



PRIVATE EQUITY **PERSPECTIVES** PODCAST

EPISODE 15: REFINING STRATEGY AS OPPORTUNITIES EVOLVE

INSIGHTS FROM THE BDO PRIVATE EQUITY PRACTICE

INTRODUCTION

Todd: Hello, and welcome to another episode of BDO's Private Equity Perspectives podcast. I'm Todd Kinney, National Relationship Director with BDO's Private Equity Practice here in New York City. I'm really thrilled to have two guests with me today, and we're going to be talking about the current private equity and investment banking landscapes. First, Justine Mannering, who is the managing director responsible for sector coverage within apparel, accessories, footwear, and the luxury sectors for Stifel's consumer investment banking team. Justine is also a founding member of Exponent Women, which is a networking collective which brings together women dealmakers. Welcome to the show, Justine.

Justine: Thank you.

Todd: Excellent. Next, we're delighted to have Ann Brophy, who's Vice President of Business Development for LLR Partners in Philadelphia. Ann has more than ten years of experience in sales, business development, and relationship management in financial services and private equity, and actually earned her MBA at the University of Michigan's Stephen M. Ross School of Business. I would also like to add that she was a standout ice hockey player at Brown.

Ann: [laughter] Thank you.

Todd: Welcome to the program, Ann.

Ann: Thank you very much.

TOPICS DISCUSSED INCLUDE:

[Introduction](#)

[Introductory Questions](#)

[Technology Outlook](#)

[Value Creation](#)

[Coffee Break with BDO's
Robin Samples and
Alison Torres](#)

[Add-On Acquisitions](#)

[Diversity & Inclusion](#)

INTRODUCTORY QUESTIONS

Todd: All right. So, Ann, why don't we kick things off with you. I think our listeners would be interested in hearing your philosophy for sourcing new investment opportunities for LLR. My understanding is that you really kind of do that by building and maintaining relationships with intermediaries. Care to share?

Ann: Absolutely. Thanks again for having me.

Todd: Of course.

Ann: Yeah. I would call our sourcing efforts at LLR very proactive and very comprehensive. I do manage most of our traditional intermediary relationships, which includes a lot of investment bankers, business brokers, and increasingly spending more time with accountants, like with firms like BDO, with attorneys, lawyers as well as lenders. So, we're trying to do a great job of managing those relationships across our firm. We also have a much larger team focused on sourcing that does more proprietary outreach direct to companies, and we spend a lot of time building out our relationships with executives and potential CEOs and CFOs. So, we try to be very proactive so that we're talking to companies at an earlier stage, even if they're too small. For us, we like to have an engaging relationship with them while they're still growing in case there's opportunity for us to partner either on the growth equity side, or a recap, or a buyout.

Todd: Awesome. Well, I see a lot of BD folks out in the market, and you're certainly one of the best.

Ann: Yeah, thanks.

Todd: So, good to have you. Justine, again as the MD responsible for sector coverage within apparel, accessories, footwear, and the luxury sectors of Stifel, maybe you could tell our listeners about some opportunities and trends that you're finding of interest in the consumer sector, and maybe broadly, investment banking.

Justine: Thanks, Todd, and thank you for having me.

Todd: Of course.

Justine: It's interesting to hear Ann talk about deal sourcing because we continue to see just a really high level of activity across the middle market. Twenty-nineteen started down a little soft compared to 2017 and 2018. Within our business at Stifel, we've actually seen an increase in deal activity, and our 2019 plan is looking extremely strong. But I think on the other side of that, this has been driven by really solid economic fundamentals, but really significant cash resources at both corporates and private

equity groups, which has made for an extremely competitive market and still really a seller's market today. And so, listening to how people are sourcing for deals and having to be creative to really get ahead of that has been a real trend in the last couple of years. I think within consumer we're seeing a bifurcation of the market. There's been a lot of very strong activity and a lot of interest and high valuation multiples. In sectors where there's been innovation and which are really playing into where the consumer's spending. So, for us, that's been food, beauty, wellness, any better-for-you product where we're really seeing a focus from consumers today. And in direct contrast to that, we're seeing some real struggles on the retail and the traditional bricks and mortar side. So, I think it's been very interesting for us just to see how quickly that happened and how the market has changed and been disrupted. And it's been interesting how it's created opportunities for some private equity firms and obviously caused issues for others, and the same within the corporate space: we expect to see that continuing through the year on both sides and working to try and take advantage of both sides of those markets.

TECHNOLOGY OUTLOOK

Todd: Okay. Appreciate it. Makes a lot of sense. Why don't we pivot to the outlook for technology? Ann, maybe you could share some details on LLR's tech and services focus, and then we'll let Justine weigh in with her thoughts on the evolution of tech after you.

Ann: Yeah. Absolutely. So LLR's been around and investing for 20 years. We are on our fifth fund, when the firm started we were very focused on investing and partnering with businesses in the mid-Atlantic region and primarily in and around Philadelphia. And so, I want to—we were generalists, but that opened us up to a lot of different industries and business models. As our firm has kind of progressed and grown, we've really narrowed our focus on areas where we have a lot of experience, expertise, and areas where we think we can be a unique or differentiated buyer. So, we have really homed in on technology and tech-enabled services from a business model perspective, and then we cover a variety of industries, including healthcare and education, fintech, B2B software, industrial tech, and security. We're covering a lot of that in markets, but we're, as I said, kind of spending time where we think we can bring something different to the table whether that's an executive or a lot of deal experience in a particular end-market. So, we look at a lot of business models that have very high growth, high gross margin, and are growing quickly.

Todd: Yeah. Justine?

Justine: It's so interesting listening to Ann talk about technology. When I started in consumer, we had a very distinct delineation between the consumer sector and our technology practice,

and today it's very hard to do that. It's almost impossible to distinguish technology from a brand, from a channel. We're very focused on trying to merge those practices. And so, across the Stifel platform, we see technology impacting every single sector and we try and work together now to really make sure that we can address the markets in the best possible way. And I think we'll continue to see that where particularly in consumer, you've got to be where the consumer is and the consumer is online, they're in stores, and they're using technology in ways that we would never have dreamed about before. Increasingly, we're just seeing this huge focus on trying to invest behind that and building infrastructure as well.

VALUE CREATION

Todd: Makes a lot of sense. Appreciate both your insights. Let's move to our next topic. Clearly, both of your firms are committed to long-term value creation. Ann, I'll go to you first and then Justine. What are currently the biggest challenges and opportunities, would you say?

Ann: Yeah. I mean, people and talent are a huge part of this business. At LLR we've made a strong effort over the last few years to build out an internal value creation team. Three of those people are dedicated to human capital management. We've built out some proprietary database of relationships and executives, and people that we can leverage and learn from when we need help with our portfolio companies, whether it's during diligence of an opportunity or post-close. We might go into partnering with the business, and sales and marketing is a big area for them so we can leverage that value creation team to help us find a new head of sales or a position like that. So that's been a big differentiator for us when we're meeting with portfolio companies, that we have that breadth and depth of resources internally. So, that's been, I guess, a challenge that we're trying to address and building a team around so that we can be more helpful and a better partner to the companies that we're working with.

Todd: Justine, what do you think?

Justine: We committed a little differently because we're really looking at how to create long-term value for our clients. I think for us we've seen a huge opportunity in the middle market particularly, and we've invested very heavily over the last 5 to 10 years to broaden our services. So, today Stifel is a full-service investment bank offering bulge bracket services to growth and middle market companies which is unmatched in the market today. We offer everything from ECM, DCM, M&A. We can help on SPACs [special purpose acquisition companies], we can help on 44As. We'll lend of our balance sheet. We really have tried to make sure that we can offer any service to our clients at any stage in their life cycle, and in that way, we've been able to really focus

on long-term relationships rather than single transactional events, and both value for our clients and to be honest for our firm as well. And I completely agree with Ann, really the challenge for us has been people and talent. We've been lucky to attract some really, really, high-quality talent in the last couple of years, but as always, that's always the focus on trying to expand and broaden our talent pool and depth of expertise.

COFFEE BREAK WITH BDO'S ROBIN SAMPLES AND ALISON TORRES

Todd: Nice. Well, it's good for our listeners to get the perspective from both the banking and investor side, so appreciate that. Now we're going to shift gears briefly for our Coffee Break with Robin Samples who is a Managing Director in BDO's Transaction Advisory Services Practice. Robin's based in Atlanta. And Alison Torres, Tax Principal with BDO's Transaction Advisory Services Practice, and Alison's based in the greater Washington, D.C., area. Robin has provided buy-side and sell-side due diligence to PE and strategic clients in transactions ranging from \$10 million up to \$1 billion. Alison leads domestic and cross-border tax due diligence, structuring, and other transaction-related advisory services for both PE and corporate clients. Let's hear now from Alison and Robin.

Alison: Hi everyone. I'm Alison Torres, and I lead the Tax side of our Atlantic Region Transaction Advisory Services Practice. Thanks so much for having me. I have to say I really appreciated hearing Ann and Justine's insights and agree that we're definitely seeing technology used in ways we would have never dreamed about before. One such convergence we're seeing play out is in the healthcare industry. Deals like the Amazon PillPack acquisition for \$1 billion, Best Buy's acquisition of GreatCall for \$800 million, and BioTelemetry's acquisition of Geneva Healthcare for \$65 million. Robin, I know that here at BDO we have a dedicated multiservice line Healthcare Center of Excellence and deep healthcare industry experience within our Transaction Advisory Practice, but what are you seeing in the South from a Q of E perspective when it comes to the convergence of technology and healthcare?

Robin: Thanks, Alison. I lead our Transaction Advisory Services Practice in Atlanta and focus on financial due diligence across industries. I've seen the PE deal flow in the healthcare sector has increased since 2009, reaching a 10-year high in 2018, with 590 deals completed, at a total value of \$88 billion. U.S. healthcare M&A has also boomed, reaching a 10-year value peak of \$171 billion in 2018. In the last 12 months or so, I'm seeing private equity firms focusing more on healthcare technology companies than on healthcare companies themselves. Additionally, I work with some healthcare companies in the Southeast that have also started to look into acquiring these very profitable technology

companies, as opposed to outsourcing. One of the most interesting challenges from a Quality of Earnings perspective for these types of deals centers around revenue recognition under the new accounting standard ASC 606. This standard provides guidance on when revenue and certain related expenses are recognized under contracts with customers. And the majority of these technology companies have extended contracts. For buyers under this standard, it's important to analyze and understand the revenue recognition and the timing of the associated cash flow as part of their negotiations.

Alison: Robin, tech and tech-enabled services raise a number of tax due diligence issues, as well. Even before the Wayfair Supreme Court decision last summer, some state and local governments were subjecting tech services to sales taxes, which has historically been thought to apply only to the sales tangible personal property. Now after Wayfair, companies can be on the hook for sales taxes on services in states in which they don't even have any business operations, when they have a minimum number of sales to the state, for example, \$100,000 or 200 transactions. What complicates the issue even more, is each state and local jurisdiction has their own rules on which services are taxable and at what rate. So, keeping track of what is subject to sales tax and at what rate is a significant administrative undertaking that most middle-market companies just don't have the internal resources to keep up on. As a result, we're seeing significant sales tax exposures being discovered during the tax due diligence.

Robin: We are clearly seeing some tax and accounting complexities arising in this emerging industry. But for now, I think we're out of time. Thanks, everyone. Now back to Todd Kinney at BDO in New York.

ADD-ON ACQUISITIONS

Todd: Very compelling. Appreciate those perspectives from both Robin and Alison. And now back to our conversation with Justine Mannerling and Ann Brophy.

Pivoting to another issue, let's talk about add-ons. According to PitchBook, the median size of an add-on deal in North America and Europe has nearly doubled over the course of really the last two years. I think in 2016 the median size was about \$41 million and that's really snowballed in the last year to about \$76 million, which is really about an 85 to 86 percent increase. This is based on PitchBook's Q1 M&A report. So, Justine, I'll throw this out to you, has your firm noticed an uptick in PE firms seeking to grow portfolios via add-ons? Then Ann can chime in afterwards with her perspective.

Justine: Yeah, Todd. It's been a really interesting evolution from our point of view. Historically, we always thought of add-ons as really a way for corporates to add value to their portfolios and that

was typically buying the private equity owned assets as add-ons. But as we've seen just a lot of cash coming into the market, a lot of liquidity, and competition increasing alongside valuations, we've seen a number of our private equity clients looking at more creative ways to deploy money. And in many cases, they can't be as competitive on the larger platform deals. But what they can often do is create a significant amount of value by buying a smaller asset and then doing a full buy and build strategy where they can benefit not only from margin arbitrage but also a lot of operational synergies. And really being able to invest in professionalizing smaller businesses and taking advantage of that. So, while we see valuations are continuing to impact this, we expect that to continue. Interestingly, we've seen corporates pull back a little as valuations in some sectors have come off and they've really refocused in some cases on returning capital to shareholders. But certainly, the private equity interest in add-ons and building companies through acquisition continues to be very strong.

Todd: Right. Ann, care to add anything on the add-on topic?

Ann: Yeah. I mean I would totally agree with everything Justine just said. Add-on acquisition strategy's a big part of the growth of our portfolio companies. In 2018, we did 10 platform investments and about 30 add-ons. This year so far, we've done three platforms and five add-ons. So, the balance of add-on versus platform is always weighing more towards add-on acquisitions. As Justine said, there's a ton of capital and cash chasing a smaller number of deals and there's a lot of competition for investment opportunities. So, we have a few different executive-led initiatives that we've done. And I know all firms do this as well, but we've tried to pick areas that we see a lot of opportunity. We spend a year or so picking the partner and the CEO or executive that we'd like to work with and then we spend time building out a pipeline and acquiring those. So, we're doing one in the ophthalmology space. We've got one in the payment processing space. And we have one in industrial tech, as well. It's again a way for us to bring something, some sort of angle or advantage to a company. It allows us to invest in smaller companies by building them up as part of a platform and ideally, it's not a huge process when we're talking with smaller companies. There's less competition and you can usually invest at a lower valuation. That will continue to be a strategy of ours going forward.

DIVERSITY & INCLUSION

Todd: I would imagine so. Excellent. Well, besides PE and deal activity since I'm lucky enough to have two very successful lady dealmakers here, I want to cover another important topic in the financial industry which is diversity. A couple stats here. Research by Preqin found that the percentage of women working in the PE industry is 18 percent and the percentage of

women employed by hedge fund managers is only 19 percent. Meanwhile, another study showed that funds with gender-balanced investment teams generate 10-to-20 percent higher than those with a majority of male or female leaders. And that study was by International Finance Corp., RockCreek and Oliver Wyman. I guess Justine I'll go to you first and then Ann, please add your comments. How do you think kind of both the PE and investment banking industry dynamics for women have changed over the years?

Justine: Sure. I think working in investment banking as a woman today is certainly significantly easier than it was in the past. I think firms have started to really take note of the benefits of having a different voice at the table, of having more diversity, not only for their clients but also for internal purposes, for culture and really being able to drive the way that decisions are made and firms are run. Certainly, at Stifel, we have a real focus on not only attracting women to our platform but I think even more importantly than that is being able to create an environment where they feel like they can succeed and they're part of the culture. I think over the last 5 or 10 years we've seen a real drive to hiring women and not always as much focus on being able to create an environment for them to feel like they want to stay and they can succeed. And I think that is changing quickly and I think as more women reach more senior levels and have a voice at senior management levels and are able to influence culture and programs internally, we're seeing them step up and really helping the next generation of women coming through. And I'm certainly positive that it's moving in the right direction. We still have a long way to go both across both investment banking and private equity. But I think increasingly it will become easier and we'll see that balance change.

Todd: Ann, would love your thoughts.

Ann: Yeah, no, I think private equity, investment banking, and finance, in general, is becoming a better place for women. I think every year it's getting increasingly better. I think policies are better internally. There's more maternity leave options. There's more organizations for women. Exponent is a good example that Justine's a founding member of. There are just more events and organizations available to women so that you can create more relationships, find mentors, and just help your overall success. At LLR, we have a Director of HR, People and Culture. That was a hire for us in the last year which has been great. I think you're seeing a lot of private equity firms and middle-market firms become professionalized in that way. We are unique in that I think about 23 percent of our team, our 60-person team, is female so we're nicely above the percentage for the industry but still, have a long way to go. So, that's a big focus for us. I think it's important as Justine said to be hiring more women—to attract them to want to work there but also then to retain them and make them want

to stay and have a path to success. I think you'll also see a lot of PE firms wanting to have more women to attract talent but also you're seeing more LPs and investors want to see that the firms that they're investing in, funds they're investing in, are hiring women and also investing in women-led businesses and more diversely founded businesses. So, hopefully that continues.

Todd: Well, we're actually recording this on the heels – we just finished our Annual Women Deal Makers Breakfast here at BDO in our boardroom in New York this morning and we had about 50 women with a mix of investors, bankers, lenders, lawyers, and a lot of seasoned C-level execs. So, couldn't agree with both of you more. We're doing everything we can from the BDO side of the world. How about we'll take on the last topic and Ann, I'll let you go first this time. Do you have any professional advice for women that are seeking to follow in your career footsteps?

Ann: Yeah, I mean I was lucky to have a couple women in the industry that have been mentors to me throughout my career so that's always important. If you can find and build relationship with someone who's maybe a bit more senior than you so that you have someone to help guide you and lean on when you have questions or are looking for opportunities and tap into someone that has a larger network. And I think just showing up at events and being top of mind with people goes a long way especially until this industry is more diverse. You are often one of the few women in the room so that goes a long way just showing up and being present. So yeah, but I would say that the biggest influence for me was having a strong mentor.

Todd: Yep, excellent. Justine, what do you think?

Justine: Yeah. I agree. Looking back, I've been extremely lucky to have both men and women as mentors throughout my career. I think even more importantly certainly my career has been having sponsors within the firms that I've worked at. I've been very lucky to have people who have really pushed me to succeed internally and then help me to achieve my goals. I think if I was advising anyone coming to this career today, I think what is really important you do have to show up. You do have to work hard. But really importantly, you need to network both internally and externally. I think the internal networking is important because you do need sponsors and you do need mentors internally to be able to work your way through what is a fairly complicated culture at most investment banks and it's important to have that support. I think externally networking with other women both senior and junior is really important from a support point of view. It's been invaluable for me in terms of both deal sourcing but also from a personal point of view just knowing that I have a group of women we refer to as our tribe who are always there to be supportive, who are always there to offer advice and really understand what

we're going through has been really vital to being able to both stay in this industry and succeed in this industry.

Todd: Awesome. I appreciate that—the passion comes through in the answers to the last couple topics. I really appreciate that and I think we all met each other through networking at different events.

Ann: Yeah.

Todd: So, that's fantastic. Well, at this point, we're going to wrap. But I can't thank you enough—Justine Mannering with

Stifel and Ann Brophy with LLR Partners, you're both very good relationships and very important to BDO. I know you're both very busy so thanks for taking time out of your busy schedules to join us today.

Ann: Thanks for having us.

Justine: Thanks for having us.

Todd: To our listeners, thanks so much for tuning in. If you haven't already, we'd love for you to subscribe, rate, and leave a review of the show on iTunes. Until next time, this is BDO's Private Equity PERSpectives.

If you enjoyed the show, please visit [iTunes](#) to subscribe, rate, and leave a review. Join us next time for another edition of Private Equity PERSpectives, and listen to the full series [here](#).

People who know Private Equity, know BDO.

CONTACT:

SCOTT HENDON

Private Equity Practice Leader
214-665-0750 / shendon@bdo.com

TODD KINNEY

Director, Private Equity Industry
212-885-7485 / tkinney@bdo.com

BDO PRIVATE EQUITY PRACTICE

Strategically focused and remarkably responsive, the experienced, multidisciplinary partners and directors of BDO's Private Equity practice provide value-added assurance, tax, and advisory services for all aspects of a fund's cycle, wherever private equity firms are investing.

ABOUT BDO USA

BDO is the brand name for BDO USA, LLP, a U.S. professional services firm providing assurance, tax, and advisory services to a wide range of publicly traded and privately held companies. For more than 100 years, BDO has provided quality service through the active involvement of experienced and committed professionals. The firm serves clients through more than 60 offices and over 650 independent alliance firm locations nationwide. As an independent Member Firm of BDO International Limited, BDO serves multi-national clients through a global network of more than 80,000 people working out of nearly 1,600 offices across 162 countries and territories.

BDO USA, LLP, a Delaware limited liability partnership, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms. BDO is the brand name for the BDO network and for each of the BDO Member Firms. For more information please visit: www.bdo.com.

Material discussed is meant to provide general information and should not be acted on without professional advice tailored to your needs.