accelerate implementation efforts.

Working capital is not a one-time initiative that can be implemented and forgotten. It is more of a discipline, that needs to be followed on a day to day basis and imbibed in the very culture/ working style of the organisation. The following set of activities can be considered:

Benchmarking with peers and setting KPIs – Setting KPIs across workstreams to improve working capital (for example, reduction in inventory provisions, improvement in cash conversion cycle of debtors, etc.) helps align managerial objectives with that of long-term strategy of the company.

Use data to your advantage - Analysing data collected from different workstreams relating to components of working capital can provide valuable insight in driving initiatives. Reviewing historic customer data, using trend analysis to support procurement and production planning, cohort analysis for evaluating cash discount schemes with supplier and customers are among examples of analytics that can be used in evaluating working capital position of the company.

Assess every decision from a working capital perspective – Managers and decision makers must be given adequate training to evaluate and consider impact on working capital for each of their decisions.

Working capital improvement should be driven right from the start; verifying financial stability of new customers and vendors, production planning, procurement decisions, etc. should all be evaluated from a working capital impact perspective.

Pro-tip

- Consider simulating multiple scenarios as part of the planning process, while exploring financial trade-offs and ensure sanity checks for data integrity
- A combination of supply chain financing and cash discount incentives to dealer networks is becoming increasingly popular as a means of cash conversion cycle improvement.
- Integrate planning relevant to all workstreams right from sales, production capacity, headcount, cashflow, inventory planning, etc. to help identify dependencies and establish realistic and achievable goals.

Value enhancement

Supercharge your business with advanced data and analytics

Competition is unforgiving, and with very less room for errors. Businesses are increasingly aware of the need to take critical business decisions across the customer value chain (from procurement to production planning to product development and eventual distribution and pricing strategies) using advanced data and analytics.

PE firms are equipping their portfolio companies with sophisticated data driven decision making tools to create value. Indian businesses across sectors have started moving away from traditional decision-making techniques based on heuristic or an 'understanding of the market'.

Both internal and external data provide key insights into customer behavior, market coverage, upcoming trends, etc., in certain cases forcing businesses to question their entire operating model, disrupt existing processes to clear the path to growth and success.

A common theme noted across PE investments is the use of data and analytics for performance measurement and reporting. With the advent of big data and easy access to external sources, PE funds are increasingly looking at benchmarking internal metrics to that of the market and driving performance improvement through effective and detailed monitoring.

A common set of action points to be considered when introducing data analytics to portfolio companies are listed below:

Data analysis is a team game – Hiring only data analysts/ scientists is not the solution to data analysis. Hence, companies need to focus on building a multi- skilled team that include strategic hires at a mid to senior level. Also, the recruitment of creative designers or deploying visual analytics cannot be ignored as a "good-to-have". A focused team will bring together different parts of the businesses working in silos to drive data-based decisions.

Promote 'purpose-driven' data analysis – Once put together, the scale of data available can be overwhelming. Clarity on what insight you need from data is essential. For example, questions like, "What is the current team productivity and how can we improve it further?" are better than questions like "How do we reduce costs?". Just identifying, "What trend does the data show?", may show interesting results with no/ insignificant monetary output.

Artificial Intelligence (AI) and Machine learning (ML) are not just buzz words - While developments in IT and ERP have made data availability easier, developments in AI are helping entities in efficient analysis and quick responses. Use of chatbots is no longer restricted to e-commerce companies or CRM applications. AI and ML analyse real time data generated by customers/ users reducing the time taken between data collection, analysis and action taken upon them.

Adopt an all-pervasive approach to analytics - Data analytics is not restricted to customer facing or MIS reporting functions. For instance, organisations are increasingly using analytics from recruitment to employee engagement and analysing production efficiency.

Case Study 8 - What went right

A leading financial services company embarked on a journey of implementing a governed Data Lake to house all masters, financial transactions and accounting information to enable automated financial reporting:

- Implemented a Data lake to store all structured and unstructured data from multiple sources
- Developed a centralized ADWH model which provides the segregation of accounting/transaction data at source level
- Enabled financial reporting through an automated and streamlined structure for 50+ entities

Case Study 9 - What went right

An American VC fund has guided a homegrown restaurant chain to reduce food wastage, increase order conversion through app-based notifications and introduce new menu items, thereby pioneering the cloud kitchen concept:

- Leveraged technology to enhance the sales and ordering process
- Accelerated turnaround times for introducing new menu items with dynamic pricing

Case Study 10 - What went right

A NBFC backed by Indian PE firm uses data analytics to enhance customer experience across the board. It leverages data for periodic monitoring to predict high probability defaulters, thereby reducing NPAs and cost to serve:

- Leveraged analytics for identifying profitable target customers
- Data modeling scenarios to predict high-probability defaulters

Pro-tip

- Benefits of data analytics permeate across functions, select the right analytics platforms so that the costs don't outweigh the benefits.
- First-mover advantage is key to using analytics for customer experience. Companies are experimenting new concepts like voice analytics, that derive insights using CRM interactions. Combined with AI, the system can predict the customers who are more likely to buy any product or service.

Exit planning

PE investments are made for a limited period, with a clear goal to exit the investment, at or above the desired hurdle rate.

It is often said that exit planning starts from the date of investment.

Exit trends in India

India witnessed c.$79billion of PE exits in the last 6 years[10], of which c.$42billion were through M&A exits and c.$16billion of open market transactions.

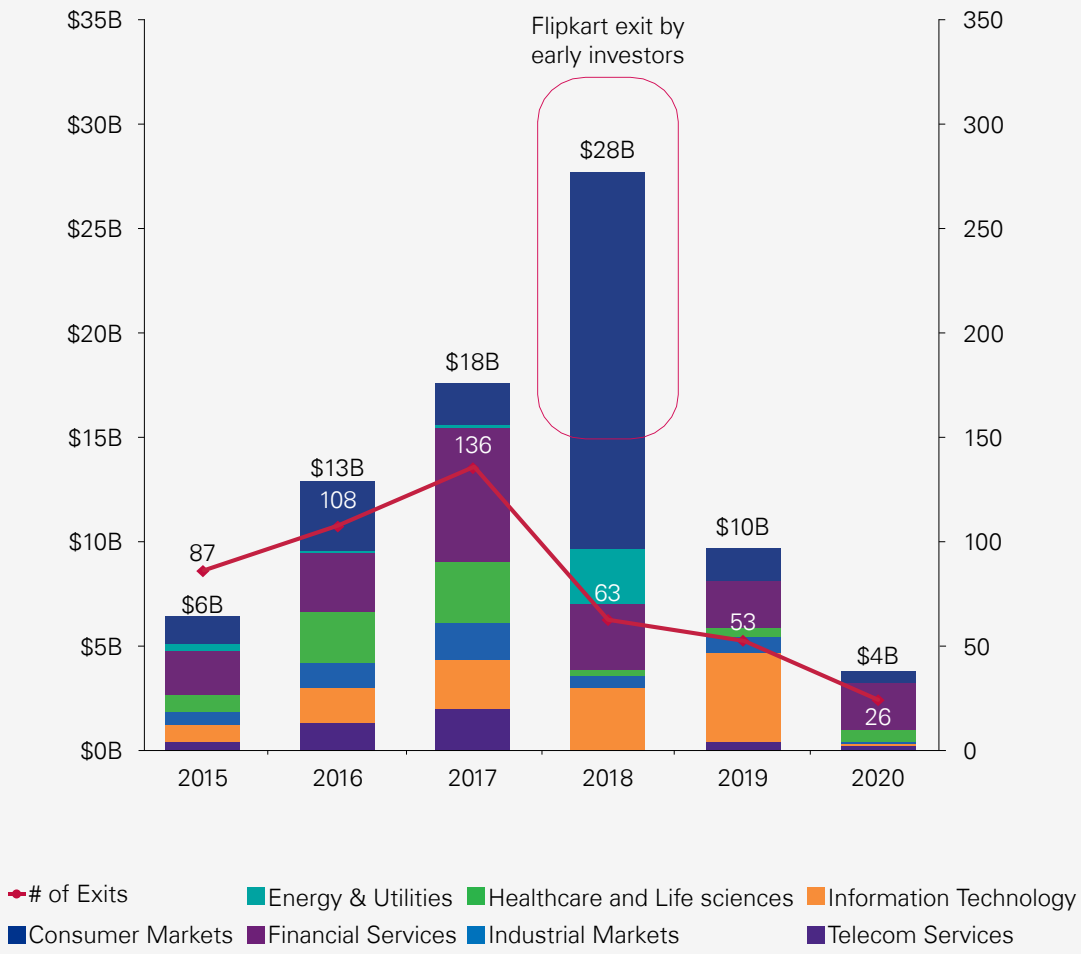
Although the number of exits per year has declined c.50% between 2017 and 2019, they have generated good returns for the PEs.

KPMG in India analyzed the top 300 exits in the last 6 years and observed that nearly 50% of the exits in India generated an annualised return in excess of 30%, across sectors, whilst nearly half the exits outperformed market indices which grew at c.10% CAGR during the corresponding period.

However, the decline in number of exits and consequent increase in median holding period to 6.2 years could be attributed to sluggish macroeconomic conditions and a weak IPO market even prior to the onset of COVID-19.

PE exits in 2020 have fallen drastically, primarily due to business disruption on account of Covid19 and resultant impact on valuations.

Figure 13: Value and Volume of PE exits between CY15 and CY20[11]



10. VCCEdge; KPMG analysis c. 500 exit transactions transactions involving 350 entities
11. KPMG analysis of c. 500 exit transactions

Figure 14 : Median investment holding period of exits between CY15-CY20[12]

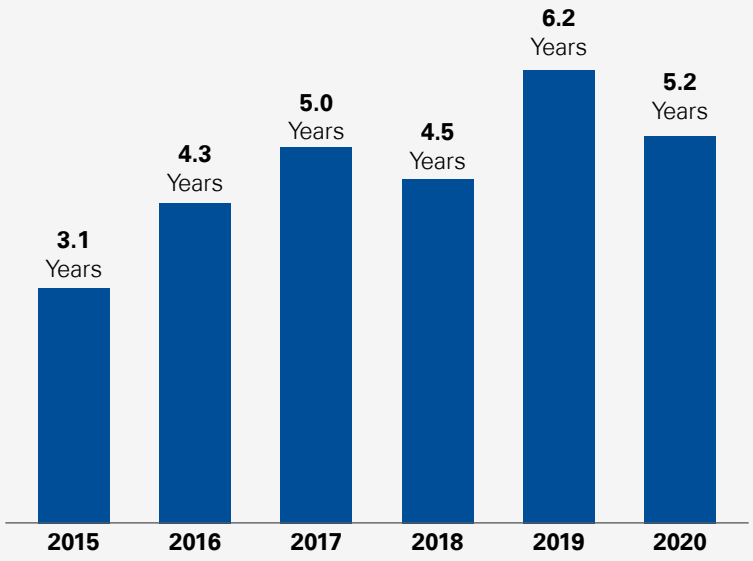
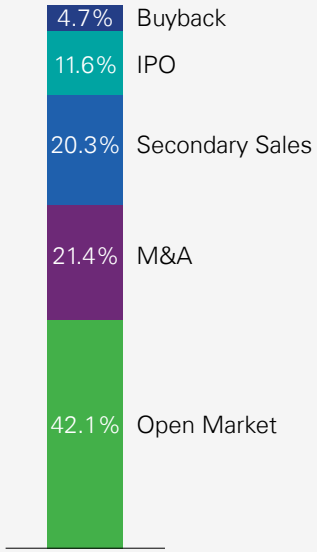
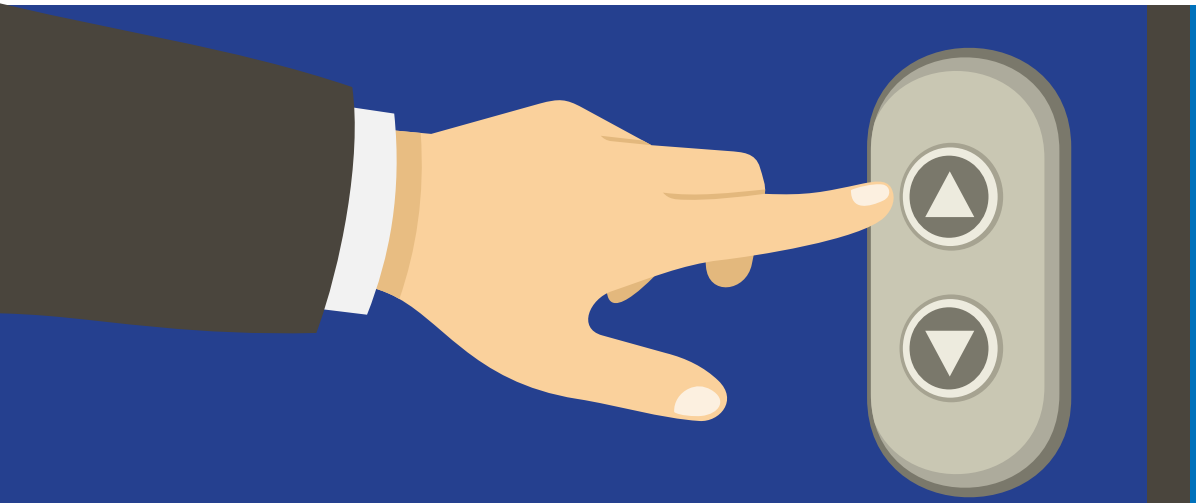


Figure 15 : PE Exit Route between CY15 and CY20[13]



12. KPMG analysis of c. 300 exit transactions
13. KPMG analysis of c. 500 exit transactions



Exit planning starts right from the date the investment is made in the portfolio company

As market dynamics impact return on investments, investors need to be cautious when reviewing targets and have a clear exit strategy in mind, even prior to signing the deal.

Exit planning structures the timeline for pursuing value enhancing activities, improving performance and exiting with good returns (MOIC or IRR). A poorly planned exit can turn an otherwise good deal into an average one.

Besides creating a compelling story around revenue growth, market reach and profitability, exit planning should also focus on strengthening the quality of management team and creating a transparent track record.

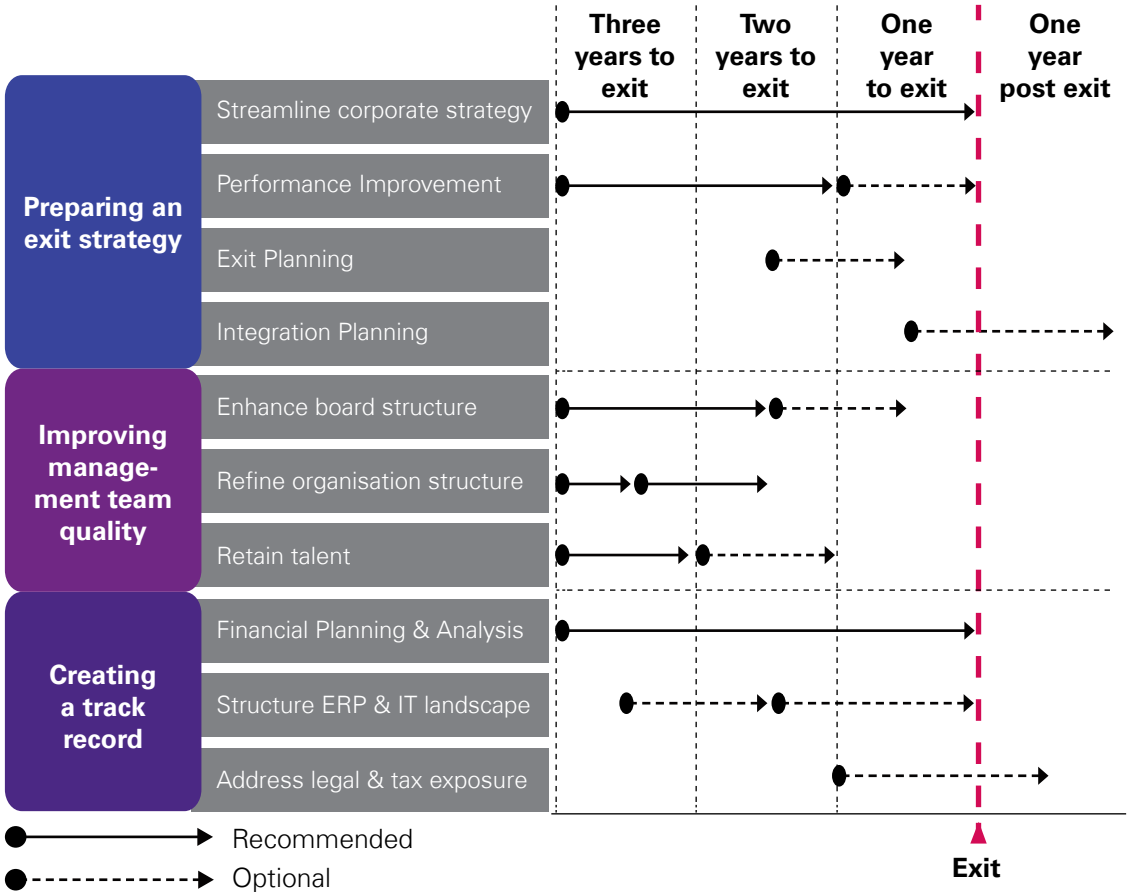
An investor's ability to achieve timely and profitable exits across multiple investments is a key indicator of its quality of initiatives and efforts to enhance value.

As per our internal study, exit strategies can be formulated three years in advance from the tentative quarter of the planned exit. Streamlining corporate strategy, financial analytics are typically the first initiatives to be implemented, followed by performance improvements, refining organisation structure and other initiatives.

Exercises around planning the exit and enhancing board structures are initiated 12-18 months prior to the targeted exit quarter.

In our experience, we have observed the following activities and considerations incorporated by PEs / VCs in their exit planning.

Figure 16: Best practices in exit planning



Exit planning

A timebound exit requires a clear strategy, alignment and cooperation of the portfolio management

A clear exit strategy – Executing a good exit begins much earlier than the actual sale and attempts to establish a sound deal rationale. The strategy must include the guiding principles for exit and detail the key milestones and roadmap of activities till actual exit.

Get the timing right – This is critical and often dependent on macroeconomic factors and overall market outlook. Unforeseen events such as COVID-19, weak consumer sentiments and choppy near term forecasts, especially in price sensitive sectors like automotive, auto components or real estate, may adversely impact valuations, resulting in postponing the exit.

If the exit is delayed or the return multiple do not fall within the predefined threshold, PEs need to develop a Plan B.

Whilst the median holding period of PE investments have declined globally between CY15 - CY19, in India they have had to adopt a 'wait and watch' approach during this period.

On the portfolio management side - the skills, capabilities and experience that directors and senior management teams bring to the table can be of immense value to vendors and incoming buyers. The succession plans that they have for the portfolio company are often important buyside deal considerations. Some themes that PEs need to keep in mind while deciding the quality of management teams required are:

Selecting the right buyer – Identifying the right buyer, i.e., a strategic buyer, financial investor or exit through Initial Public Offering (IPO), helps in tailoring the sell- side story to fit the investor's needs and highlighting the key achievements and milestones. For example – a strategic buyer would be more interested in operational metrics and integration challenges while a PE would be more interested in financial metrics. This also has implications on selecting the right deal-type for the exit.

Figure 15: PE Exit Route between CY15 and CY20 shows that Open Market transactions followed by M&A have remained the most preferable exit routes for PEs in Indian, both in terms of aggregate deal value and deal volume.

Orienting the management – identify program leader for the exit planning to ensure clear and consistent messaging throughout the exit process. Management teams also need to be sensitised on do's and don'ts, impact of information shared on valuation, risk of value erosion due to a poorly managed process and the benefits of proactive communication to stakeholders.

Ensure management bandwidth is not choked – Management team's bandwidth is usually consumed in maintaining business as usual. Managing multiple projects simultaneously, such as exit planning and running operations, requires intense focus and efforts, lest one suffers at the cost of the other.

In such scenarios, setting priorities and striking a balance between the two during the exit process becomes crucial.

Build a due diligence proof business case – As part of the exit strategy, PE firms should also develop a compelling business case, showcasing historical accomplishments, robust business plan and well documented assumptions.

The process also involves identifying operational blind spots that can be fixed and creating a convincing sell- side story. Performing an exit readiness assessment 1 year prior to the actual exit can help identify weaknesses and aid adequate planning.

Execute the entire exit process in a timebound manner – The entire exit planning and execution process could easily last from one to three years depending on the size and complexity of the deal and the type of buyer involved. In this context, operating groups of PE firms need to have the necessary bandwidth to support the sell-side management teams in the exit process. Further, legal and regulatory requirements especially in cross-border transactions can impact the overall duration of this process.

Normally, a sale to another PE investor should take less time to complete compared to a strategic buyer.

Pro-tip

- Have a dry-run of buy-side due diligence 12-18 months before the tentative exit.

Glossary

AI	Artificial Intelligence
b	billions
B2B	business to business
B2C	business to consumer
BCP	business continuity plan
NFSI	banking, Financial Services and Insurance
BSE	Bombay Stock Exchange
c.	Close to
CAGR	Compounded Annual growth rate
CIO	Chief Information Officer
CM	Consumer markets
CRM	Customer Relationship Management
CSR	Corporate Social Responsibility
CY	Calendar year
DoA	Delegation of authority
DRP	Disaster recovery plan
EBITDA	Earnings before interest tax depreciation and amortisation
EM	Emerging markets
ERP	Enterprise Resource Planning
EU	European Union

FMCG	Fast moving consumer goods
FS	Financial services
GDP	Gross domestic product
GDPR	General Data Protection Regulation
GoI	Government of India
GPS	Global positioning system
GST	Goods and Services tax
GTM	Go to market
H1	1st half year
HR	Human resources
IBC	Insolvency and bankruptcy code
IBP	Integrated business plan
INR	Indian rupee
IoT	Internet of things
IPO	Initial Public offer
IRR	Internal rate of return
IT	Information technology
ITeS	Information technology enabling services
KMP	Key management personnel
KPI	Key Performance Indicators

L&D	Learning and development
LP	Limited Partners
M	millions
M&A	Mergers and Acquisition
MIS	Management Information systems
ML	Machine Learning
MOIC	Multiple on Invested Capital
MOSI	Ministry of Statistics and Programmed Implementation
NBFC	Non-banking Financial companies
NIST	National Institute of Standards and Technology
NPA	Nonperforming asset
O2C	Order to Cash
P2P	Procure to Pay
PDPB	Personal data protection bill
PE	Private Equity
RFID	Radio frequency identification
RoI	Return on Investment
RPA	Robotic Process Automation
SANS	System admin, Audit, Network and Security.
SAP	Systems Applications and Products

SCM	Supply Chain Management
SKU	Stock keeping unit
SoD	Segregation of duties
SOP	Standard operating procedures
T	trillions
T&C	Terms and Conditions
TAT	Turnaround time
TMO	Transition management office
TSA	Transition services agreement
USD	US Dollars
VAPT	Vulnerability and Penetration testing
VC	Venture Capital
YTD	Year to date

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