KEYNOTE INTERVIEW

Making the most of tech vendor relationships

PE firms should collaborate with their tech service providers to enhance their value creation opportunities, says John Pushparaj, chief growth officer at Persistent Systems

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Q How can technology-driven strategies be aligned with the overall business objectives of private equity-owned portfolio companies to maximise enterprise value?

Harnessing the power of innovative technology is an urgent imperative for private equity firms that are refocusing their operating models and embracing digital transformation. When PE firms go with a buy-and-build strategy, they often result in a lot of outdated systems with legacy stacks. This means that they need to look at the technologies that are underperforming and modernise them to ensure they are fit for purpose and drivers of profitability.

When you are working with a lot of legacy technology, a considerable amount of investment is needed to maintain the status quo before you can even consider developing innovative processes. Many tools that can automate routine tasks are available on the market, allowing for more resources to be dedicated to making investments that unlock value. The key is to automate what you can to allow your technology stack to drive value across multiple levers, building top-line growth and maximising capital efficiency.

Q With subpar top-line growth, which areas can PE firms look to for optimising cost and enhancing EBITDA?

Certain teams, such as the support teams on declining legacy products or the IT team, are needed for business continuity, but they do not generate any top-line growth. If PE firms can reduce the costs associated with these functions, they can help improve EBITDA and enterprise value for the business.

Customer support systems can streamline these processes and help a business manage its existing customer base, for example. Customer churn is a huge cost to any business, so it is imperative that a good retention plan is in place to ensure customers are mined with quality services.

Even if the macroeconomic backdrop is challenging and top-line growth is muted, these are areas where PE firms can unlock value.

Q How do you balance short-term cost implications with long-term value creation?

Any time there is a requirement for technology remediation or updating the stack, a private equity firm looks at capital investment. As such, they need to look at the ROI on these investments. Based on that, and keeping in mind the broader strategic business plan, a decision can be made to prioritise investments.

There are multiple ways to optimise that spend, such as going through some disruption over a six-to-12-month period to extract value. Short-term wins can include the optimisation of specific areas, so management needs to look at fees and exit strategies and then execute on the relevant value-creation levers across talent, systems and technologies.

Such an approach also builds some flexibility into the process if the hold period changes, because then there will be additional means to extract value.

Q How can PE firms structure their partnerships with technology service vendors to maximise collaboration and ensure long-term value creation?

Most portfolio companies will focus on their areas of expertise rather than expanding into new areas. Their strengths may lie in their product engineering, salesforce or data analytics teams, but few companies are likely to be strong across the board. As such, it makes sense for them to get help from a technology service vendor that excels in the areas they wish to target.

For example, certain technology service providers are best-in-class when upgrading customer support models using chatbots and 24-hour follow-the-sun models. Smaller portfolio companies, therefore, do not need to invest so much in these areas and can instead partner with an established vendor to achieve their goals much faster.

If a specific operational area needs greater focus, a PE owner can help a management team to prioritise. It may be that non-core areas are addressed by a service provider so that the business remains focused on the core business issues.

Rather than working with multiple partners, it is best to choose two or three vendors and have those partners get some skin in the game, working with the company to push for long-term success. Those partners can then keep the portfolio company's strategy and roadmap in mind and develop customised solutions, rather than taking a cookie-cutter approach. It is much better to build that kind of relationship with a few strategic partners than to work at a superficial level with 30 vendors.

Q How can technology service vendors be utilised as a source of innovation, helping portfolio companies to stay ahead of technological trends and disruptions?

Many private equity firms are exploring the advantages of generative artificial intelligence and large language models. They are likely to have a lot of in-house material about these technologies, but there is also a lot of innovation among their tech vendors. Therefore, it makes sense for firms to collaborate with vendors and get a clearer picture of what vendors see in other industries.

For example, a PE firm might only focus on two or three sectors, while a technology provider oversees several more. By hosting workshops and sharing insights, PE firms can discover new approaches from other industries that can be adapted to their portfolio, bringing an additional element of diversity of thought.

Since service providers work across multiple segments, geographies and companies, they can bring that knowledge to bear and be a valuable source of innovative thinking that private equity firms should take advantage of.

Q How does tech value creation influence exit strategies for PE firms, and what role should technology service vendors play in maximising the exit value of portfolio companies?

Private equity firms should review the technology stack when it is time to exit the business, and technology service vendors can help a lot with that. Another key thing to think about is product sustenance. Most of these companies have a customer base and a product out in the market where a lot of engineering effort goes into maintaining the existing customer base without much growth in this product segment, which can mean that innovation stalls and their ability to develop into new areas is hindered. A technology provider can work on product sustenance, freeing up valuable in-house resources for innovation around new features.

Another area to consider is time to market. Rather than hiring people across the world, a company might work with service providers to quickly stand up a team and get its products to market much faster.

There is also the matter of cleaning up balance sheets. A company may have staff in more than 10 countries, raising questions about the potential to rationalise running those sites moving forward. A technology service vendor may be able to consolidate operations to work out of fewer centres, which might make the business more attractive to a buyer. They could also align those locations with where a buyer is present, increasing the enterprise value.

Q What criteria should private equity firms use to prioritise technology investments in their portfolio companies, ensuring that these investments contribute to sustainable value creation?

The question firms must always ask themselves is whether an investment will help to deliver top-line growth and meet bottom-line targets. If it isn't, why get involved with it? Firms should consider making technology investments with a longer-term playbook model to avoid using a hammer to push in a safety pin.

There is also a tendency for firms to favour proprietary technologies, but this often means that they lose sight of what is available for a lower cost off-the-shelf. Firms should be careful not to be drawn into making a substantial investment into something that looks new and flashy but cannot be monetised quickly.

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Q How can PE firms ensure that the cost of engaging technology service vendors is justified by the value they bring in terms of enhancing enterprise value?

First, there must be a clear business case that the vendor can share. The private equity firm should evaluate the proposed offerings and solutions, either in terms of top-line growth or the bottom line. There should be a clear and compelling value proposition.

Secondly, top-line growth is imperative – if a company will double its growth by adopting certain technologies and methodologies, then it is a 'yes'. But while those things might be said up-front, PE firms should ensure vendors put some skin in the game. If they are going to double your sales or halve your costs, they should benefit from that if they deliver.

If your providers become long-term partners, you can expect them to deliver proof of concept and validate their models. Private equity firms can foster effective collaboration between portfolio companies and service providers to fully leverage a provider's expertise. They might try something with one portfolio company and then roll it out to others if it is successful. Such an approach can build credibility and lead to the creation of useful value-creation playbooks, reducing the cost of similar projects in the future. ■