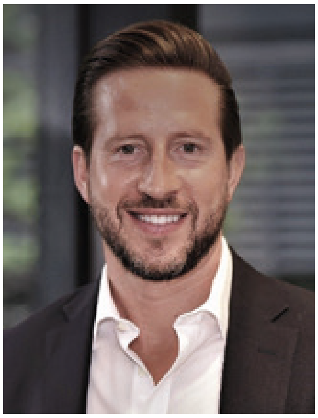
KEYNOTE INTERVIEW

Catching the exit wave: Are CFOs ready?



CFOs are at the core of maximising value on exit – but a lack of exit experience could be a cause of concern for private equity investors, say Chris Donovan of Deloitte UK and Emma Cox of Deloitte Global

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Q Deloitte recently published a report on the role of private equity portfolio company chief financial officers in maximising value on exit. Why did you choose to research this particular topic?
Chris Donovan: One of the big concerns in the market right now is the huge wave of exits that needs to take place. Limited partners are focused on returns, and distributed to paid-in capital has been suffering because many exits have not been completed over the last two years. That wave of exits needs to happen, and yet there are still macro challenges – particularly market volatility and corresponding higher buyer scrutiny – that mean the bar is much higher for a successful exit. CFOs and finance teams take most of the impact, as they typically run the majority of the process, so we sought to find out whether CFOs are really ready for this wave.

Emma Cox: The goal was to get a broad spectrum of perspectives on that question. We interviewed more than 200 people to understand how ready CFOs are for exits and what they believe is important in that process. We then compared that to the views of PE investors.

Q Why is the CFO's role so important in an exit?
EC: Ultimately, the success of an exit process is about valuation and the value that the PE firm will get from selling the business. That is underpinned by numbers, so the CFO is very important in being able to talk credibly about the financial performance of the business and the future equity story.

The CFO is the guardian of the numbers and therefore plays a core role in the exit process. In the survey, we asked about the extent to which a good CFO can positively impact the value realised on exit, and the result was surprising: one third of respondents said the positive impact of the CFO could be as high as 20 percent or more of the value realised on exit. A further half suggested the uplift could be between 5 percent and 20 percent.

The reverse is also true: a poor CFO can destroy value or even break a deal. So, it is not just about finding a really good CFO – a number of PE investors have been burned by having a poor CFO who inhibited exit potential.

Q Where can it go wrong for a CFO, and what are the key attributes to achieving success in the role?

CD: An interesting statistic to start with is that three-quarters of PE investor respondents said they regularly replace the CFO in their portfolio companies – so the job is clearly a tough one to keep.

In the current environment, given volatility and uncertainty, CFOs are having to front a lot of the challenges associated with delivering business performance. The demands placed on them can be significant and perhaps not always fully appreciated.

When CFOs are facing an exit process at the same time as their day-to-day role, there is a real risk that they get distracted from the deal by conflicting demands – or, vice versa, being distracted by the deal to the detriment of delivering the business plan. Taking their eyes off the ball on either could prove costly in terms of erosion of value or, more fatally, the end of a deal.

Some of the key attributes that CFOs need to deliver a successful exit include an ability to articulate the equity story and to represent the business and its future growth path to buyers. Further, the relationship between the CFO and the CEO is critical: internally, the CFO should provide a healthy challenge to the CEO to help ensure a balanced, supportable view is presented externally to bidders. Externally, being aligned in public to come across as a compelling, backable team is key.

EC: Where it can go wrong for the CFO is their lack of experience in doing these deals. Our survey found that only half of the CFOs interviewed had experienced more than one exit during their career. A further third had no experience. Additionally, given current market conditions, those that do have exit experience probably haven't done a deal for three or four years, so that experience is now out of date.

A consistent theme from respondents was around CFOs recognising that developing a robust finance team is a crucial component. An experienced CFO will adapt their finance team's skill sets to respond to a new environment. They should also prioritise team morale and cohesion to help navigate the added pressures of the exit process.

> *"34 percent of CFOs interviewed said they received insufficient or no support from their PE investors in preparing for exit"*
>
> **EMMA COX**

Q How can PE firms support their portco CFOs to maximise the chances of a successful exit?

CD: Having an exit mentality from day one is important for every CFO. They are not necessarily expected to have a detailed plan, but the way they shape the finance function and determine the right KPIs for the business can be important, so they shouldn't just start to think about the exit six months before a deal process. The PE investor can help with embedding this mindset.

Portfolio companies should prioritise enhancing the finance function from an early stage. That means having the right systems and capabilities to track KPIs and proactively provide data to the broader business to drive value creation. Given strong data is disproportionately important for successful exits, PE firms should prioritise that investment from the start of the hold period.

EC: Something else that became clear in the survey was that CFOs want more support around exits, with 34 percent saying they receive insufficient or no support from their PE investors in preparing for exit. Often, PE houses assume CFOs and finance teams know what they need to do to run an exit, but when it comes to actual transaction management and readiness, investors need to lean in more.

Probably two years out, the PE firm should be making sure CFOs understand the process and have sufficient resources to run the deal while continuing to run the business. They should also make sure the CFO has the equity story confirmed, the KPIs and data to support that story, and the requisite presentation skills, providing mentoring if needed.

Q What piece of advice would you give to your PE clients to support their CFOs in the current environment?

CD: With so much going on for CFOs, my advice is to be wary of underestimating the amount of support and resources needed. Given the significance of these deals, the ultimate return on investment will help justify making those commitments.

EC: It is important to remember that completing a successful exit is not about what you do in the six months leading up to it: it is about building a high-quality finance function that enables you to build value in a way that you can realise. My advice to PE firms would be to invest in your CFOs and your finance functions from day one to help build that exit mentality from the outset. ■

Emma Cox is global PE leader at Deloitte and Chris Donovan is head of portfolio company services and PE exits leader at Deloitte UK

For further insights, explore Deloitte UK's latest report:
The role of PE portfolio CFOs in maximising value on exit.

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